Structural Changes in the Economy of Hong Kong since 1997*

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Abstract

The Asian financial crisis which became evident around 1997, the time of the return of Hong Kong to Chinese sovereignty, challenged the city to maintain its growth trajectory as the global metropolis for Asia. The subsequent severe recession caused a retrenchment in various intermediary sectors of the city’s economy, especially in financial services. Recovery in sectors such as trade and financial services remained below the heady years of growth prior to 1997. Hong Kong has entered a new period of structural change with the increasing shift of back-office jobs to Guangdong province. More sophisticated intermediary service jobs such as those in private equity and hedge funds are growing, but their expansion is obscured for now in aggregate figures because exiting back-office jobs far out-number the new jobs. The city continues to expand as the regional corporate management centre for the world’s leading firms from the most developed economies in Europe, North America, and Asia. Producer services are maintaining their high growth rate, positioning the city as a service provider for Asia. Global

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firms continue to validate Hong Kong as Asia’s leading business centre, positioning it as a partner with London and New York. Hong Kong’s growth benefits from the bonds with its sovereign power, China.

Success Is Challenged

As the 1990s unfolded, Hong Kong soared as the global metropolis for Asia. Its real gross domestic product (GDP) rose at annual rates of 4% to 6%. The strength of its financial sectors, international regional corporate headquarters, global trade, and business services increased at rapid rates, and this success alleviated concerns about the return of Hong Kong to China’s sovereignty on 1 July 1997. At the same time, China had explicitly enshrined its guarantee to preserve Hong Kong as an international financial centre in Article 109 of the Basic Law, the constitution governing Hong Kong under Chinese law and which was approved at the third session of the Seventh National People’s Congress on 4 April 1990. Senior officials of the Chinese government repeated that guarantee time and again, including an explicit statement by Dai Xianglong, Governor of the People’s Bank of China, at the Conference on Financial Integration in Asia and the Role of Hong Kong held on 7 March 1997, just prior to the handover, and they continue to do so right up to the present.

The euphoria of the smooth handover quickly turned to concern, not because of anything China did, but because of events outside Hong Kong and China. Hints of the looming Asian financial crisis appeared in various countries already in 1996 and continued into the following year. During the second half of 1997 countries such as Thailand, Indonesia, the Philippines, and South Korea faced currency crises and bank collapses. Over the next year or so Hong Kong experienced several speculative attacks on its currency, which is pegged to the United States dollar. The Hong Kong Monetary Authority withstood the attacks using various defences, including buying in the securities markets. This was funded by its huge foreign currency reserves; at the time they were the third largest in the world. Nevertheless, with economic distress sweeping across Asia, the heady growth of Hong Kong and its global businesses came to a halt. The real GDP of Hong Kong fell from 1997 to 1998 and then began an erratic, laboured recovery. The pace of GDP growth did not pick up in a sustained way until after 2003.

The economic difficulties of Hong Kong during this period from the