

The Editor's corner

A Plutocracy in trouble

The majority of the Hong Kong people are dissatisfied with the performance of the first Chief Executive of the Hong Kong Special Administrative Region, C.H. Tung. The shipping tycoon was unknown to the public when he was chosen, officially by a local Election Committee, unofficially by Jiang Zemin, to replace the last governor of Hong Kong, Chris Patten.

The succession was bound to be difficult. During five years, Patten, a professional politician, had done his best to stay in the limelight as the last bulwark of Hong Kong's liberties. There was no substance in such a claim, but it did not matter. Hong Kong has always been a place where the bigger the lie, the better. Chris Patten was able in the process to maneuver himself from an ardent supporter of the Tories to a respected friend of Tony Blair, the Labour leader, and from an unknown defeated member of the parliament to an international figure. To follow the Houdini of politics would have been a challenge for anyone. For C.H. Tung, who is not a politician and whose social prominence came from birth, it was bound to be even more difficult.

Then, in the first year of his new job, the Asian crisis struck. It was the start of an economic storm that moved from Asia to the shores of America, and still roams the world. Companies went bankrupt, currencies collapsed and many economic clichés were destroyed.

Today, it is hard to pass a judgment on what would have been the consequences of the change of ownership of Hong Kong - all other things being equal. No one was expecting an economic crisis of the magnitude of the 1930's crash.

That interesting question can no longer be addressed, and it deprives every analyst of an important point of reference. If the economies of Asia and the rest of the world had been performing as they were in the 1980's and until 1996, Hong Kong would have had no objective reason to face the present unprecedented crisis engulfing the city, if, as proclaimed by the British, it was a well-managed city. But if a crisis had ensued in an idyllic economic

environment, then it would have been quite legitimate to conclude that the change of sovereignty had done no good to Hong Kong.

As it is, we are left with no indication as to the validity of either claim. Hong Kong, since 1998, has to face a far from idyllic economic environment, although it could be argued that China, its main engine of economic growth, has performed at its usual best.

Yet, on closer analysis, there are strong indications that, more than the external environment, the former colonial system that was supposed to be the best protection against an unknown future, has in fact a large responsibility in the current crisis and proves to be the biggest impediment to a return to prosperity and progress.

The British were the founders of Hong Kong, an artificial city whose history is only 150 years old. Because the British had proclaimed the enemy to be China, every one was expecting a battle between countries, between political systems, between economic systems. It did not happen. China was moving so rapidly into the XXIst century, that the most practiced power-diviners faltered badly. Hong Kong became a Chinese city without realizing it was one, while the Central government started to consider it pretty much the way it looks at its neighbours, Guangzhou and Shenzhen.

What is happening was probably inevitable. A great shifting of power was taking place, and as Malcom Muggeridge, the British writer, said, when power shifts, men shift with it. The ensuing commotion always has a price. Hong Kong, a city of excesses, could only make it more expensive than really necessary. It is in a way its trademark.

The shift has yet to be concluded. It is a classic battle for political influence and political representation. As we shall see, it is a complex battle with many parties involved, one that requires skills, one where the only purpose is not the good of the city or the people, but power, the everlasting pursuit of man.

The perception conveyed by the local media and many observers is that C.H. Tung, at the center of it, is a political novice. The common judgment is that he is weak (Chinese like display of authoritarianism) and an ineffectual leader.

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Some, such as Emily Lau, say he is incompetent. This issue looks at those claims.

That C.H. Tung is not “a great communicator”, as Christine Loh, a keen observer of the local scene says, is obvious, but in a restricted democracy, unimportant. Leaving aside the rhetoric and the hyperbole so common in Hong Kong, we found in fact that C.H Tung is following to the letter the precepts of his class, knowingly making decisions that have a political significance with a specific purpose in mind.

That the majority of the people disagree with such a purpose is now clear. But it should not surprise anyone. C.H. Tung is an archconservative and his government, using the argon of political analysis, is at the extreme right of the spectrum. If judged by classic established references, he would be among the hard-core Republicans in the United States, the staunch conservatives in the United Kingdom, the Berlusconi supporters in Italy.

Thus his government is not at best chaotic and at worse incompetent, it is just implementing policies that serve the interest of the plutocracy that is in power. Like in every plutocracy, the government represents a minority.

Any plutocracy with five years of deflation and anaemic economic growth behind it, and contemplating another five years of economic pain, would be in grave danger. Hong Kong is therefore at a turning point of its short history. But whose fault it is and what can be done to change its fate are not questions confined solely to the personality of C.H. Tung. It is a matter for the community to find solutions and to strike an acceptable balance between competing interests.

Compounding the challenge Hong Kong has to tackle is the fact that, whether it wants it or not, it is ageing, and world-cities do not grow old. They die to be reborn. Hong Kong will have to go through the process and actually is going through it, no matter what.

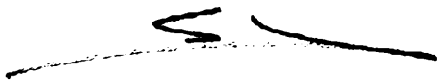
Thus, the American business magazine “Fortune” that already twice announced the demise of the former colony, first in 1997, announcing its imminent death, then again in 2002 when asking who needs it, is not so wrong after all.

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C.H. Tung disagrees. The reader will be able to see how his ideas fit with the reality of Hong Kong and what their real meaning is.

James Tien, the leader of the Liberal party, the political wing of the elite of Hong Kong, Emily Lau, an outspoken critic of C.H. Tung, Albert Chan, a grassroots legislator, Christine Loh, the Head of Civic Exchange and a former legislator, Alan Lung, currently Chairman of the Hong Kong Democratic Foundation and Tsang Yok-sing, the leader of the DAB have agreed to share their views with our readers.

Enjoy your reading

A handwritten signature in black ink, appearing to be 'Serge Berthier', written in a cursive style.

Serge Berthier

CHAPTER 1 - WHAT HONG KONG IS

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HONG KONG, A WORLD-CITY, IS IT?

To quote a bad slogan adopted by the current government, what sort of a city is Hong Kong and what does it mean to be a world-city?

Hong Kong is a city of 6.8 million people, created in the middle of the XIXth century by a foreign power. There had been many such places in the world with the same history. Close to Hong Kong, there is still Macao.

The city is in appearance a rich one. Yet, as we shall see later, it is a relatively poor community by many standards. Nevertheless, it still retains a substantial economic power.

The city is currently going through an economic downturn creating hardship, unemployment and deflation, but we have been reminded a couple of years ago that economic cycles do exist. Therefore, why would Hong Kong be worse off than its neighbors? Why does it have to lose when the others won't? Why all these talks about an "unprecedented" crisis?

Leaving aside financial considerations that we will study further, Hong Kong panics because its elite wants to keep it on its pedestal as the "world-city of Asia".

It is this divergence between aspiration and reality that has given Hong Kong's crisis a spin. Hong Kong is not satisfied being only Hong Kong. It needs to be more than that. C.H. Tung wants Hong Kong to be the London of Asia, the New York of the region.

'This identity embodies the spirit and characteristics of Hong Kong and reflects our competitive edge' he declared in his Policy Address.

This insistence to claim to be more than Hong Kong, as if the rest of Asia, not to mention the world, were unable to recognize what it is, does no good to the city. Isn't it just a naive admission of weakness and the sure sign that the ex-colony has lost its edge forever?

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There are many reasons to think that it is the case. Aside from the economic downturn, which keeps being presented as one of the many ups and downs of Hong Kong but not as a turning point, an historical reason for that is that Hong Kong has indeed been a world-city. Therefore, it will have the same fate as its predecessors.

World-cities have always existed. Notably Fernand Braudel in his book "Civilization and Capitalism" studied their characteristics and their fate in details. What are they then exactly and why do they become world-cities and cease to be so?

According to the French historian Fernand Braudel '*world-economies are autonomous sections of the planet to which their internal links and exchanges give a certain organic unity. The Mediterranean in the sixteenth century was one of them, a world economy, not merely the sea itself but a whole area stimulated by its trading activities, whether near its shores or far away. Its center was Venice, and then it moved to Genoa before going outside the Mediterranean sea (to Antwerp). The economic activities of the whole area ignored the frontiers of empires, in the case of the Mediterranean, whether it was the Spanish one or the Turkish one, or other kingdoms. That is why such sections are labelled as a world-economy. Its characteristic is to bestride the political and cultural frontiers.*' (1)

Thus, world-cities are the center of gravity of a specific world-economy. When such a world-economy evolves, its center of gravity changes.

We can recognize in Fernand Braudel's description many of the attributes of the economic region that had Hong Kong as its center for probably a century. The colony was then truly the only world-city of the South China Sea, with no real concurrent in Asia.

History books recorded enough data to construct a typology of the world-economies at different times of their life. The first observation is that world-economies have clearly defined boundaries that give them their identities and they invariably have a center with an already-dominant type of capitalism.

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Fernand Braudel also observed that *'a profusion of such centers, in a single world economy, represents either immaturity or on the contrary some kind of decline or mutation'*. That the Pearl River Delta bordering Hong Kong today has a profusion of emerging centers, the biggest one being Guangzhou itself, is self-evidence that the world-economy surrounding Hong Kong is changing rapidly.

'In face of pressures both internal and external, he wrote, there may be shifts of the center of gravity: cities with international destinies, world-cities, are in perpetual rivalry with one another and may take each other's place.'

The above observation fits Hong Kong's current predicament very well. While during the second part of the XXth century, it was the unparalleled and unchallenged center of an economy encompassing the South of China whose reach could be felt in most parts of China, it is today challenged in many fields, not only by Shanghai, but other Chinese cities as well.

A further remark is that a world-economy is always a sum of individual economies, some poor, some modest, with a comparatively rich one in the center. As a result, there are inequalities *'which make possible the functioning of the whole. Hence, the international division of labor, not a new division but an ancient and no doubt incurable divide'*. But what happens when such inequalities are eroded? This is precisely this unprecedented question that Hong Kong has to solve to retain its former glory.

Although Fernand Braudel had not included Hong Kong in his list of world-cities when he wrote his masterpiece, the former British colony in the 1980's and 1990's fitted very well along its peers in the above description. Indeed, Hong Kong, being the center of its own world-economy was truly a world-city. But a city cannot be a world-city forever.

THE RULES OF THE WORLD-CITIES

Plentiful historical data from former world-cities uncovered three rules to apply to them. Are they still in force in Hong Kong? We shall see that they are not.

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Rule one is that if the boundaries of a world-economy change slowly, they do change. *'The limits on one world-economy, Fernand Braudel wrote, can be thought of as lying where those of another similar one begin: they mark a line, or rather a zone which it is only worth crossing, economically speaking, in exceptional circumstances.'*

In his 2003 Policy address, C.H. Tung, outlining that the future of Hong Kong lies in the Pearl River Delta, acknowledged such a fact. His declaration was an unmistakable admission that the boundaries of Hong Kong have shifted.

The admission is all the more significant that in 2002, not only didn't he mention it at all, but his own administration was objecting to a critical connection to the Pearl River Delta, a bridge between Lantau (Hong Kong) and Zhuhai and Macao across the estuary of the river. The Secretary for Transport went as far as saying that such a bridge would not be needed before 2020. Less than twelve months later, C.H. Tung stated the reverse, saying it was an urgent necessity (2).

As a general rule, the frontiers of a world-economy have always been quiet zones, *'the scene of little activity'*. It was within the limits imposed by such difficulties that world-economies became established, grew, survived, and developed. For a long period of time, the Hong Kong's economic frontier was the scene of little activity. From the 1950's, to roughly the end of the century, the colony was the last frontier beyond which started a despised economic no man's land: China. Of course, in those days, Shenzhen did not exist and Guangzhou was in the doldrums (3).

The second rule of a world-economy is that it always has an urban center of gravity, a city, as the logistic heart of its activity. News, merchandise, capital, credit, people, instructions, and correspondence all flow in and out of that center.

What better description of Hong Kong could we have? Indeed its vibrant financial center, its modern telecommunication facilities at a time where one Chinese out of one hundred was lucky to have a telephone line, its airport, the only international one within a thousand miles, its deep-water port, the only one of the South China coast, its multinational environment, its banking system and

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stock market, its bilingualism, made it indispensable. In those days, where else would one go anyway? China was still a forgotten country.

Fernand Braudel noted that powerful merchants have invariably controlled world-cities. In the process, they were always becoming extraordinarily wealthy while laying down the law without bothering to assume the direct management of the city. Again here, the description fits very well Hong Kong, whose powerful elite, in the 1970's embodied by Y.K. Pao the shipping magnate, nowadays by Li Ka-shing, never held any official responsibilities in the city, leaving such menial tasks to their underlings.

World-cities are never isolated. They do not function in a vacuum. Generally there are other cities playing the role of associate or accomplice, generally resigned (for a while) to their second-class role. Hong Kong's reach went as far as Taiwan and even Singapore. The activities of those associates were subordinated to those of the metropolis: at the onset they directed the flow of business toward it, redistributed or passed on the goods it sent them, used its credit, benefited from its services and wealth. Later in the process, they invariably tend to adjust to tailor their activities according to the standard of the center.

Such a process is actually the first sign by which a world-city is recognized. Thus the loss of its retinue of assistants and subordinates is a sure sign of change in its status. As it is, Hong Kong has witnessed such a loss which is expressed by the vagueness of the Guangzhou officials and the stern attitude of the Shenzhen municipality (4), when dealing with cross-border issues and planning their future, towards Hong Kong's officials.

Perhaps the most distinctive characteristic of all the world-cities was their pronounced social diversification. They all had a proletariat, a bourgeoisie, and a patriciate, the later controlling all wealth and power and so self confident that it did not need to deal in politics. Eventually the elite and the proletariat grow further apart, as the rich became richer and the poor even poorer.

Nowadays, Hong Kong's poor are increasing as we shall see, and the divide between the rich and the poor has never been so wide. It has political

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implications in the long term that might affect adversely the stability of the city, as was the case with its predecessors on the world stage.

A sure sign of success of the world-cities was their constant high cost of living, their permanent inflation resulting from the intrinsic nature of the higher urban functions whose destiny was to dominate adjacent economies. Notwithstanding, economic life flowed spontaneously towards their high prices.

In the heyday of London, or Amsterdam, Venice, Antwerp to name a few past world-cities, the cost of living sometimes reached an intolerable level, just as New York today is losing its Fortune 500 companies and many other businesses, leaving the city to escape the huge costs of local rates and taxes. And yet, these great urban centers appeal too strongly to interest and imagination not to be heard, as if the people from all walks of life, poor and rich alike hope to grab part of its wealth.

An important lesson coming from historical data is that no world-city has ever been cheap. To be a world-city means to be expensive, as if wealth breeds wealth. And whenever a world-city becomes a cheap place, it is the sign that it has lost its attraction and is therefore no longer what it was. Cities become world-cities not because they are competitive, but because they assume an economic function with unparalleled mastery. Therefore, the prolonged deflation surrounding the economic activities of Hong Kong, while being presented as a positive sign, should be considered as a negative one that underlines its fall.

Why should Hong Kong be over-worried by such a loss of status? It is only a matter of perception, as the lesson of history is that dominant cities do not dominate forever.

Nevertheless, is it the end of the world when it happens? Not all the time although some may suffer more than others. Amsterdam and London have survived very well and if we look at their inhabitants, they are certainly better off today than they were in the heyday of the city, so we should not confuse two issues (5).

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Notwithstanding, when one world-city replaces another, as was the case in about 1929 when New York upstaged London, it is always the sign of a massive historical shift of forces, revealing the precariousness of the previous equilibrium and the strengths of the one replacing it.

In Asia, there is an interesting precedent in China. When in 1421 the Ming rulers left Nanjing for Beijing, the massive world-economy of China turned its back to an economy based on ease of access to seaborne trade to a landlocked trade. Beijing was deep in the interior and started to draw everything towards it. The choice, whether consciously made or not, was decisive. China was turning its back to the world.

The third rule of a world-economy is that there is always a hierarchy of zones within. While the different zones within it face towards the center of gravity, they combine in many ways to form a whole. Once such connections were established, they lasted. The zones circle the center of gravity in concentric circles of activities of unequal exchange.

This inequality has its origin and its genesis. But any alteration of its pattern directly affects its center. Economic forces move like typhoons do. The eye keeps being at the center. A shift of the forces will result in a shift of the center. And today there is no doubt that the breadth and the depth of the economic development in China has definitely alter the previous pattern upon which Hong Kong built up its reputation.

Of course, world-cities may vary in more than one aspect. Historical data provide the clues to their development and their differences. They might be more or less firmly controlled and endowed with variable value of the weapons of domination: shipping, trade, industry, credit, as well as political power. But all share the same history and an identical fate.

COMPETITIVENESS DID NOT MATTER. DOES IT TODAY?

Fernand Braudel's observations, fitting Hong Kong like a glove, have a corollary of importance that has escaped the scrutiny of many economists and also more importantly of the Hong Kong leadership. Competitiveness was not

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what mattered. Why would it matter today? And if it does, what does that mean?

We have already mentioned that the high cost of living in a world-city is not detrimental to its development, but rather an element of it. Competitiveness has no bearing on a world-city.

Of course, some might argue that it is important to be competitive, having in mind the pseudo-theorem of David Ricardo that the relations between two given countries depend on “competitiveness”, expressed as the difference between “comparative costs” obtained in each of them at the point of production.

The basic concept of the argument is that all foreign trades tend towards a mutual balance and can only be profitable to both sides since *‘it binds together, by one common tie of interest and intercourse, the universal society of nations. It is this principle which determines that wine shall be made in France and Portugal, that corn shall be grown in America and Poland, and that hardware and other goods shall be manufactured in England.’* (6)

But the Ricardo theorem leaves aside a core issue that destroys its validity: if comparative costs were the heart of the system, when and why did the division of tasks begin? Indeed nowadays, after so many centuries of trade of all kind, why do poor countries remain poor, and rich ones rich? Why are world-cities invariably expensive and other cities less so?

The truth is that, over time, not a single data is really backing up the claim that comparative advantages are the fundamental rationale to economic intercourse. Nor is there any serious scientific data to backup the claim that the trade has to be mutually beneficial. If anything, the reverse is happening most of the time. As an economist, Ragnar Nurske, seriously said in his book “Problem of Capital”, *‘a poor country is poor because it is poor’*. Why it remains so is still a crucial question left with no proper answer if the debate is confined to pure economic considerations.

Competitiveness was certainly not the reason at the root of Hong Kong’s success. It was rather the lack of competition that let Hong Kong fix the rules

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and rig the game, taking advantage of every event coming its way (such as the embargo against China, the Korean war, the Vietnam war, the open door policy).

If economic competitiveness is not at the origin of a world-city, then it is hard to argue that it mattered at the end of its era. Rather, it is the tide of history that is against the survival of the city in its former status. It is natural evolution that matters most. Orders have always existed in space, and time, each with its own history and its own domain.

Hong Kong today is facing a new future, which does not imply a poorer one but certainly a more modest one. In view of the inevitability of this evolution, what matters today is whether the city is using the wealth accumulated during its glory for the benefits of its citizens or squandering it as if there were no tomorrow. The signs are that it is doing the later rather than the former, because institutions and systems established during its heyday are not willing to disappear easily, if at all.

If competitiveness did not matter in the past, it probably does now. Yet, all the rules that were designed to impede it are for most sectors still in place. Some will object that it can't be. The Heritage Foundation (7) is claiming that the Hong Kong economy is the freest of the world, ranking Singapore as second best.

There is little scientific work backing up such a claim. Like Singapore, Hong Kong is a place where a “free market economy” has lost its meaning entirely. Both cities enjoy a managed economy where cartels and organized oligopolies control the market. The difference is that, in Singapore, the largest owner is the State, while in Hong Kong, it is a small number of people that Fernand Braudel has identified as the merchant elite.

What “free” means for the Heritage Foundation is entirely different from the concept of freedom for the consumers to choose. Free, for this foundation, means the freedom to maximize the return on invested capital. What matters is not the people of Hong Kong, but the investors investing in Hong Kong (or actually through the Hong Kong financial market).

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Indeed Hong Kong is a city where investors enjoy extraordinary privileges. Those were born out of the colonial system, since to attract anyone to the colony, the government had to offer some kind of incentive and a protection. Over time, those privileges became entrenched. The freedom to maximize return is heavily regulated through franchises and licenses. The rule of law is a formidable guardian of the regulation, which is not tailored to favor the community at large but the investors. The beneficiaries of such a system were for a long time the British merchants (the Hongks), not the Chinese coolies. Starting after 1950's, a Chinese elite, mostly coming from Shanghai, started to dislodge the British hongks. Only two of them managed to survive the onslaught. Yet, the system built around them never disappear, as they transferred extensively their privileges to their predators.

That is why Hong Kong does not have anti-monopoly laws. It was deemed unsuitable because, in a colony, monopolies were granted in exchange of services whenever possible. Then monopolies were turned into franchises. Cartels were organized and tightly controlled (8).

'We don't think that a blanket law would be good for Hong Kong, says James Tien, a member of the elite. If we had it, you will have to dismantle the franchises of Hong Kong Electric and China Light and Power. How would you deal with the six oil companies that supply Hong Kong? In fact, I don't think it would improve the economy because large companies are more efficient than small ones. Take the retailer Park and Shop (which, by the way, is part of the Li Ka-shing empire). We receive many complaints against it because its pricing is too low and the small grocers are going out of business. Park and Shop is accused to be too good and too cheap! A blanket anti-monopoly will not result in an improvement. It might in fact result in a loss of efficiency in some cases. When it can be done, it is done and the government is sector by sector dismantling anti-competitive practices. We support this sectarian approach. Telecoms were deregulated and there is a severe competition. It is good for the customer. Other sectors will follow.'

The above arguments are vintage. They have been used all over the world whenever a dominant position was challenged.

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The Hong Kong inhabitants have nevertheless started to realize that something must be wrong with the fact that the flat they buy was built by company A, which runs a bus company that provides transport from the housing estate to an office block that belongs to the same company, which provides a telephone line through one of its subsidiaries, owns the supermarket, provides the power needed for the fridge that came imported through one of its subsidiaries, supplies the equipment and the stationery at your office, and is on the board of the bank which is around the corner.

In its 2002 review about Hong Kong, the World Trade Organization has deplored the lack of progress in this area. *'Hong Kong's reversion to China in 1997 has not altered the territory's trade and investment regime, it said. The absence of a comprehensive policy to address anti-competitive practices and the entrenchment of a few dominant conglomerates in the domestic market, could constitute an obstacle to greater competition from domestic and foreign firms, especially in the provision of services, thereby possibly discouraging foreign direct investment (FDI) in Hong Kong.'*

The government dismissed rapidly the comments, as baseless since FDI (foreign direct investments) reached a record high of US\$64bn in 2001. However most of the FDI are not really invested in Hong Kong but go to China, which in 2002 overtook the United States as the single largest recipient of foreign investments. So the government's objection is misleading and unfortunate (9). Since then, FDI have dropped sharply but the government has refused to reopen the issue. It sticks to the view that, in the domestic economy, there is no relation between investments and competitiveness, having no problem to invert the same proposition when talking about other economies.

When the financial crisis of 1997 hit Asia, the Asean countries seized the opportunity to deregulate further their own domestic market to insulate the economy from the consequences of the collapse of some dominant companies. But the Hong Kong government did not have to deal with the potential collapse of a dominant conglomerate as the balance sheet of the Hong Kong companies remained quite healthy throughout the turmoil. It was so not because they were well managed, or efficient, but because their cash-flow was protected by the peg and therefore they did not have to cope with the massive loss of paper money the Indonesian or Thai companies had to deal with (10).

Although C.H. Tung's government does not want to look at an anti-monopoly law, the integration of the Hong Kong's economy with the Pearl River Delta's one and the entry of China in the WTO are bound to bring to the fore major problems linked to the lack of such a law.

One issue that has already come to the light is the utility franchise that grants to China Light and Power (CLP) and Hong Kong Electric (controlled by Li-Ka-shing) the monopoly of generation and supply of electricity in Hong Kong. As a result of badly written agreements drafted when Anson Chan was Secretary for Economic Affairs, the two franchises are guaranteed until 2008 a rate of return on their fixed asset investments that is far too high. As result, although Hong Kong has been through 52 months of deflation brought about by the collapse of the property prices, Hong Kong Electric and CLP have managed to raise tariffs substantially, offering token rebate to cover-up a general increase. Today, both companies that do not compete since the agreement is that one supplies the island of Victoria and the others the New Territories are the second most expensive power utilities in the world. Protected by their contracts, they are immune to the vagaries of the local economy.

'That some property tycoons complain about the price of electricity in Hong Kong which is fixed by a scheme of control does not surprise me at all, says James Tien. The scheme itself is a big mess. But it does not mean that a scheme cannot work. It means this one is pretty bad and has a flawed control mechanism. What we have is that the electricity companies used the hottest day of summer as the benchmark of the scheme to get approval for their investment. They follow the letter of the franchise (11). We now have an overcapacity. That is absolutely ridiculous and the customers pay for it! In winter Hong Kong uses about 40% of the capacity and in summer roughly 50%. Since the scheme allows a return not on the consumption but on the total invested capacity at a rather generous rate of return, nobody cared for a long time. Why the government of the day did not pick up that the day used as benchmark was the wrong day is a mystery. One wonders what the civil servants were doing when the calculation both companies presented where based on the hottest day of summer.'

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The remarks of James Tien, who leads a party opposed to a blanket anti-monopoly law, point to the direction the government wants to go to avoid a frontal assault on entrenched positions. To say that the system is not flawed but the regulation is requires somehow further regulations. The irony of such logic is that Hong Kong might end up regulating what China is trying to deregulate. Hong Kong's elite is still using the same logic that the Carnegie, Rockefeller, and Mellon applied when at the turn of the XIXth century they successfully cornered their economic sector, under the guise of efficiency.

'The most sensible solution is to have a rational index to control the price mechanism, confirms James Tien. The Democrats want to open up the sector to more companies. In the electricity sector, I believe it is just not practical. Elsewhere where competition can be enforced, it should be done.'

But when one tries to define in Hong Kong what "elsewhere" means, one is soon hitting a wall. Carrefour, the world leading company in mega stores has now developed 40 mega-supermarkets in China, as well as several in Indonesia, but it had to pull the plug on its Hong Kong operations, with a loss of hundred of jobs, complaining that it could not get a fair level-playing field. The government replied to its complaints that Hong Kong was a free market and that competition was welcome. If Carrefour was not able to succeed, it was the law of the market, no a government matter. In other words, the laws were the same for everyone.

But what laws, one is tempted to ask. In Hong Kong, the business sector was built up over the years not in the spirit of competition but rather the contrary. For a century, the main purpose was to enforce and protect the vested interests of the British merchants, originally a small group of former drug-dealers who reinvested their ill-gotten profits into lucrative monopolies. As the British government would not spend any money in Hong Kong, the agreement was that they would be the ones financing the colony. In exchange, they would get "concessions", that is a monopolistic hold on specific trades and some pieces of land. Those privileges have never been abolished. They still permeate the economic fabric of the domestic economy.

Over the years, while the beneficiaries of the trade and the land may have changed, the principles of the regime have never been altered, and that is where the biggest problem of Hong Kong lies.

There are however more and more signs that the regime is under severe stress. In the long run, it is certainly unsustainable, the main reason being the pressure generated by the Guangdong economy on Hong Kong. The Hong Kong tycoons have sense that there was a danger to their dismay, have been unable to establish the control they have in the former colony (12).

THE SOCIAL STRUCTURE OF HONG KONG

Hong Kong was ranked eighth in the world for its per capita income in 1995, before Switzerland, France, Germany, or the United Kingdom. In 2001, Hong Kong was still ranked in the same league as France, the Netherlands, Germany or Japan with about US\$24,000, and was by that standard a richer economy than the Australian, the British or the Swedish one. It is in fact a statistical fluke, '*an illusion of wealth*' says James Tien. Yet many are using it as a proof of Hong Kong's wealth.

The per capita GDP indicator is the least serious of all the indicators a government can look at to know what sort of community it is running. One indicator that is easily accessible is the tax base. (We will later on, when looking at the budget issue, show how important the concept of public taxation is to a democracy).

If Hong Kong's per capita was around US\$24,000 (HK\$190,000), the number of taxpayers in the city actually paying salary taxes would be expected to be close to the number of employees (around 3 million). Yet, quite recently Anthony Leung, the Financial Secretary speaking in the Legislature Council said: '*among the population of 6.7 million, only 1.3 million are taxpayers, of which only 13,000 need to pay the standard tax rate, that is a salary tax rate of 15 per cent.*'

In Hong Kong, to pay taxes, one needs to earn more than HK\$108,000 a year if he/she is single. If we take the average benchmark of a household in Hong Kong at 3.3, on average each tax declaration pertains to a couple with at least

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one dependent or more as relatives and parents can be added as dependants in addition to children. To pay taxes, such a household will have to reach an income level of no less than HK\$241,000 (US\$30,897). To pay the maximum rate of 15%, the income of the household has to be no less than HK\$2,620,000 (US\$335,897), or HK\$1,450,000 for a single household with no dependent.

Based on Anthony Leung's statement, one can assume that in Hong Kong, 13,000 households have a taxable income of no less than HK\$2,620,000. Thus, if we consider that each of these households is made up of 3.3 people (which is an overestimation) we can deduct that about 40,000 individuals enjoy a minimum per capita income in the range of US\$101,000 (a per capita income is the assumed income of each individual, children and adults alike). Further data from the tax department indicate that another 53,000 households are between HK\$900,000 and HK\$2,620,000.

This group could be qualified as the super-rich individuals of Hong Kong, the elite. Yet, at most the group is made of about 200,000 individuals (2.9% of the population). And, from the data of the Tax Department, it is known that a further 135,000 households (or taxpayers) may have a per capita income of US\$24,000 per member of the household (which means that the tax return pertaining to that household is at least 3.3 times the per capita income).

What does that mean? That at most, 650,000 individuals, less than 10% of the population, actually have a per capita of US\$24,000. The conclusion is that 90% of the population has a per capita income below US\$24,000. Among them, tax data indicate that about 1,600,000 individuals are members of 500,000 households earning between US\$12,000 and US\$25,000. Once we allow for the average number of people for households, thus dividing by about a third the income of the family to have the individual per capita income, the average per capita income is likely to be US\$7,575 for each individual. That leaves the rest of Hong Kong, 4,7 million people, with a per capita income below US\$7,575.

If the government had some doubt on the not so pretty picture delivered by its own tax records and dismissed it with the classic argument that people tend to avoid taxes (although the computerization of the system in Hong Kong leaves little leeway to the taxpayers), it may still ponder over the fact that out of 3,041,000 employed workers, only 1/3 earns between HK\$108,000 a year

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(USD13,846) and HK\$241,000 (US\$30,897) a year. The rest, the Financial Secretary said, earn less. That, at the same time, they are considered enjoying a per capita income of US\$24,000 a year is thus a mystery (13).

It is of course a crude approach to gauge the validity of the per capita figure that is used to measure up the wealth of the 6.8 million people living in Hong Kong. But Alan Lung from the Hong Kong Democratic Foundation is not surprised: '*Hong Kong is not a developed country. If anything, it is just at the top of the developing countries*' he says.

Incidentally, a critical aspect of such imbalance in the distribution of wealth that comes to light and is of paramount importance to explain the current deficit is the fact that, not only the average population of Hong Kong does not live on a per capita income of US\$24,000, but to pay a salary tax, one must have a per capita income that is 28% above it at about US\$32,000. Only 18.9% of the whole Hong Kong population is likely to be at that level. Thus the tax structure excludes 82.1% of the population. Another obscene consequence is that probably more than half the civil servants are also outside the tax bracket and do not pay taxes, (and do not contribute to a pension plan that is passed on to the community).

Why then is the per capita income so inflated? There can only be two sources of errors: either the GDP is inflated or the population is underestimated. As we know, the characteristic of the Hong Kong economy is that it is the center of an enormous trade totalling about three times the size of the domestic economy (US\$440bn against US\$145bn). Therefore the GDP reflects badly the domestic economy. It is inflated by hundred of billions that are only paper money bringing little or no benefits to the population. As James Tien observed during a discussion '*the majority of the population does not benefit from such economic activities that are concentrated in the banking and financial sector*'.

Why then is the government using a flawed benchmark? To be consistent in its inconsistency. The colonial government has always inflated the per capita income of the population, but the reasons have evolved over time. Originally, and up to the mid 1990's the bureaucracy was always underestimating the number of people living in Hong Kong. The motive was that it would allow for underinvestment for basic services. Schools, hospitals, and other infrastructures

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were determined on a population that was about 10% below the real number of people living in the colony. The mistake started probably genuinely, when the floating population was important and it was hard to keep track of the refugees, but somehow the colonial administration discovered that the divergence had enormous advantages. As no governor wanted to be seen as having impoverished the colony, the per capita income kept increasing with little relation to the reality year after year.

In those days, and until the end of the 1980's the trade figures of Hong Kong were more or less in line with its domestic economy since Hong Kong was still a manufacturing center. Re-export trade was then minimal and the local stock market was not a financial center but a casino. Hong Kong Bank was still considered a local bank and Bank of China did not even exist in the radar screen of the financial analysts.

With the opening of China in 1978, soon the re-export trade overtook the domestic trade that, by the end of 1980's, had started to crumble because of the relocation of its manufacturing activities across the border. The surge in trade directed to China or coming from China inflated the GDP figures to the point that the government had to consider that a 'GNP' would have to be worked out, to reflect all the activities generated by Hong-Kong based companies, which now employ through subsidiaries about 5 million people in the Pearl River Delta. Notwithstanding, the GDP grew rapidly, inflated by trade paper money and transitory foreign direct investments. The service sector replaced the manufacturing sector as the largest employer and the per capita income jumped. The inflation, which was rampant at close to 10% a year for a decade, while the peg protected the exchange rate at 7.8, did the rest. Hong Kong, technically, became super-rich.

By the mid 1990's, Hong Kong people were in US dollar paper money richer than their UK counterparts (who had seen their per capita income expressed in US dollar badly affected by the melt-down of the pound sterling). That it was a fallacy was evident but the bureaucrats had a vested interest in maintaining it was a reality. The level of pay of the civil service was looking reasonable as long as Hong Kong was ranked in the top ten economies in the world. If Hong Kong had been ranked at number 45 or below, it would have been hard to

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justify the salaries of the senior civil servants, which were two or three times higher than those of their homologues in the leading economies of the world.

That Hong Kong was broadly an economy on par with sophisticated European countries with vast public resources and infrastructures was always a charade. Hong Kong has never been as wealthy as its colonial master, the United Kingdom, whose per capita income is actually far below that of France and Germany. Hong Kong, as a city, is in another league, much closer to Kuala-Lumpur or Bangkok than it is to London. That fact has yet to be accepted by C.H. Tung.

The resistance of the government to look squarely at the distribution of wealth has two self-serving motives. The first one is that, if Hong Kong is rich, it can pay for the most expensive administration of the world. If it is poor, it makes the current pay-level unacceptable and unsustainable. We come back here to the heart of the debate about public finances that C.H. Tung is trying to evade.

The second motive for Hong Kong's officials to live a fantasy is a dogmatic one. To admit that the Hong Kong society is far poorer than proclaimed would destroy the virtue embodied in capitalism. It would have a far-reaching impact on the chimerical values the Heritage Foundation attributes to Hong Kong's capitalism.

We have mentioned already that this foundation has constantly ranked Hong Kong as the world's freest economy because its government does not engage in public policies that would reduce the inequality of the society. The law of the market is supposed to be unimpeded. That Hong Kong is actually a cartelized economy, as William Pesek Jr recently wrote in the Herald Tribune, is conveniently forgotten. But if Hong Kong is the closest you can have nowadays to a pure capitalist society, then it is of paramount importance that it be wealthy as well and that such wealth benefit the community at large. Hence the use of the inflated per capita GDP. If it were not the case, some might be tempted to seriously ask what capitalism is about.

The skeptics can use three other indicators to corroborate the fact that the community is far poorer than previously thought. They are however strictly ignored by the Hong Kong officials. The first one is the level of poverty, the

second one relates to income distribution (giving the answer to where the money goes), the third one is the Gini indicator widely used by social academics to measure up economic equality.

Those indicators are generally ignored in countries where, either political representation is weak, or wealth disparity is no longer significant. In Hong Kong, since wealth disparity is significant and those indicators are ignored, one is led to conclude that political representation remains weak, which is the case. After all, C.H. Tung cannot be voted out of office and so far the leaders of Hong Kong have never run for election.

The new ministers did not need to present themselves to the public either. The majority were former bureaucrats and the others were, for the most, unknown personalities before their appointments. Thus, inequality can be ignored because a backlash against the establishment is never translated into votes (as can be seen with the scandal surrounding the purchase of a luxury car by the Financial Secretary, days before announcing a major increase in car registration taxes, which was not enough to force his departure from the government while it is obvious that he has lost all credibility).

In Hong Kong, where officials and businessmen are flooded with researches on the elusive “competitiveness advantage”, there is no official data providing the number of people living below poverty line. However the Confederation of the Trade Unions (CTU) worked one out. The result of its research was appalling. There are about 385,600 households, a rise of 13,7% since 1996, living below the poverty line. That number translates into a poverty level higher than in Indonesia at the end of the Suharto era. Yet, Indonesia was known as a poor third-world country, and Hong Kong as a wealthy economic tiger.

To determine the poverty level, the CTU used the classification of the OECD, so it provides a number that can be benchmarked against those of other countries. 385,600 households live on half the median household income which has been worked out by the CTU at being HK\$62,400 a year (a level that further corroborates the conclusion arrived at using the tax data). As a household is 3.3 people, it means that 1,284,000 Hong Kong residents live in a household having a total income of HK\$31,200 a year (US\$4,000). They represent 18,8% of the population. Their per capita income is about one-third

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that figure, that is to round up HK\$10,000 (US1,282). They are the super-poor of Hong Kong. The CTU has worked out that another 31.2% of the population lives on a per capita income somewhere between US\$4,000 and US\$8,000.

If accurate, and it looks it is, the research confirms that most of the population has a purchasing power far lower than what is in the government's booklets and the IMF reports. The largest group of people, an obviously silenced majority, has a disposable income below US\$8,000 per year. Thus there is little doubt that the real per capita income of the average Hong Kong resident is anything between 1/6 and 1/3 of the official per capita income used by the government.

The gap, or shall we say the gulf between the two figures is a sad reflection of the wealth disparity of Hong Kong. In that respect, Hong Kong's social structure is certainly that of a world-city, with a profound divide between the proletariat and the elite, but it is nothing the government can be proud of.

Could it be that C.H. Tung and the Financial Secretary remain totally ignorant of the situation? There are signs that it is not the case. To UNDERMINE the significance of the divide, the government officials go to great length to mask the situation, accusing if necessary the poor of being rich people trying to pass themselves for destitute in order to get some money from the government's pocket. The message the government wants to convey is that there are not so many poor, that people are smart (14) and that the government (not the rest of the community) is generous.

Such accusations are baseless and rather callous. They have been denounced by many caring organizations. Nevertheless, because of its weak political representation, Hong Kong entertains the fiction that the poor are always abusing the kindness of the benefactors. We will see why later on. In the meantime, the arguments are used to justify that a cut of 11.1% per cent cut in the Comprehensive Social Security Assistance (CSSA) budget will not be as bad as it looks (15).

Finally, for those who doubt that the difference could be so large, because it remains unacknowledged at the political level, there are two other data that deserve consideration. One comes from a study released by the Chinese University of Hong Kong. It reveals that from 1981 to 2001, households with

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the lowest income failed to increase their share of total income. Furthermore there are signs that the relative income of the poorest actually fell during the period.

In 1981, 20% of the population with the lowest income earned about 4.6% of the total household income. The figure increased to a peak of 5% in 1986, then receded to 4.3% in 1991 to stand at 3.2% only in 2001. That 410,000 households, about 1,400,000 people, are living on just 3.2% of the total income of Hong Kong is a reality. It may explain why C.H. Tung outlines in his Policy Address that welfare spending is increasing, but clearly he is misguided when he attributes such an evolution to the effect of ‘globalization’ or other fancy economic concepts. The hard fact is that the polarization of the society along economic lines is at an unprecedented level.

It is all the more obvious that while the poor get less from the total, it is not the middle-class that benefits but the rich. The 20% of households with the highest income earned 50.4% of the total income in 1981. It more or less remained in the 50% range in the 1980's but jumped to 56.3% the year before the handover and rose to 56.5% in 2001.

This evolution certainly justifies the argument that 80% of the population shares only 43.5% of the income and therefore that the real per capita of a middle-class Hong Kong individual is about half the official per capita figure used by the Hong Kong government to promote the image of a wealthy city.

Translated into monthly income, the above data revealed that the income of the poorest families has fallen from a peak of HK\$44,016 a year (US\$5,643) in 1997 to HK\$25,600 (US\$3,282) two years later, a drop of 23.3% in a decade. As deflation has yet to stop, it is quite probable that the average income has crashed through the US\$3,000 level in 2002.

At the other hand of the spectrum, the Asian crisis and all the factors mentioned by C.H. Tung to explain the economic downturn have yet to dent the income of the wealthiest of the city. The average income of the top 20% earners in Hong Kong was HK\$346,200 a year (US\$44,384) in 1990. It rose to HK\$436,764 (US\$55,995) in 1997 and in spite of the Asian crisis and the crash in the

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housing market, to HK\$445,380 (US\$57.157) in 1999, a total rise of 26,1% in a decade.

Thus, while the poor saw their share of the pie dropped by 23.3% in a decade, the rich managed a gain of 26,1%, increasing to an extraordinary level the wealth divide.

A last data to look at is the so-called Gini coefficient Social scientists use the coefficient to measure equality in society with zero representing absolute equality and one representing absolute concentration of wealth at the top. Statistics elaborated by the World Bank over many years show that in a developing country, the Gini coefficient is weighted in favor of the largest number in the population. It is the characteristic of a developed nation and is true of regardless of its political system. The United States, Canada, the European countries share a Gini coefficient in the range of 0.4. The United States, with less social harmony is at the upper range but quite below 0.5. China, in that respect is becoming a developed society, or at least an equalitarian one, with its Gini at 0,36.

In developing countries, where usually the wealth is concentrated in few hands and obscene disparity often the norm, the Gini coefficient is surging towards one. That is the case of Mexico, with a Gini at 0.525, far higher than Indonesia, not exactly an example of social harmony between extreme poverty among the masses and extreme wealth among its Chinese population, yet managing a Gini at 0.48. Using this indicator, Hong Kong is not London, or New York or Paris; it is Mexico, with the same Gini at 0.525.

That was before 110,000 households became negative equity holders because of the property crash. That was before the budget 2003/2004 was announced, a budget that targets the middle class, more than it does the elite (see chapter 4 on that issue). There is every indication that Hong Kong's Gini between 2003 and the end of the term of C.H. Tung will increase. Therefore social harmony is not increasing. By that benchmark it is fast decreasing.

There is a reason for that. Hong Kong has yet to catch up with the modern world. Being for 150 years a colony has left the population at large without adequate representation against the merchant elite, hence the total lack of

balance and check in matter of public policies. For the time being, it plays in favor of the elite.

Hong Kong's wealth is a delusion and a per capita income of less than US\$10,000 would provide a more accurate picture of the wealth of its community. Hong Kong is made of people with considerable less purchase power than it is generally believed. Its real per capita income is not that far above the per capita income of the middle class of its neighbors, Shenzhen and Guangdong, where per capita income are the highest of China at above US\$6,000.

Furthermore, while the Hong Kong people, to the exception of the elite, have seen a contraction of their per capita income after 52 months of deflation, the per capita income of their neighbors keeps growing at a rate of 10% a year on average (even faster in Shenzhen). Deng Xiao-ping had allowed fifty years for the Pearl River Delta to be integrated. The current trend in the per capita income points to a much faster process.

HONG KONG, A TALE OF MYTHICAL PROPORTION

And so, the story of Hong Kong is a tale of mythical proportion with little relevance to the reality. But it was always the case. Hong Kong was an eldorado for the few. It remains so. Therefore we should not be surprised that Hong Kong people, from the top down are generally clinging to a mythical past rather than looking squarely at the facts and taking the interest of the community as the paramount criteria.

It was in 1998 that we wrote: 'Hong Kong is part of the super-rich. It is even richer, according to the GDP benchmark, than its former master, the United Kingdom. But averages and trends and graphs and GDP that the Civil Service of Hong Kong is very good at putting together are not always what they seem. There may be more to them than meets the eye, and there is maybe a good deal less. A well-wrapped statistic can deceive. It can trick honest people into honest lies. Hong Kong statistics trick people into honest lies.'

Facts are not very kind with prejudices and lies. They outlast them and they ridicule them. Hong Kong is far from being developed in the sense you could

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say that a country with a GDP of US\$24,000 per capita is developed. In a way, it is miserable, maybe because the government is a miser, except for its own servants, the highest paid in the world.

Hong Kong has a myriad of problems to solve which is a legacy of the laissez-faire attitude that was the hallmark of the previous governments. But laissez-faire is not a hallmark of a free market system. It is a characteristic of indifference. It is not therefore surprising that there is a feeling of confusion at all levels. In the process, the tale of Hong Kong is exposed as being nothing more than a charade.' (16)

Asian Affairs' views were at the time considered outrageous by most of the establishment of the city. Yet C.H. Tung himself told the Legislative Chamber in January 2003 '*Now, we have the direction*', a clumsy admission that before Hong Kong had none. The city is discovering that it is not what the British said to the rest of the world and to the Hong Kong people it was.

Indeed Hong Kong since its handover to China in July 1997 has been bogged down by unprecedented problems. Some scholars argued in the 1990's that it would happen. Historical precedents highlighted that none of the former British colonies did well once they were left to their own fate. Could it be that Hong Kong is suffering from the same virus, the ex-colonial bug?

There were many reasons for the failure of the ex-British colonies. Some were certainly their own doings, others were circumstantial. But a few were imported from London and give some common traits to all of them, including Hong Kong.

Hence, one may not be far from the truth when stating that Hong Kong may be the victim of a combination of factors, one of them being its British legacy that makes it unable to move as fast as its successful neighbors, the most impressive being Shenzhen located at the end of its mass transit railway system

C.H. Tung sees that things are going wrong. He does not know why, but as a result he has transformed himself recently into a doomsayer. One of his recurring themes is to warn the community of tough days ahead. He attributes the bad news to events beyond his reach. '*As the most open economy of the*

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world, it was inevitable that the global economic crisis, etc. ... would affect Hong Kong' he said in his Policy Address of 2003.

While there is not a single data to back up his claim, but rather the contrary (17), there is anyway a vast irony to say that the world is responsible for Hong Kong's woes.

Prior to 1997, the main worry in London and Washington was China. The communist state was the biggest threat to Hong Kong mythical prosperity and way of life. It seemed a plausible concern, since China was presented as a country where the state was not working for the benefits of its citizens while in Hong Kong, it was believed that the government was there to defend their liberties. That the story had no substance did not matter. It was pure British political grandstanding.

As a result, a lot of energy was wasted to create a safety zone around Hong Kong that would prevent any kind of tinkering with the local system. Hong Kong was insulated and isolated, without consideration for its future. Notwithstanding, at the time, 80% of its economy was already China-bound. The divergence between reality and illusion was considerable.

The system of isolation was marketed by Chris Patten. It had a name. It was the rule of law. It is certainly true that good politicians are the ones who recycle old ideas under new slogans. Patten had this talent. The rule of law is now so commonly accepted as a slogan than no one really bothers to check what, in Hong Kong, it veils.

Without going into details, the rule of law could be summarized as a system that organizes rules, many of them in such a manner that changes are not welcome. The main characteristic of the rule of law is that it prevents change to established practices. Considerable amounts of money are spent on specialists, to find out whether a precedent could help a legal case to succeed. Therefore one could say that the rule of law does not look into the future, or does not look at what is equitable, but at what has been done in the past. When the rule of law refers to a colonial system, one can easily conclude that its use is to bring the past to overshadow the future. This is not a recipe for a positive dynamic but

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for at best the status quo and at worst, disaster (as many former British colonies can attest).

In Hong Kong, although it was admitted that some improvements were necessary, no one paid any serious attention to the fact that the rule of law might just be a tool to protect vested and ill-gotten interests. It was presented as its best immune system against China.

But what was supposed to be an asset for the city rapidly became a liability, as China was not after all a disease. It would rather be a drug that could enhance the performance of Hong Kong. As it happened, it was the only lever Hong Kong could rely on to slow its fall from its pedestal.

However to go from China being dangerous to your health to China being a medicine in such a short time confused everyone. The spillover effect of the perceived change gave rise to a sentiment of chaos and, for a short while, of insecurity. People had lost their crystal ball.

Hong Kong people don't feel insecure any more, China, from a potential threat has become in less than five years the anchor of last resort. It is a telling indictment of the misleading policies of Chris Patten. Nevertheless, such a rapid change led them to feel pretty much in the middle of chaos.

History books are full of such errors. In the future, they will record that the British and the Americans passed years trying to thwart any ambition China might have to integrate Hong Kong into its nascent economic system after the handover of July 1997. In the end, a mere five years later, with Chris Patten a forgotten man in the European Commission, the Hong Kong people wish their own Chief Executive would resign in the forlorn hope that the former Prime Minister of China, Zhu Rongji, would do them the favor of taking over the position rather than go into retirement. This is how far, and how weird some would say, Hong Kong has travelled between June 1997 and December 2002.

Of course, this wild dream shared by half the population of a Chinese official taking the helm of the city is not going to happen. To govern Hong Kong, one needs to be of Chinese descent and to have spent twenty years in the city. That excludes anyone in power in Beijing or elsewhere in China. The city is truly

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isolated and left to its home-grown officials, no matter how good or bad they are.

Indeed, one of the main problems of the city is one of governance. It is not that the Basic Law is not implemented but rather that it does not serve any good purpose. Today the latent defects of what remains mostly a text written with the exclusive view that it would freeze the colonial system into an everlasting model make it very difficult for Hong Kong to evolve.

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Notes fo Chapter One

- 1.- in Civilization and Capitalism - translation from the French by Siân Reynolds (Fontana Press 1985).
- 2.- The bridge would connect Hong Kong to Macao and Zhuhai, across the estuary of the Pearl River. The anchor point in Hong Kong would be on Lantau Island. It would open in 2006 at the earliest. The concept was first put as a proposal in the 1980's by Gordon Wu, a Hong Kong construction tycoon.
- 3.- Shenzhen, in the suburb of Hong Kong, is a city of 4.7 million people. It is a 20 year-old town established at the request of Deng Xiao-ping. Its growth has been spectacular. It is not a cramped city with badly designed infrastructures, but large avenues and a modern conception of what a urban development should be. The modernity of the city is best expressed by one ratio. The number of telephone users per inhabitant in Shenzhen is higher than in Hong Kong. There are 6.1 million telephone users in Shenzhen (1.29 telephone per people) against 6.3 million users in Hong Kong (0.94 telephone per people). Hong Kong claims to have the highest penetration of mobile phone in the world. Actually, it is probably Shenzhen.
- 4.- In Asian Affairs n° 11, Li Zibin, then Mayor of Shenzhen (1995-2000) was highly critical of the administration of Hong Kong. *'Shenzhen does not need Hong Kong's money any more, he was saying. The period when we did not have enough to invest is over. Here, we believe to develop together our potential will be much more efficient than wasting both our energy like we do every day because the Hong Kong officials react and move very slowly (...). The consciousness and acknowledgment of the necessity for Hong Kong to restructure its economy and industry came very late. If the financial crisis hadn't passed through, Hong Kong would yet have to realize it has to restructure. To some extent, the crisis has somehow helped Hong Kong to make up its mind. The second reason why Hong Kong is not efficient is that the Hong Kong financial, tourism and trade sectors are doing well. But its manufacturing sector is still under developed, not to mention its high-tech development industry, which has yet to create something. The financial crisis warned Hong Kong that in its economy the bubble element takes too much place. (...) but some people at some level who deal with these questions in Hong Kong do not adhere to the view that to develop a closer relationship with Shenzhen and to harmonize the build-up of high value industries will be beneficial for both. They look down on Shenzhen, and although we repeatedly emphasized the opportunities for each side to benefit each other, they really believe that they will do well on their own. In a way, they are just keeping an old colonial mentality. They still ignore the fact that Shenzhen can develop without Hong Kong. We have had a 15% economic growth annually for the past ten years; not many cities in the world can put forwards such an outstanding performance. With cooperation we could improve that, yet they don't see the point!'*

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In the same interview, Li Zibin, who was already appointed Vice-Minister in charge of the Go-West policies noted that Hong Kong, in 2000, was not yet conscious that Guangzhou, Shenzhen, Zhuhai, Macao, Dongguan, Foshan and the entire Pearl River Delta would in the next twenty years become a single urban zone as large as Los Angeles. Two years after such remarks, C.H. Tung listed the construction of a bridge linking Hong Kong to Macao as a fundamental necessity for the economy of Hong Kong.

- 5.- Not all cities survived the shift of the center of the world-economy they used to control. Some were destroyed by competing cities - such was the fate of Carthage. The Roman world is full of former world-cities. Palmira in Syria and Volubilis in Morocco are classic examples of lost cities because the trade pattern shifted. Closer to the modern world, Zanzibar in Africa, Galle (Sri-Lanka) or Calcutta are also examples of cities that have lost their economic importance, although both are much bigger cities than they were at their heyday.
- 6.- The British economist David Ricardo (1772-1823) was one the most important figures in the development of economic theory. He articulated and rigorously formulated the “Classical” system of political economy. The legacy of Ricardo dominated economic thinking throughout the 19th Century. On foreign trade, Ricardo set forth his famous theory of comparative advantage. Using his famous example of two nations (Portugal and England) and two commodities (wine and cloth), Ricardo argued that trade would be beneficial even if Portugal held an absolute cost advantage over England in both commodities. Ricardo’s argument was that there are gains from trade if each nation specializes completely in the production of the good in which it has a “comparative” cost advantage in producing, and then trades with the other nation for the other good. Notice that the differences in initial position mean that the labor theory of value is not assumed to hold across countries as it should be, Ricardo argued, because factors, particularly labor, are not mobile across borders. As far as growth is concerned, foreign trade may promote further accumulation and growth if wage goods (not luxuries) are imported at a lower price than they cost domestically thereby leading to a lowering of the real wage and a rise in profits. But the main effect, Ricardo noted, is that overall income levels would rise in both nations regardless. With his 1817 treatise, Ricardo took economics to an unprecedented degree of theoretical sophistication. He formalized the Classical system more clearly and consistently than anyone before him had done. He acquired a substantial following in Great Britain and elsewhere, what became known as the “Classical” or “Ricardian” School. Ricardo’s theory gradually fell out of favor, and died a slow death soon after the Marginalist Revolution of 1871-74.
- 7.- Founded in 1973, the Heritage Foundation is an archconservative think tank whose mission is to formulate and promote conservative public policies based on the principles of free enterprise, limited government, individual freedom, and other so-called traditional American values. What the Foundation appreciates in Hong Kong

is the fact that the government policies are always with a view to maximize return on investments for the investors. It concludes that Hong Kong is a free economy because monopolies and oligopolies are allowed to fix the rules of the market without intervention from the government. The yearly ranking has little credence among scholars, because the Heritage Foundation is a partisan think-tank funded by lobbyists. Their publications have generally little scientific value.

- 8.- One sector that came under scrutiny more often than others is the oil products industry. The Consumer Council indicated in 1998 that *'the oil products industry is highly concentrated and largely vertically integrated, with three oil companies holding over 70% of the piped and wholesale cylinder LPG market, 90% of the motor gasoline market, and 80% of the diesel market. It is characterized by relatively small total demand, limited growth opportunities, and barriers to entry such as the need to achieve economies of scale in storage and retail and the high cost of land. As such the three product markets can be characterized as oligopolies. Theoretically, the consequences of this form of market structure can lead to cooperative behaviour, which may be explicit or implicit in form. Explicit collusion leads to a cartel, which is usually a target of scrutiny by jurisdictions with competition oversight. However, cooperation may also be implicit, in the sense that the few firms in the market recognize their mutual interdependence and realize that it is not in their interest to constantly drive prices down to marginal cost levels. In any case, a symptom of both explicit and implicit cooperation is that prices are uniform and above their competitive levels.'* In spite of such a report, the government failed to deregulate the sector.

Five years later, Dr Enzo von Pfeil, the founder of an independent investment advisory boutique, noted in a report that, while the price of Brent crude fluctuates, the retail price of petrol in Hong Kong always keeps rising. Focusing on diesel prices in Hong Kong, he subtracted duty and converted prices to US\$ per gallon, trying to illustrate price differentials between Hong Kong and the USA. In March of 2002 US diesel, before duties was US\$0.77 per gallon whilst it was nearly 300% higher in Hong Kong.

He also made the following comparison. In February 2000 the price of a gallon of petrol in Manhattan was US\$1.56 per gallon (Manhattan is known for its high prices just as Hong Kong is). At the same time the average price in Hong Kong was HK\$10.50/litre or US\$5.10 per gallon. Then he tried to evaluate the cost structure (who makes what) on a litre of petrol in the US and to apply it to Hong Kong, assuming that the price of crude oil and refining costs are the same in both countries, then factoring in the respective applicable taxes and duty. That method isolated the margin of distribution, marketing and profits as the balancing figure in the price at the pump. As Hong Kong is a very densely populated city, distribution should be cheap and efficient, and advertising is minimal as the sector is heavily integrated, he concluded that most of the balancing figure is pure profit margin. He came to the conclusion that while American companies work on a gross margin of 5%, in Hong Kong they secure 21%.

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In another sector, the Consumer Council has outlined that one company (Ng Fung Hong) controls around 90% of the supply of pork meat into the market and retailers had been complaining that the company was practicing discriminatory pricing, with a subsequent detrimental effect on the competition between wet markets and supermarkets. In the rice market, it is only in 2002 that the cartel organized by the government since the end of the second world war was dismantled. Prices dropped by 50% overnight.

It would be easy to list many more examples that would illustrate the lack of competitive pricing in the city. It is of course a legacy of its former glory as a world-city at the frontier of China.

- 9.- Blurring the line on the real value of FDI invested in Hong Kong is the fact that the city remains the most important source of external direct investment in China. According to Hong Kong's statistics, the stock of Hong Kong's outward direct investment in China amounted to US\$130 billion at end-2000, accounting for 33% of Hong Kong's total outward direct investment. According to China's statistics, the cumulative value of Hong Kong's realised direct investment in the Mainland reached US\$195bn at end-June 2002, accounting for 47% of the total external direct investment there.
Hong Kong's investment concentrates largely in Guangdong. According to Hong Kong's statistics, the stock of Hong Kong's direct investment in the Guangdong province amounted to US\$50billion at end-2000, equivalent to about two-fifths of its total direct investment in China. The bulk of such investment belongs to industrial investment, involving primarily outward processing arrangements. About five million Chinese workers in Guangdong are working for around 36,000 companies involving Hong Kong interest. This is 24 times the size of Hong Kong's own manufacturing workforce. Thus, it is quite difficult to have a correct appreciation of what is a foreign investment that is invested in the city itself. Disney World is a good example of an investment directed to the city, but the Disney company is only investing US\$400 million, the balance being provided by the Hong Kong government.
- 10.- The borrowings of the Hong Kong conglomerates were hedged against the US\$ dollar by the Hong Kong peg. Their cash-flow was not affected by the currency melt-down that other Asian companies had to withstand because their income was in fact dollarized. None suffered any currency loss.
- 11.- The scheme of control for Hong Kong's two electricity firms - CLP Holdings and Hong Kong Electric Holdings - is flawed and should be replaced with an efficiency-based mechanism after it expires in 2008, analysts at Bear Sterns, JP Morgan, HSBC Securities and Lehman Brothers say. They found the scheme encouraged spending on fixed assets and over-building, while customers were expected to bear the cost. They said the post-2008 regulatory environment should give incentives to boost efficiency.

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They suggest the asset returns of CLP Power and Hongkong Electric should be benchmarked with overseas counterparts - at between eight per cent and 12 per cent (it is currently 15%). *'The current scheme of control is flawed . . . First, the returns are too high compared to the risks. Second, there is no incentive to operate efficiently. Third, there is incentive to over-build'* Bear Sterns analyst Gary Chiu said.

Angello Chan, a Lehman Brothers analyst, said the future returns should be tied to the consumer price index, which would ensure power firms delivered a certain level of efficiency gains and did not overcharge on tariffs through over-building or unnecessary capital expenditure. Shareholders would be left with a reasonable return if the companies managed to cut costs, Mr Chan said. HSBC Securities analyst Ivan Lee pointed out that the reliability of electricity supply was on the list of priorities when it came to mapping out the future regulatory scheme. In 2004, the government and power firms will start an interim review of the scheme of control agreements, but Li Ka-shing who controls one of the tow utilities (Hong Kong Electric) has already indicated that he would oppose any substantial change. *'The scheme serves Hong Kong well'* he argued.

- 12.- It is not that the Hong Kong merchant elite did not try, but rather that their efforts and tactics to monopolize a trade through early investments in a sector have been constantly thwarted by the Chinese government. For example, when Li-Ka-shing started to invest in the Shenzhen port facilities which he was the first to see as a threat to the Hong Kong port facilities where he enjoyed an entrenched dominant position, his company (Hutchison Port) tried to take a majority stake in all the future berths. The Chinese government refused. Gordon Wu tried the same tactic as regards toll roads and power plants. He, too, got sidelined when his position started to be too dominant.
- 13.- The exact spread of income among the Hong Kong taxpayers is as follows (HK\$ dollars converted in US\$ at 7.8)
- | Annual Income (HK\$) | Total | % population |
|---------------------------|---------|--------------|
| US\$12,820 to US\$25,640 | 500,000 | 7.35% |
| US\$25,641 to US\$38,460 | 316,000 | 4.64% |
| US\$38,461 to US\$51,280 | 190,000 | 2.79% |
| US\$51,280 to US\$76,920 | 149,000 | 2.19% |
| US\$76,921 to US\$115,380 | 69,000 | 1.01% |
| US\$115,381 and above | 66,000 | 0.97% |
- 14.- Anthony Leung, while defending his budget in February 2003, made a more provocative remark. *'Hong Kong people are damned to misery for the hedonist times they have enjoyed'* he said. He later on had to apologize, saying that he had used an inappropriate analogy. He was lambasted in a radio-talk show, where a caller surnamed him "a squandering brat".
- 15.- The number of people receiving welfare benefits has hit an all-time record high of 258,000 in July 2003 (1.2% more than June), according to government figures.

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Professor Nelson Chow from the Department of Social Work and Social Administration, the University of Hong Kong, stated that 1 out of 8 families received CSSA and it's a high rate. But in line with the attitude of the government, instead of seeing this development as a proof of an increasing poverty, he attributed the rise to an abuse and suggested a revision of the CSSA system.

- 16.- In Asian Affairs n°4 . The issue was published in the autumn 1998, with interviews with Joseph Yam, Chief Executive of the Monetary Authority, David Li, Chairman of the Bank of East Asia, Arthur Li (his brother), Vice-Chancellor of the Chinese University (he is today Secretary for Education), Martin Lee, Chairman of the Democratic Party, and two industrialists, Peter and John Mok.
- 17.- If the claim has any substance, it would be expected that if the external conditions improve, then the Hong Kong economy would recover quickly. But it is not happening. Trade figures show that Hong Kong has been enjoying in 2002 one of its best years ever, tourism was booming until March 2003, and yet deflation continued unabated, property prices remained still at rock-bottom and if on paper economic growth was said to hover around 2 or 3%, there was no signs to a return to growth in the domestic economy. This is a clear sign that the correlation between the current domestic crisis and “globalization” is a far-fetched idea.

**CHAPTER II -
THE POLITICAL LANDSCAPE**

- 2.1. - THE ABSENCE OF DEMOCRATIC TRADITION.
- 2.2. - THE BASIC LAW: A MONUMENT OF AMBIGUITY
- 2.3.- SMALL OR BIG GOVERNMENT
- 2.4. - THE ANSON CHAN LEGACY
- 2.5.- A WEAK AND INEFFECTIVE LEGISLATURE
- 2.5.- THE ARTICLE 23 SAGA:
AN INDICTMENT OF THE SYSTEM

THE ABSENCE OF DEMOCRATIC TRADITIONS

Hong Kong, as long as it was a British colony, did not have a proper system of governance. One of the characteristics of the British colonies is that a governor, who, in many respects, had kept a regal authority, while at home the King had lost all political power, ruled them. The Master of the Governor was first the Foreign Office and second, the Prime Minister. The Foreign Office, being a permanent institution, had the advantage over the British government and therefore the colonial system evolved overtime into a formidable bureaucracy. Tradition prevailed over initiative and in the United Kingdom tradition is nowadays called the rule of law.

The United Kingdom does not have a constitution and Westminster power is not enshrined in a constitutional document. Hence the inability for the government of Hong Kong to derive its authority from a clearly define set of laws.

When the question of Hong Kong's governance came up, when the British told Deng Xiao-ping that Hong Kong would be returned to China, they added a proviso: the colony would be returned as it was and its system of governance would have to remain the same. The argument was that it would protect the way of life of the Hong Kong people. The not so-implied but rather clearly stated opinion was that China was notoriously careless towards its own people, while the United Kingdom was a gentle and benign colonial power. It was of course a charade.

China did not have any particular knowledge of the Hong Kong system (1) that the British proudly boasted as the best for its people. The problem was that the British, as they soon realized, had no a particular knowledge of their own system either. Or rather they discovered that the system as it was, was rather in the mould of a dictatorship, which was an embarrassing admission to make!.

The Governor and its retinue of officials were ruling Hong Kong as they saw fit. In theory they were answerable to the Foreign Office, but in practice it was of little relevance. As long as Hong Kong did not cost money to the Treasury, the Governor was the master of his kingdom. Any sign of progressive politics, such as the devolution of power to the locals, was what one could call a private initiative, some Governors being inclined to delegate it, others not. In short, there was no real law applying to Hong Kong but rather a set of conventions and traditions easily bent whenever necessary.

This highly flexible system was by essence not democratic at all but it suited everyone. The reason why it suited everyone was that Hong Kong was developing along the principle that anything that was not permitted was illegal, but everything was negotiable. And the underlying thinking was that if you did not like it, then you left it. Hong Kong had always been a place of last resort. Its very transient population was classified as "refugees".

What was then considered a considerable asset at government level could today be a liability for the mindset among the population has not changed much. *'If the businessmen feel that the government is not acting for their benefits, James Tien says, they might as well move across the border. Most have no attachments to Hong Kong. It is just a place of business. Their roots are in China where they spend 50% of their time.'*

And indeed everything was negotiated. Many vested interests developed in the vacuum of any strict legal and constitutional arrangements that would have clearly delineated the power of the

government and force a unique set of rules to apply equally to every citizen (as a civil code would). Whenever necessary, a new set of laws would appear to enshrine what had been decided behind closed doors. That is what the rule of law is about. The result is a very fragmented and unequal society as can be seen in every former British colony.

The consequence, in terms of public life, is a lack of cohesion and equality in the community. It is at the heart of the problem of governance facing most if not all the former colonies of the British Empire.

But how do you translate such an accumulation of ad-hoc rules and laws into a comprehensive constitution? That was an impossible task, yet it had to be done, otherwise the Chinese would just have established a new system of governance with a new set of laws and regulations. It was not the interest of the people that mattered so much, but rather the private interests of the elite. The rule of law was a fire-wall established to protect the banking cartel, the property sector, the duopoly that controlled Hong Kong's port facilities and many other undisclosed cosy arrangements.

The fire-wall is so efficient, the vested interests so deeply entrenched, that, to give a single example, Hong Kong Bank that is now known under the name of HSBC as the largest retail banking institution in the world still derives the largest chunk of its profits from a small city of 7 million people where it had at some point a near-monopoly. Yet, it officially moved out of Hong Kong in the 1990's. The Li Ka-shing empire (Cheung Kong, Hutchison and many other companies) is also another conqueror of the world from its Hong Kong fortress.

As Jasper Tsang, the leader of the DAB party put it *'before 1997, all decisions for Hong Kong were made in London, not here. Take Hong Kong being declared a port of first-call during the Vietnamese boat-people crisis. It was a London decision and the local officials simply carried out the policy. They did not feel any responsibility to answer the concern, queries, and objections of the people of Hong Kong. They did not feel responsible for the social consequences of such a decision; they were simply carrying out orders. The Hong Kong people had just no say whenever it was considered necessary to ignore them.'*

While the British did not want the Hong Kong people to carry out orders coming from Beijing, they had little choice but to package a flawed system into what turned out to be a badly drafted document.

The mini-constitution of Hong Kong, known as the Basic Law, far from enshrining a clear set of governance, piles up a set of ad-hoc and ambiguous rules that today hinder any move towards accountability and transparency, not to mention a decent democracy (2).

THE BASIC LAW, A MONUMENT OF AMBIGUITY

When it comes to the head of the government, the Basic Law states in its article 45 that he or she shall be "selected by election or through consultation". The wording of the article is purposely ambiguous. Who is going to make the choice between one method and the other is not specified. And if the word used is "selected", rather than "elected", it is to provide legal arguments that an appointment through an ad-hoc committee is perfectly in accordance with the rule of law thus defined.

While the “ultimate aim” is the selection by “universal suffrage”, there is no commitment on a date. Furthermore, before being so-elected, the candidate will have to pass a first test: “nomination by a broadly representative nominating committee in accordance with democratic procedures”. Thus, the nomination of the head of government is a convoluted process that is everything except a one man, one vote process.

The text will certainly in the future be the center of furious legal interpretation and arguments. There will be on the one hand those claiming that the rule of law is so important to Hong Kong’s future that the Basic Law has to be upheld, while others will be asking for the reinterpretation of the article 45 or an amendment to make it a clear and unambiguous document. There are already signs that the government is trying to push the issue of the election by “universal suffrage” of the Chief Executive beyond 2007.

The article 45 has been used twice, in 1997 and 2002. In 1997, there were officially five main candidates, two from the business community (C.H. Tung and Peter Woo) and three from the legal sectors (Simon Li, Lo Tak-shing and Yang Ti-liang). C.H. Tung was known as the uncontested winner days before the Election Committee convened.

In 2002, the Election Committee did not receive any other candidacy than C.H. Tung’s one and therefore he was “selected” without a proper election. The reason for the lack of candidacy was that no other public figure thought he or she could garner enough support among the members of the Election Committee. The Election Committee members, being unelected, had no public comment on the matter and no justification to give to the Hong Kong population.

‘In the past the British used to impose a governor, so after 1997, Beijing used the so-called election system to impose the Chief Executive on us, but unlike the British who appointed someone from London, this person is from Hong Kong’ says Emily Lau, one of the most popular legislators of Hong Kong.

The membership of the Election Committee is therefore of critical importance. Who chooses the members and how is crucial. There is no doubt that the matter will come under scrutiny long before the next election in 2007 and will be a major bone of contention between the grassroots politicians and the elite.

Currently the Election Committee does not represent the people of all walks of life but primarily the establishment. It is itself a “selected” committee among the elite. One can easily understand the incestuous relation that exists between the head of government and its electorate (3). It is in a way a medieval institution. Venice, at the peak of its glory, was using a similar method to elect the Doge among its merchant elite.

‘Anything is rigged and controlled. We want the system to open up and that the power be up for grab’ Emily Lau laments. *Once the political parties are really competing for power, independent legislators like me may disappear. That is fine. That is the sort of logic that should be used and we should not let vested interest hijack and use the system.’*

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THE ANSON CHAN LEGACY

The architect of the so-called “neutrality” concept was the highest-ranking civil servant, Mrs. Anson Chan, who, to satisfy one of the requirements of the Sino-British agreement of 1984, was appointed by Chris Patten as his Chief Secretary (5). She went on to remain the Chief of Administration until her retirement (6).

‘Any bureaucracy, whether American or European, behave the same way, points out Alan Lung. Its main aim is to be immune to change, because change means trouble. Civil servants are always worried to get into trouble. Our civil service was and is just aiming at self-preservation regardless of anything else.’

Anson Chan had a profound effect on the civil service culture post 1997 for she conceptualized and put together a coherent theory for the political neutrality of a civil servant to stand apart from the Chief Executive in any important decision.

‘Even today you find this motto that the civil service should remain politically neutral as if it were possible, Jasper Tang says. Let me give you an example. There was a debate on the reforms of the housing policies and whether or not land sale should be frozen. The decision was delayed by one week. And why? The ministers had argued that the measures were necessary. Then from the civil service came the argument that because we are a free economy, the government should not interfere and no decision should be made in favor of a freeze. Mr. Tung, others, and myself argued that we should not deceive ourselves. The government is the largest player in the housing market. That has always been the case. So how could we claim that we should be neutral under the guise of a free-market that does not really exist? The civil service could have asked why the housing market was government-led, but it was not its point. It wanted to be seen as neutral, meaning it should do nothing. Since all of the decision-makers knew that in the housing market, the government was the main player, to argue that it was a free market economy and therefore the government should do nothing was nonsense. Yet the civil servants would not admit it because to recognize the truth would challenge the myth of their so-called neutrality. The officials did not really care about the economic situation in the sector. So, even today when there is a debate among the top civil servants, a debate where the Chief Executive himself is a party, you find this motto that the civil service should remain politically neutral as if it were possible.’

Anson Chan was not only able to shape the so-called neutrality concept; she had become the only source of power within the civil service, long before C.H. Tung assumed the position of Chief Executive.

‘She was surrounded by people she was familiar with. Hong Kong people called them the “handbag gang”, because these ladies had very close personal relations with her’, Jasper Tang said with a ironic smile on his face.

James Tien, although at the other end of the political spectrum, concurs: *‘in the old days, when Anson Chan was at the top of the civil service, the whole civil service was run as an old boys’ club. No one from within would rock the boat because once you retired you would join a public body such as the airport authority, and enjoy the gravy train up to the end. Many if not all the*

senior officials took advantage of the system. Just look around and you will see how many landed plum public appointments after retiring.'

What made matters worse for C.H. Tung was his lack of public relations skills. In his previous activities, as the heir of a vast fortune, he never had to develop those. As Christine Loh puts it mildly: *'It certainly carries a political price.'*

Anson Chan, who started her career at the bottom of the colonial ladder, had thirty years to perfect the art of being obedient and in the right light at the right time. As for every civil servant, her remarkable career owed probably more to her PR skills than her competence. She therefore easily outsmarted C.H. Tung and positioned herself immediately as the symbol of continuity.

Thus, any attempt to control her or reign in her authority among the civil service would then have been interpreted by the media as an attempt to subvert continuity. Anointed the conscience of Hong Kong by the international media, she soon considered that she did not have to be answerable to any one but her own conscience.

She had positioned herself skilfully as the center of everything within the civil service and senior officials were afraid of her because she would not tolerate any dissenting view. She would promote or sideline people without consideration to any other matter than their loyalty to her.

She was very good at enlisting an army of supporters, even among the legislators, who nevertheless lambasted her for the disastrous opening of the new airport. She was everywhere, while C.H. Tung did not even look carefully at his own pro-Chinese clan.

'After our former Vice-Chairman Gary Cheng got in trouble, revealed Japer Tang, the leader of the grass root party D.A.B, Anson Chan was the only senior official who spoke to me most often of his legal problem. She was always asking me to let her know if she could do something to help. She used to say: " I miss him very much". But how could it be true? I knew and she knew that she could not do a thing about his legal problems. But that was the way she was operating and trapping people within her own circle or pushing them outside.'

Eventually Gary Cheng was jailed for one year for corruption (7).

Ultimately, the disharmony between the Chief Executive and Anson Chan became public knowledge, even though they kept denying it.

If Anson Chan was in the eyes of the public the conscience of Hong Kong (8), C.H. Tung started to look more and more like a blundering and incompetent leader, for everything that was going wrong was attributed to his leadership and every positive move the work of the civil service upon which he had no control whatsoever. Anson Chan was constantly in the news and her rating far higher than her boss' one.

Behind the spin the main thrust of her actions was preventing Hong Kong from moving closer to China. She had never been comfortable with the Mainland authorities, and had little knowledge of China. She had been constantly ambiguous about her future, telling me in 1993 that she was considering moving to London where her children were living. Then, the offer to

be number one of the administration came. It was too good to be refused. Her ambition got the better of her resolution.

Thus C.H. Tung was after all telling the truth when he reckoned in his Policy Address 2003, that Hong Kong had at last a direction, for it had had none as long as Anson Chan was his Chief Secretary for Administration.

'I can see the reason why it happened, James Tien says. Our civil service is imbued with a British type mentality. Considering that we were richer than our neighbors, our officials inevitably thought why should we go and help a poor neighbor such as Shenzhen, for example, that is likely to compete against Hong Kong as soon as it has the means? That was not only a very narrow-minded point of view, but also an extremely short-sighted one. It was as if the meaning of the "one country-two systems" concept was the further we, Hong Kong go up, the further you, China, must go down. Of course, it could not work.'

No one had any time to look into the future. Hong Kong was drifting slowly but surely outside its own world economy, a development that today has many implications.

'Before Anson Chan's retirement, within the civil service, you were either a friend or a foe, Jasper Tang says. People were just looking after themselves.'

'No one from within would rock the boat, laments James Tien, because once one retired one was eyeing a public body. In their days, most of the top colonial civil servants when retiring were doing the honorable thing. They were going home. In 1997, the Hong Kong Chinese civil servants had nowhere to go home. They just wanted to go on and on forever at the taxpayer's expense. No one wanted to be off the gravy train. A very unhealthy development for the society took place, unchecked.'

A WEAK AND INEFFECTIVE LEGISLATURE

The Basic Law provided Hong Kong with an elected legislature known as the Legco. It is made up of 60 seats, 50% being allotted to functional constituencies, and 50% to geographical ones. If every Hong Kong permanent resident and citizen can vote in a geographical constituency, only the few and selected ones can vote in a functional constituency. In other words, less than one third of the population theoretically has two votes and the others one.

To be directly elected in a geographical constituency, a legislator needed in 2000 as little as 25,971 votes (Wong Sing Chi in Kowloon East). The most popular support went to Chan Yuen Han and Chan Kam Law whose lists attracted 108,587 votes in Kowloon East (9). At the other end of the spectrum, as many as 7 functional constituencies' legislators, that is more than 10% of the legislative chamber, did not face an election as they had no opponents.

James Tien, the leader of the Liberal party, was one of them. And where elections took place, David Li (banking sector) was elected to his seat with 89 votes while Miriam Lau (Transport sector) held to the seat she has secured a decade ago with a mere 106 votes. In a city of 6.8 million inhabitants, the inequality introduced in the voting system is blatant.

People unfamiliar with the past would probably squarely blame China for such an unbalanced system, but it is in fact the British that originally designed the system as a way to prevent the

emergence of a popular vote that would have been able to provide an unified front against the colonial administration after the first election held in 1985.

'The British were extremely good at dividing loyalties' reckons James Tien today. He is nevertheless one of the beneficiaries of a system that was denounced in 1995 by the United Nations as fostering inequality.

This electoral system has created some entrenched positions that explain both the difficulties of the Executive to implement policies and its lack of accountability when those policies fail miserably. It also undermines gravely the genuine development of political parties and political awareness among the population (10).

Since about 10% of the legislators are not elected at all, they consider themselves as independent. However they generally represent very narrow interests. The Legco seems to be more or less without direction, as the legislators have no common interest but only vested allegiance that may change according to the topic under scrutiny. It explains many inconsistent votes and the fact that the government is able to overturn any opposition to its stated policies and gets the laws it wishes to see adopted passed by the chamber. It also explains the lack of coherence in government policies as the administration tries to satisfy conflicting interest so as to catch all the independent votes in order to block the possibility of the democratic vote banding together against a specific law and imposing its rule.

Emily Lau explains why there is such a lack of coherence: *'we are four members of the Frontier in the chamber. On political issues, the four of us share the same view and will probably vote the same way, but on economic issues we may differ. Cid Ho (Sau-lan) and I are maybe more on the right than our two colleagues. They are more left-minded.'* Actually, Lee Cheuk-yan from the Confederation of Trade Unions and Leung Yiu Chung, another Trade Unionist, currently affiliated to the Frontier are Trade Unionist leaders.

A two-time legislator known for her outspoken views, Christine Loh became by the end of her second mandate disillusioned with the work of the Legislative Chamber. Disappointing her supporters, she decided not to run for another mandate in 2000.

'I felt that the Legislature and the Executive were losing credibility, she says. By and large, political parties have lost public support. That was what I was afraid of. The institution of the legislature is now less regarded than it was before.'

'The relationship between the Executive and the legislature remains fraught, she adds. Legco cannot do too much. Legislators, individually, have not kept their popularity. It has gone down, rather than up. Political parties are less well regarded as they were because I think they are all having problems defining themselves and finding a path to reflect the reality of today. I don't think if I had stayed in the legislature I would have necessarily done better than them. I left because I wanted to be able to refresh my entire attitude to politics. It does not mean that legislators and other political figures are not doing their job, but the perception is that the system is not as effective as it could be.'

THE ARTICLE 23 SAGA: AN INDICTMENT OF THE SYSTEM.

An obvious sign of how little trust the citizens of Hong Kong have in their own system of governance and in Legco as a watchdog that represents the will of the majority is the attitude of the public in the implementation of the Article 23 of the Basic Law.

The Basic Law provides under article 23 that *'the Hong Kong Special Administrative Region shall enact laws on its own to prohibit any act of treason, secession, sedition, subversion against the Central People's Government, or theft of state secrets, to prohibit foreign political organizations or bodies from concluding political activities in the Region, and to prohibit political organizations or bodies of the Region from establishing ties with foreign political organizations or bodies'*.

Since 1997, Hong Kong has been without such laws. Hong Kong never had in the past laws dealing with state secrets or secession or sedition for the simple reason that being a colony such laws pertain to a sovereign state. An act of treason or sedition could conceivably have been solely one against the United Kingdom.

If the sovereignty of the United Kingdom over Hong Kong was absolute, since the handover the former colony has had to define a path between its own limited sovereignty over its region (the Hong Kong SAR) and the sovereignty of China to which it belongs. Such a dubious arrangement was born out of necessity rather than rational, because the British government did not want to go down into the history books as one delivering to a communist country millions of people that had been stripped of their British nationality without having a say in the process.

For some, the debate should remain purely academic and the issue should be trashed out by lawmakers, but the proposal to enact laws in respect of article 23 have stirred up many emotions that, we thought, no longer had any place in the Hong Kong society. The level of emotions the issue raised highlighted that, among its characteristics, a world-city always keeps a political dimension. Today, some, mainly outside Hong Kong, believe that such a dimension still matters.

The debate rapidly turned to a simple question: if the laws derived from article 23 were merely to shadow the Chinese law, it would mean that Hong Kong has finally surrendered its autonomy to China, as if the possibility of a grey area in matter of national sovereignty could exist and been forced against the will of the sovereign nation.

Whether it is possible not to surrender it is actually academic, as Hong Kong belongs to China, and the issue is no longer of any interest for the future of Hong Kong as a city. Yet, many were prepared, and are still prepared to go a long way to challenge again whether the ultimate arbiter on such matters is the central government and the National People's Congress. Playing an important role in the debate was the fact that the issue, arousing considerable interests in the foreign community, was providing an easy opportunity for political grandstanding from some fading politicians.

In any case, the interesting consequence has been the resulting indictment of the current system of governance, suspected of being unable to protect the interests of the population. The more the critics said the proposals were unacceptable, the more they were telling the world that their own lawmakers who had the ultimate say (and had not yet seen the draft), would do the wrong thing.

In Hong Kong, no law has ever been implemented against the ultimate will of the legislature. Nevertheless, the government has never seen any substantial proposal being rejected. Many bills have been modified by the legislators, unfortunately generally for the worse rather than the better, as their amendments tend to cater for the vested interests they represent rather than for the public good.

The legislative process is somehow a tedious and convoluted one because the legislators or the political parties do not have the initiative. They do not propose laws, they only study the laws prepared by the government and which are on the agenda. The Chief Executive has absolute power over it and he can easily derail any initiative coming from the floor. Nevertheless, it can be argued that a united Chamber could defeat a proposal. That would not necessarily prevent the Chief Executive from enacting it, but it would certainly trigger a political crisis.

Therefore under such a system, one would think that laws to be enacted under the article 23 have to be ultimately approved by Legco and that the people could rely on their law makers to work diligently on a matter of such importance. The political process could therefore have been straight forward, if the people had any trust in the Hong Kong institutions and would recognize the ultimate authority of their own institutions. As it happens, not only the people of the city have shown that they do not trust anyone, but many legislators have disparaged the process. The result has been to further weaken the credibility of the political parties and the politicians in general.

Of course, to word laws that would maintain the integrity and sovereignty of China while maintaining the autonomy of Hong Kong in the matter is a difficult exercise, all the more because Hong Kong uses the common law system while China uses a civil law (a problem that Macao does not have to face since Portugal did not use the common law system). This introduces significant differences of legal definition compounded further by the fact that the law has to be a bilingual one (Chinese and English). But such unavoidable technicalities, which are likely to create a considerable amount of paper and a diversity of opinions, could probably be solved in a rational manner without arising suspicion of bias. But what happened when the Hong Kong government announced the project was to trigger an avalanche of criticisms, most of them underpinned by a political bias.

In essence the British laws on sedition or treason are as drastic and as secretive as the Chinese ones. The fact that they are hardly used nowadays does not make them less drastic. What matters is the way a government exercises its authority and its mandate. Hong Kong had to live with such laws for a very long time, and no one really bothered about them. Although they existed, it was felt that they were irrelevant. But because China would be the ultimate arbiter of sovereignty laws applying to Hong Kong, and because its present government has specific views on religion and political dissidence, every one in Hong Kong, rightly or wrongly, was asked to feel threatened. The “China” threat that has been overused in Patten’s days was back with a vengeance in the front page of the newspapers.

Thus, at a time where everybody thought he would turn his attention to economic issues and not to politically sensitive ones, C.H. Tung came under tremendous criticism from all quarters, including his own supporters.

‘I do not know why the issue was raised at the beginning of C.H. Tung’s second term, says James Tien. But in all likelihood, we have been five years without a law treating sedition and

security of the state. It is a long time. Beijing must have pointed out that the legal void could not continue. Yet, in the end, I suspect it was badly handled. Now it is a public relation disaster. It is a political issue that could distract the government from more pressing problems.'

What most of the critics wanted was a formal public consultation on the content of the bill. In Hong Kong, short of a legislation authorizing a referendum, public consultations that are not binding on the government are called “white bills”. The government publishes a text and the public can for a period of time suggest changes. In practice, very few proposals are included, but the process allows the government to gauge whether it is appropriate to table the law at the Legco. Occasionally the bill would be scrapped altogether.

When the government made clear that it would not publish a white bill, the public jumped to the conclusion that the blue bill presented to the legislators would be a foregone conclusion, no matter how harsh the wording. Ten of thousands of people marched in the street to protest against the decision, not realizing that the march in itself was an indictment of the legislative process.

Emily Lau readily admits that it is indeed the case. *‘Nobody, not even the legislators, is privy to all the documents exchanged between the government and the mainland authorities, she said when talking about article 23. And now, if the government gets into law that communications between Beijing and Hong Kong are going to be documents classified as privileged or state secrets, not even the legislators will have access to it. The question then is, how do you control and judge? The government should come clean and tell the Hong Kong people what has been discussed instead of keeping it secret. But it won’t do it. People including legislators are left to speculate. It is quite terrible.’*

The government disagreed with such an interpretation of the facts. Elsie Leung, Secretary for Justice, was quick to point out that *‘while her department was actively involved in the proposed implementation of Article 23, its main function was solely to ensure that the proposed new laws were consistent with the human rights guaranteed in the Basic Law and the International Covenant on Civil and Political Rights, [and] to provide advice on relevant laws in other jurisdictions’.*

‘Ultimately, she added, the manner in which a balance is found between the need to protect national security and the need to protect rights and freedoms is for the community and Legco to decide.’

Finally the government introduced a draft (called a blue bill) in the Legco at the end of February 2003 for the legislators to consider. Some legislators opposed to the legislation considered that it was a foregone conclusion as the majority of them have expressed support in principle after the original proposal had been considerably watered-down to take into account a number of remarks made by various sectors of the community. 21 of them, the Democratic camp as they labelled themselves, out of 60, staged a walkout to protest what, they said, was the government’s bid to rush the bill into law (10).

Thus, the issue of the article 23 became a litmus test of the level of trust Hong Kong has in its system of governance. The answer was a resounding “no trust” at all. Many concluded that if C.H. Tung had been a directly elected leader, he would probably have been censored, but actually the commotion has shown that he has a point when he says that to ensure a peaceful

transition was no mean feat. The Chinese government must have been alarmed by the criticisms levelled to his administration, but it is doubtful that they did him any harm.

To the contrary, they have exposed clearly that in Hong Kong, China's sovereignty is still for some a problem. That perception could only reinforce C.H. Tung rather than weaken his support in Beijing. On the other hand, those who have been using the argument to gain political mileage such as the Democratic legislators have further distanced themselves from the masses, which, as we have pointed out, are no longer ambivalent about China, but rather supportive of a government that they see as being more benevolent than theirs.

To conclude, the article 23 saga exposed further among the community the lack of trust in the system of governance. While C.H. Tung may be asking that the Hong Kong people work together, his policies have increasingly polarized the society. To attribute such a divide to his lack of abilities is misleading or naive.

It appears, as we shall see, that, since 1997, the unelected leader of Hong Kong has a political agenda, one which requires the majority of people to acquiesce to the omnipotence of the plutocracy, and therefore to accept his own legitimacy and competence. What we see is that some segments of the population are starting to react to his policies, thus the problem with C.H. Tung is not one of competence. It is one of choice and political orientation, thus the so-called political parties when they try to personalize the issue of governance are showing a lack of political awareness that is quite puzzling.

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Chapter two notes

- 1.- Lu Ping, Chinese Minister for Hong Kong and Macao Affairs, in an interview with Serge Berthier (Autumn 1992) in the French review "Politique Internationale" – Special issue on Hong Kong.
- 2.- The drafting of the Basic Law began in 1985 when the National People's Congress appointed the Basic Law Drafting Committee (BLDC), comprising over 50 mainland and Hong Kong members. The Basic Law Consultative Committee (BLCC) made of Hong Kong people selected by the colonial administration was set up to canvass the views of the Hong Kong people. The first complete draft of the Basic Law was published in April 1988, followed by a five-month public consultation exercise. The BLCC was loaded with people close to the colonial administration and it reflected strongly the views of the Foreign Office. A second draft, taking into account some of the views expressed by the public (and mainly by vested interested parties such as the civil service itself) was endorsed by the Standing Committee of the NPC in February 1989. The BLDC had then been divided into five Special Groups that had up to December 1989 to present a final wording. The final draft was then endorsed by the BLDC in its plenary session in February 1990 and was enacted and promulgated by the National People's Congress of China on April 4, 1990. The most ambiguous and contentious articles of the Basic Law are in fact copied from the Joint-Declaration signed on December 1984 between the United Kingdom and China. The terms of the Joint-Declaration were negotiated in strict confidence and the guiding principle was to establish "One country - Two systems". Thus the British had to pen from scratch what the second system was.
- 3.- The Electoral Committee is made of 800 members from the Industrial, commercial and financial sectors (200), Labour, social services, religious and others (200), the professions (lawyers, doctors, etc...) (200) and political personnel (Legco, Hong Kong deputies to NPC, etc) (200). Among the members, there are prominent families that are well represented. Li Ka-shing and his two sons, Henry Fok and his two sons, C.H. Tung and his brother, are members of the Electoral Committee. A legislator is not necessarily a member (most of members of the Democratic Party are excluded), while the head of a monastery (Po Lin) is included (and for fair balance the bishop of Hong Kong, who represents a religion practised by less than 2% of the Hong Kong population). The members of the Electoral Committee are the elite of a selected group of about 6,100 people who are appointed in a rather secretive manner members to some 400 advisory committees.
- 4.- In Asian Affairs n°4 – Autumn 1998.
- 5.- Under the Sin-British agreement, all senior officials in the administration would have to be Chinese by 1997. In 1992, the most senior colonial administrator was David Ford who had the title of Chief Secretary. Anson Chan was then Secretary for Economic Affairs since 1987. David Ford was not due for retirement before 1997. In normal circumstances, he should have kept his position until his retirement but was pushed aside to groom a Chinese civil servant as the most senior civil servant. David Ford was offered a new posting in London, created for the purpose (as Hong Kong's representative in the United Kingdom), and a position in the Executive Council. There were other senior Chinese civil servants than Anson Chan that could have been appointed, but she was the only one young enough not to be forced into retirement before the year 2000. She was therefore appointed as Chief Secretary.
- 6.- After July 1st 1997, according to the Basic Law, the Executive Authorities were defined as the Chief Executive, a department of administration, a department of finance and a department of justice. It meant that the Chief Secretary under the colonial rule was to be known as the Chief Secretary for Administration. Anson Chan took the view that the change of title was in effect a

down-grading of her position and she started to use in the English media the title of Chief Secretary, dropping the “for Administration”, thus subverting the hierarchy of the government. When she retired, she was succeeded by Donald Tsang, former Financial Secretary and the title has been fully restored to Chief Secretary for Administration.

- 7.- Gary Cheng Kai-nam had been elected in the Hong Kong Island constituency in 1998, securing more than 100,000 votes. He was re-elected in September 2000 with 72,617 votes, although he had run as an independent candidate, to distance his party from a looming scandal. A public relations executive, he admitted failing to disclose his business links to several officials, while acting as a legislator. On September 29, 2001, he announced that he would not take up his seat in the legislature. He was convicted in December 2001 and jailed for 18 months for misconduct in public office, accepting an advantage as a public servant, theft and false accounting. After remission of one-third of his sentence for good behaviour, he was freed on December 2002. Gary Cheng was found to have spoken on behalf of the Sports Development Board in three Legco meetings between October 26 and December 6, 1999, without disclosing the fact he was paid by the board, a public body, as a public relations consultant. He also arranged a meeting with Deputy Secretary for Home Affairs Arthur Ng Sek-hon, in which he sought to influence the selection of members for the new Sports Development Board without revealing to Mr Ng his link to the board. District Court Judge Alan Wright told Cheng his crimes had eroded the public’s trust in their leaders. The judge spared Cheng a heavier sentence because of his “very substantial fall from grace”. Among those who stood by him was DAB chairman Tsang Yok-sing and vice-chairman Ip Kwok-him. Some believes that he was harshly treated and a victim of the SAR’s judicial system since it was public knowledge that he was a public relation executive. Furthermore, it is quite common for officials and political appointees to exercise pressure and influence decisions.
- 8.- In October 2002, the Far Eastern Review has found a new conscience for Hong Kong: its new bishop. It did not matter that Bishop Zen represents only the view of a religion that is practised by less than 2% of the Hong Kong population and is the spokesperson of the Vatican. His views have little support among the majority of the population, and little to do with his conscience. They generally reflect the opinion of the conservative wing of the Catholic church.
- 9.- In the 2000 geographical Constituency Elections, 24 LegCo members were returned from five geographical constituencies, Hong Kong Island (5 seats), Kowloon East (4 seat), Kowloon West (4 seats), New Territories East (5 seats), New Territories West (6 seats). A List Voting System operating under the Largest Remainder Formula - a form of proportional representation voting system - inaugurated in the first LegCo election in 1998, was used to allocate the seats among the candidates.
- 10.- They then burned an enlarged copy of the blue bill to register their disapproval. Cheung Man-kwong, the most vocal of the legislators opposed to what he called a draconian law said that the pro-democracy lawmakers would do their utmost to oppose the law. *‘I can assure you we will not allow this piece of legislation to pass through the council smoothly, he said. We will not be the government’s rubberstamping machine.’* Since then, the Bill Committee has been working four hours a week on the proposal and has screened 57 objections raised by the public. The focus of attention of the democratic camp is the power to proscribe organizations that might be considered endangering the state. There is currently under the Society Ordinance the possibility to deregister any organization at will. The power lies with the police. In the past, the British hardly used the power because prior to 1997, they hardly authorize the registration of a society that would have been able to carry out political activities but they relax their control six months before the handover, which allowed more than 500 non-governmental organizations with clearly a political content to register. One of them is the Hong Kong branch of the Falun Gong, an organization considered subversive in China.

**CHAPTER III -
FROM BRITISH RULE TO PLUTOCRATIC RULE**

- 3.1. - THE PRICE OF A SUCCESSFUL HANDOVER
- 3.2. - THE MEANING OF THE MINISTERIAL SYSTEM
- 3.3.- DOES CHINA CARE ABOUT THE ANTICS OF C.H. TUNG?

THE PRICE OF A SUCCESSFUL HANDOVER

At the time of the change of sovereignty, Chris Patten had successfully planted the idea that China was a potential threat to Hong Kong. While the population had been led to believe that the threat was against its way of life, the real meaning was that China, a proclaimed socialist country, could be a threat to the way the elite had cartelized the city for its exclusive benefits. The paranoid attitude of its politicians brainwashed by their Western sycophants, had had the unfortunate result of depriving the ordinary people of a serious political debate about what kind of city they wanted to see emerging once the British had gone.

Not surprisingly, when C.H. Tung took over, his main priority was not to look carefully at the state of Hong Kong, for he believed strongly in the myth, but to focus on two indicators: the level of foreign investment in the city, and the number of people emigrating to some perceived foreign paradise (they later turned out to be on tax nightmares for the Hong Kong people, and some of them were put in jail for tax-related offences).

'There has been a continuous inflow of capital following reunification, with foreign direct investments growing at twice the rate of GDP, he emphasized in September 2002. Enterprises from all over the world come to establish their business. More and more multinational corporations set up their regional headquarters here, making Hong Kong home to the largest number of such offices in Asia. People emigrating overseas before 1997 have returned. The "brain gain" and the continuous inflow of capital over these five years strongly reflect people's confidence in Hong Kong.' (1)

He did not question whether it was because China, unscathed by the Asian crisis, was at last perceived as a normal country rather than a dangerous place, or the realization that after all foreign paradise were tax hells, that people returned and foreign investments kept going (directed to China actually). He had no doubt that it was because of his own policies. In any case, that phenomenon allowed him to take the credit and to argue that the "One Country-Two systems" concept was successfully implemented.

But such a perception seems to be a fantasy. Very few people in Hong Kong are prepared to give him any credit at all, since the majority of them, those with a per capita income of about US\$10,000 rather than US\$24,000, think that they would be better served by someone like the former Chinese Prime Minister, Zhu Rongji. Their tepid opinion of the Hong Kong government leaves little doubt as to where their hearts and minds are. There is thus no doubt that the reversal in the perception of China, from negative to positive, was instrumental in the confidence building process that allows today C.H. Tung to say that the "One country-Two systems" has worked. On that, neither C.H. Tung nor the political establishment of the city had any control or direct responsibility.

Remarkably Emily Lau, well known for her scathing views on China, admits that: *'the One country-Two systems formula has worked in the sense that Beijing did not send guardians into the civil service or the government.'*

But she will not let China off the hook so easily. She still considers that the Chinese government *'abused the system by supporting C.H. Tung over any other contender for the position of Chief Executive'*.

Alan Lung, the Chairman of the Hong Kong Democratic Foundation, disagrees. *'That argument makes no sense, he says. China is entitled to its opinion, as we are. The "One country-Two systems" system is working. But we should not fool ourselves. It is bound to evolve into a single system. We are part of China. I do not believe that local governments are constrained by the Chinese leadership. When we get down to the provincial level in China, we can see they are not. And to me, the provincial leaders look more progressive than our own local leadership. That is our problem and not a Chinese plot. Our government officials want to please the Chinese leaders, and not knowing what to do because they receive no instruction, they speculate on what is expected, and inevitably are going overboard.'*

Jasper Tang is the leader of a party considered by some as pro-Beijing and by others as the only efficient grassroots party. He agrees with Alan Lung. *'Most of us agree that China has held up to her word, he says. All important decisions are made here. But no one should forget that any final consideration is of a political nature. The government has a duty to do a balancing act between various interests. That is the nature of the job. It should not be seen as a mark of bias and we should admit that we are part of China.'*

While political analysts and observers were speculating whether China would erode the values of Hong Kong, C.H. Tung was very careful not to change the Hong Kong system. It did not require much persuasion to convince him that it was the best course, since, coming from an elite that benefited greatly from Hong Kong, he has the strong conviction that the system we described in the preceding chapters was the best Hong Kong could get. He therefore did not have the slightest inclination to challenge any aspect of it. That is where he was different from some other contenders to the post of Chief Executive.

The more forceful one was another member of the elite, whose social prominence was also inherited, Lo Tak-shing. But while C.H. Tung's family originated from the Shanghai elite, Lo Tak-shing belonged to the bluest clan of Hong Kong, the "Honges", the few Chinese families that, as early as the end of the XIXth century, had already been accepted among the colonial elite. Lo Tak-shing had a deep and long knowledge of the colonial system, and he had been through its excesses, resigning his position of Executive Councillor in the wake of the 1984 Sino-British agreement in protest against the Foreign Office's views.

He was for a long time the front runner for the position, many believing that his past was pleading in his favor, as an ardent defender of Hong Kong's interests. His resignation, as a sign of a principled man, would have been an asset in other days, but after the circus created by Chris Patten around the handover, the Chinese government had no choice but to transform the change of sovereignty in a nonevent. Lo Tak-shing was out. His coming to power would have sent the wrong signal. The international media would have interpreted his coming to the helm as a revenge, no matter what his attitude would have been. In politics, perception is always more important than substance. Chris Patten had shown the way, and contrary to what the democratic politicians believed, it was not Jiang Zemin that positioned C.H. Tung on his pedestal, but the imperatives created by his own antics.

Rather than helping Hong Kong to move with confidence into uncharted territory, he had created the perception that anything new was bad. As China did not want Hong Kong to look bad, it came to the sensible conclusion that nothing would have to have the appearance of being new. C.H. Tung had not expressed publicly a single view during the five years he had been an Executive Councillor, while others had said many things one way or another. It was expected

that he would not say much once appointed "Chief Executive". After all, he was the first to believe that Hong Kong needed only a figurehead, the rest being run as usual.

But to think that Hong Kong would not change was an impossible proposition. It was bound to change anyway in a very significant way. The Governor owed his existence to the British. As inconspicuous as he would be, the Chief Executive could not owe his existence to China, for it would mean that China was denying the Hong Kong people political rights and political capacity. The only alternative to give a semblance of legitimacy to the process and influence public opinion was to purport that power was vested in the civil service, not in the Chief Executive who was a figurehead. It meant that the civil service had to be presented as an apolitical animal.

It proved to be a dangerous manipulation because what the Chinese government intended to be a public relation exercise proved to become under Anson Chan a reality. In the vacuum of power that Chris Patten had created by focusing only on his feud with China so as to polish his public international image, she had manoeuvred herself as the center of the local power long before July 1997. Even though she is today criticized for that, Anson Chan did it with the compliance or the complicity of the Legco, which proved to be, time and time again, very inconsistent in its judgment towards her.

Without popular support and with a mandate to transform the change of sovereignty into a nonevent, C.H. Tung was thus condemned to enter into a marriage of convenience with the civil service. Any initiative to the contrary would have been interpreted as a sign of change, even though the people and the media had failed to fully admit that a great shift of power had taken place between the arrival of Chris Patten and his departure.

It would have been a difficult position for anyone, but it was even harder on C.H. Tung who, due to his social background, had never been urged to share any power with anyone before being elevated to the position of Chief Executive. As the heir to a fortune, the successor of his father at the helm of a company, he never had to cope with sharing his authority with anyone, except the members of his family. There is no indication that he was prepared to share power either, but the fact that he did not bolt when he discovered the situation is a proof of his resilience.

To enter into a coalition to assert power and authority is always problematic. It was even made more so by the fact that he had expected to conduct the government as the governors and he discovered this would hardly be the case.

To assuage his disappointment, Anson Chan had promptly agreed to play the role of the good administrator. Unfortunately, her competence in that respect was minimal as had been revealed by the fiasco of the opening of the new airport of Hong Kong, a pharaonic project with a price tag of about HK\$140bn.

The British wanted it to open before their departure, as a testimony of their dedication to the Hong Kong people, but it had been embroiled in the unnecessary wranglings that Chris Patten and herself had entertained with the Chinese administration for five years. That the project was late because of China's interference was easy for Chris Patten to say, although it was only half the story. But for Anson Chan to admit a year after the handover that it was further delayed

because of the incompetence of the administration would have looked ridiculous. She therefore agreed to an official opening that proved to be six months too early.

The result was a logistical nightmare, with a price tag of about HK\$1bn. A public inquiry was held and the legislators disclosed that, in the chain of command, far from being innocent, she had been instrumental in more than one way in her wrong appreciations of the project. Her choice of appointees had been disastrous.

But rather than sanction her, C.H. Tung must have considered that by being lenient, and saving her job at a time when her departure would have been accepted by the public as her gross incompetence had been exposed, he was transforming their marriage of convenience into an alliance where he had the upper hand.

It could have worked if Anson Chan's perception of Hong Kong had not been fundamentally different from that of her boss. While he believed firmly in the world-city concept, he also knew from experience that China was the natural source of wealth of Hong Kong. It was not even a sentiment that was politically motivated, although C.H. Tung entertains very strong nationalist sentiments towards his country. It was a pragmatic judgment of what Hong Kong was about and where the elite sources its wealth.

But Anson Chan had no experience in real life. She had been used, on the name of the British master, at keeping China at bay, for many reasons. For her, the source of strength in Hong Kong was not China. She strongly believed in the reverse. Like many misinformed and politically biased people, she was convinced that Hong Kong was the indispensable actor of China's economic revival.

Thus, she continued to act as if the handover, the Asian crisis and China's economic reforms had changed nothing. The divergence with reality was absolute, but civil servants are used to work in an abstract world reduced to procedures and reports. On the other hand, C.H. Tung had worked in a world made of invoices, bank loans, interest rates and investments.

Inevitably, overtime, their relationship came under stress. They had nothing in common, and they did not share the same vision for Hong Kong. The feud engineered a standstill, which ironically was perceived as a positive move, while in reality it was a catastrophic development for a world-city. Hong Kong was easing itself out of its own world-economy. By the time the feud was over, others had moved into its position.

When Anson Chan retired a year earlier than contractually required, C.H. Tung had been expected to quickly assert his authority over a restive administration. Disappointment followed when it did not happen.

It is in that restricted sense that the transfer of sovereignty could be labelled as a success. The combination of the administration and the elite provided a framework of reference quite similar to the colonial one. Since the aim was to transform the event in a nonevent, it can be said that C.H. Tung had been instrumental in achieving such an aim. But to create such a perception proves today to be beyond the means of Hong Kong, as we shall see.

THE MEANING OF THE MINISTERIAL SYSTEM

There are signs that either C.H. Tung perceived quite soon the handover that the community had lost trust in his government and his ability, or that in order to be able to hold the reins by which he would guide the political life of Hong Kong, he realised that he had to get rid of the structure he had inherited as soon as it was politically possible. The later is more probable than the former.

In any case, people were challenging the *fait accompli*. Such a sentiment was in Hong Kong a novelty. *'The colonial government was never challenged, Christine Loh says. Before 1997, the people were mentally used not to challenge what the government wanted to do. Rightly or wrongly, we never had the feeling that the government did not know what to do. But more and more people started to criticize the government and the officials. Because they are not used to the feeling of challenging a government's policies, the Hong Kong people may look confused or irrational. Yet, they feel they should challenge them because things are not going very well for them.'*

During his annual policy address on 1 October 2000, C.H. Tung proposed a solution to the confidence crisis that had set in the community as well as in its own kitchen cabinet, alluding to a new "executive accountability" system.

The delay in the implementation of the system that was finally introduced on 1 July 2002 was credited to his lack of leadership, but in retrospect it appears that the main stumbling block was Anson Chan who had not yet retired. Although she was officially supportive of the idea, it is hard to believe that she would have willingly implemented a system whose aim was to curtail the power of the administration and to hand over part of the responsibilities of the government to outsiders whose promotion and terms of employment would have been out of her control or that of her successor. C.H. Tung therefore, had no choice but to wait for her scheduled retirement before making his move.

'When C.H. Tung mentioned his ideas, recalls Jasper Tang, the leader of the DAB party, I was heavily criticized for supporting it. Many were against any innovation while they kept criticizing the way the government was organized. They thought that the move would just be cosmetic. Then, for a year, not much happened. We had no precision coming from the top. Legco was kept in the dark. In 2001, the Chief Executive said that he had no time to look at all the details. I concluded that he would not say much in his next policy address but actually he did the reverse, giving more specific details in his policy speech of 2001. I don't think it was tactic. I rather believe that at some point he realized that the existing system was under too much stress. All the senior civil servants who were formulating the policies kept pretending to be neutral. They did not consider themselves responsible for the many scandals going on in the housing department and many things were going wrong. He had officially to shoulder every blunder. His advisers must have pointed out that he had no choice but to move out of the trap laid by Anson Chan with her neutrality concept.'

C.H. Tung is by nature a rather secretive man. Therefore we should not attach too much importance to the sequence of events. Yet, being a public figure has a price. How his policies are made and pursued are under increasing scrutiny, and he has yet to master the art of playing up the gallery. But it does not mean he is a political novice, only that his style is different.

Christine Loh disagrees. She says that he is not politically savvy. *'Hong Kong doesn't have skilful politicians, as politics is something new in this place, she says. This lack of competence*

is compounding the perception that Hong Kong has lost its way, that the government is incompetent, and the people unhappy. All these things are coming together.'

Jasper Tang, James Tien, and Emily Lau believe that Hong Kong is not politically matured, arguing that their political parties are very young and very small. By membership, the largest one in Hong Kong is the Democratic Alliance for the Betterment of Hong Kong (D.A.B) with about 2,000 members (2), a small number for a city of 6,8 million people. In the past, it was the Democratic Party, but its membership has shrunk dramatically to only 560 members (3). As for the Frontier, a well-known vocal pro-democracy group, it is not a political party per se but only a group of pressure, *'because it would be ridiculous to call it a political party with less than one hundred members*, Emily Lau, its most well-known figurehead says. *Furthermore most of them do not want to stand for elections. They are only interested in the public debate, but political parties have to face elections. They have yet to make the connection.'*

But the Frontier is not unique in its predicament. Everywhere, and at any time, the number of those who have a lively interest in public affairs is relatively insignificant. Professor Robert Michels in his master book *"Political Parties: a sociological study of the oligarchical tendencies of modern democracy"* observed long time ago that, in the majority of human beings, the sense of intimate relationship between the good of the individual and the good of collectivity is but little developed. In Hong Kong, it is all the more so because, in a colony, such a relationship is always discouraged in many ways. Thus the issue of quantity is not really what matters and the Hong Kong politicians are wrong to consider their reduced numbers as a sign of immaturity. In fact, for a city, it seems that it has already too many minor professional politicians and it appears that it is not political skills among them that is lacking, but purpose.

Egoism, private interest and vanity can spur people to an interest in public affairs, and do spur in Hong Kong many of them but so far with little vision and originality. That only a minority participates in party decisions, and sometimes that minority is ludicrously small, is not the problem. The problem is a lack of breadth and social awareness.

That effective power is always in inverse ratio to the number of those who exercise it, is a permanent characteristic of the democracies. It must not be construed as a sign of apathy on the part of the people, but as a constant need for direction and guidance. In actual fact, the best field of observation of this tendency is offered by the intimate structure of the democratic parties themselves. There are no denying that their structures are invariably less than democratic. The reason is the undeclared craving people have for the cult of a leader.

Hong Kong nascent political parties do not escape the rules, and the way the critics of C.H.Tung react to his decisions is a clear proof of such a craving. Time and time again, they argue that the Chief Executive has never been able to clearly articulate his policies. They say he lacks political sophistication (a quality they attribute to themselves), while a minor theme is that he is unable to build a working relationship with other politicians.

'C.H. Tung does not involve people in any process, complains Emily Lau. The legislators have no responsibility. We collectively vote on the budget and laws that are presented to us, but then, because of his attitude, we have no other responsibility. It is very stupid on his part.'

Albert Chan, a twice-elected grassroots legislator, attributes C.H. Tung's indifference to the legislative process to mistrust rather than stupidity. *'It is hard to know whom C.H. Tung trusts*

or does not trust, he says. The very narrow circle around him blamed Anson Chan for his failure during his first term. For the past nine months, he has had a new team but Hong Kong remains directionless and chaotic. Anson Chan is no longer the head of the civil service. Can he continue to blame her for what is going on? Clearly there is no sense of leadership and a lack of decision on many issues.'

But the substance of such criticisms is about C.H. Tung's personality, rather than his policies. We are not told that the policies are unacceptable, but that they are poorly prepared or poorly implemented. On that basis, if one was to construe what is wrong with the policies, one would have a hard time to find out from the political parties what would be a reasonable alternative to a set of decisions, because none offer a substantive one. The debate rests on the qualities a leader must show, and thus the critics expose solely their genuine, although not directly expressed, sense of disappointment in the hero the leader is supposed to be, rather than a new direction.

Participation in political life has always an echeloned aspect. In Hong Kong it is taking an extreme form, because the political actors have yet to devise a sense of purpose. The opponents do not challenge the plutocratic system, but its figurehead. Thus politics is personalised to such a extent that the political parties constantly fail to convince the people that their economic and social interests are identical to their own. That is the origin of the sense of confusion that is now prevailing across the board in the society. By aping the tastes, the mode and the mentality of a plutocracy, the political parties fail to expose the mechanisms at play that sustain it. They, too, desire to maintain the myth of Hong Kong so intensely that whenever the government is perceived to fail its duties, they attribute it to the incompetence of the actors, not to the system. Thus the struggle between C.H. Tung and its opponents is devoid of any real political substance, as their aspirations are indistinguishable.

This is why when C.H. Tung there engineered a very significant point of departure from the colonial system of governance he had inherited which undermine the very "raison d'être" of the political parties, they fail to see how dangerous the move was for their own future. It was also the proof that C.H. Tung has no qualms about the privileges a plutocratic system grants him

In essence, when he announced his new accountability system, C.H Tung was declaring to the Hong Kong people and the legislators that he did not regard them as capable of playing an active part in influencing the destinies of the city, and for that reason alone, telling them that they ought to be deprived of any say on the government. That was an incredible statement, of incomparable sincerity, a sure sign that C.H. Tung is the weak leader the political parties think he is. He made clear that he does not accept public approval as a necessity to his rule. He demands authority. The most surprising thing is that his declaration of war to his opponents left the opposition in total disarray.

Emily Lau admits that the political actor are at a loss. *'Since they are perceived as being without responsibility, she said, talking about the legislators, they become irresponsible. They propose policies that cannot be tested anyway. They can do that because no responsibility is attached to their political discourse. That is why they constantly criticize, fairly or unfairly, the government every time it comes up with a new initiative. After all, it does not matter. Their counterproposals and their criticisms will never amount to any concrete action.'*

Actually C.H. Tung is probably quite satisfied to see the Legco casting itself in a decorative role rather than a substantive one, because it discredits a system for which he has little regards.

In any case, the system, known as "Principal Officials Accountability System (POAS)" was designed and imposed quickly so that it would be in place for the start of the second term of C.H. Tung's mandate (July 2003).

'I see in C.H. Tung's attitude towards issues a pattern, Christine Loh says. We have a bad precedent with the housing policy he enacted in a rush when he came to power (the policy will be analysed later). When he became convinced that he had to back down, he rushed into another series of commitments. No one is sure where it will lead us. Most of the road map on housing policy has yet to be released. Maybe there is no road map, but just an idea. It is exactly the same pattern with the ministerial system. Once C.H. Tung was convinced it was a necessity to do something, he rushed into it. But if you looked at the original proposed ministerial structure and the final one, it seems that there were no coherent views. Then, because the structure has no real logic, people wonder if in the end the portfolio were tailored to the wishes of some candidates.'

But Christine Loh misses the point when she sees a lack of coherence. The creation of political appointees who are to serve as top policy-makers, and report to him exclusively, confirms that C.H. Tung believes that he does not need any political apparatus to influence public opinion. It is a political vision that could have been challenged thoroughly on various political grounds. But it was not.

As for C.H. Tung, it is doubtful that he sees the system has an innovation, because the colony was run under a similar arrangement, where the colonial administrators were only answerable to the Foreign Office and the Governor. Furthermore such a system has many similarity with the system of management C.H. Tung know best, that of a company

C.H. Tung made clear that Hong Kong, in his views, is some kind of Fortune 500 company. The ministerial structure, with a board (Executive Council), a Chairman (himself), three Senior Chief Executives (Administration, Finance, Legal) and a retinue of Senior Vice-Presidents (the Secretaries) happens to be the structure existing in every company he can think of. The rest are details that the appointees have to sort out themselves to reach a better efficiency. He had no intention of dwelling on the details. Chairmen rarely do.

His admiration for the captains of industry is well known. Maybe the structure was discussed among the members of his Council of advisers. Maybe he asked Jack Welsh, Chairman of G.M., and the most admired C.E.O of the American business world to seat on his Council (that was before Jack Welsh's reputation went into flame during a bad divorce) what to do. Just because his Councillors were celebrated C.E.O of well-known companies (some of them being today in great difficulties), he might have been led to believe that they knew what sort of management structure was needed (4). But first and foremost, the ministerial system copies a structure he has practised over the years in his own business empire. He was back into a familiar landscape, or so he thought, and out of the world of the civil service.

But can Hong Kong, even as a world-city, pretend to be a company. The Chief Executive does not have to deal with productions and return on investments, but with perception and people. That is what politics is about. The question is does it really matter under a plutocratic system? It

is not certain that it does, since the Chief Executive is not constrained in the future by any electoral goalposts to secure his position.

Thus, what Christine Loh sees as an ill-thought reform was actually a rush towards a familiar world, with known parameters. The government of Hong Kong is now structured as Disney World or General Motors are.

C.H. Tung has made clear that he considers himself as a Chief Executive Officer. Rightly, his official title is 'Chief Executive', not Governor, like his colleagues in China. He has three assistants, a Chief Administrative Officer, akin to a Secretary General, Donald Tsang (his official title as we have seen is Chief Secretary for Administration), a Chief Financial Officer (Anthony Lung) and a Chief Legal Officer (Elsie Leung). They cope with eleven departments run by people that in a company would be the "Vice-Presidents" (their title is actually Secretary of the department).

Finally, C.H. Tung has his own board. No company could run without a board, and in the board you have executive directors and non-executive directors. In Hong Kong, the board is called Executive Council. He has no shareholders to report to but a watchdog: China. That he thinks he has no shareholders to report to should not surprise. He never had in the past to consider the opinions of the minority shareholders of his listed company OCCL. They were discarded as mere participants in something that was larger than themselves. Here the masses of Hong Kong have not made any difference in his outlook.

Hong Kong, in his view, is something larger than the sum of its parts, and the people are only, in his view, one of them. That is why he has a very peculiar notion of what "accountability" means. When the Financial Secretary, Anthony Leung, became embroiled into a scandal for not declaring that he had purchased a luxury car days before announcing a substantial increase in tax registration, C.H. Tung said that '*whether (Anthony Leung) made a declaration at the Exco meeting was relatively unimportant*'. He meant clearly that the Executive Council is not accountable to the public, but to himself, thus depriving the Exco of a political legitimacy. This means his perception of a system of governance is that he is the ultimate authority, and that between him and the public, there are no other public figures. The principal officials are his employees, not the employees of the public.

The community was doubtful from the first day of the introduction of the Ministerial system. Whether it would provide a more efficient and more accountable system of governance remains to be seen, but today the issue appears a moot one for his views as to what the government is supposed to do and to whom it is therefore answerable for its performance exclude the participation of the people of Hong Kong.

We are here at the heart of the matter. Hong Kong was a tale of mythical proportion that the British invented to prove that their colonial system was successful. It was a fallacy as far as they were concerned that had to last until 1997. Unfortunately, the elite adopted it as a truth. Nowadays, the people have yet to define for themselves what "successful" should mean in the future. In the meantime, C.H. Tung has asserted his views that "successful" means providing the elite with a high-level of return on their investments, as in the past. Hence the confusion among many who shy away from the political confrontation that seems inevitable at some point.

Christine Loh is one of them, who prefers to focus on details rather than on substance. She feels that C.H. Tung was as usual blundering. *'By tracking the history of how the portfolios were assembled and then reassembled, she says from the original proposed ministerial structure to the final one, it seems that there were no coherent views.'*

As we have explained, it was not so and does not really matter. He had a coherent vision. How the departments were assembled was a secondary issue. That environment was lumped to one department then switch to another, as she complained to backup her argument, was irrelevant. The view from the top was that whoever was in charge was to be accountable to the boss for whatever was in his or her portfolio. For a Chairman, such details had to be left to the subordinates, otherwise they would decline to endorse a responsibility that was forced upon them. The only issue was that they should come up with a management plan to improve the performance.

What was left aside by all the political actors of Hong Kong in their critics was what the performance should be about. In the absence of any political debate about the duties of the government, C.H. Tung imposed the view that it should be as in the past. It was a bold and cunning move in a way, as the public has yet to come to term with the facts that it has been mislaid not by C.H. Tung but by the British and the entire world as to what the government was about in the past.

As in the case of the housing policy that was his biggest innovation during his first term, C.H. Tung implemented his decision without paying much consideration to some of its practical consequences. In a way, it could be argued that his biggest weakness lies there. He is not a man to deal into details. It would not matter if he was surrounded by a good team. Unfortunately, that is not the case.

We should not be surprised by such a weakness. Businessmen are notoriously bad politicians, and scholars and civil servants have never been good at devising policies. Each has his pet ideas and vested interests, and none have broad based experience out of the Hong Kong mould. Governments are much more complex machines than companies.

It did not take long to bring to the fore a major oversight, which can only be understood in the Hong Kong context. When C.H. Tung presented his new ministerial system, the immediate focus was on the pay scale of the ministers. It was adopted without substantive oppositions by the legislators who, all of them, failed to point out that it was going to be a problem in the long run if the pay was linked to the civil service's one.

They missed the point because, officially, it was not. However, the salaries had to be set. Not surprisingly, the fraught logic underpinning anything in Hong Kong, that money means quality and quality money, was the recurrent song from all quarters, with no one challenging that assumption. As far as C.H. Tung was concerned, in due logic to the hierarchy that he was borrowing from the business world, the highest paid in the government would have to be the highest in the hierarchy. That is where things started to go astray.

Political appointments are not the same as business employments. Seniority is not what generally matters in politics. A forty-year-old politician can become a President, and be replaced by a sixty-year-old one. The President of United States earns a tenth of what he would earn in the private sector, and the same rule applies across the board. By agreeing that ministers

be paid a notch above the highest salary paid in the civil service, C.H. Tung had fallen in a trap laid by the civil service whose payroll is one of the biggest headaches Hong Kong has to solve (more on this when we look at the deficit).

In order to expedite the matter and introduce the system as early as possible, he did not consider the side effects of the decision or just discarded them as “insignificant”. After all, for a man whose private income is in the tens of millions a year, the numbers, in the range of two million, probably did not seem that impressive. Six months later, under pressure from Beijing to curtail the emoluments of the civil servants, he ordered a 10% cut for all his senior staff, including himself.

The blunder can be attributed to his oversight of the matter, or to a lack of political sense. It is rather a reflection of the lack of vision of his closest staff which should have perceived the ramifications of the issue.

‘Again it is a characteristic tied up directly to his managerial style and his staff, Christine Loh says. We all know that the civil service is a time bomb ticking away and today it is just at the heating up stage. And he forgot it.’

But even Christine Loh has to admit that C.H. Tung is not entirely a blundering caretaker. *‘To his discharge, she admits, he has not been entirely complacent. There has already been a lot of restructuring within the administrative structure. Departments have been merged and a first round of early retirement done and a second is on the way. But what we constantly see in Hong Kong is that problems are left to simmer until you have no choice but to tackle them. You ignore them as long as possible. So Hong Kong’s political life is some kind of pressure cooker.’*

Certainly, Hong Kong's political life is some kind of pressure cooker, and one gets the sense that the chief cook is C.H. Tung. By changing the landscape to suit his purposes he ruffles many feathers. That is the sure acknowledgment of a political agenda in motion.

That feeling runs contrary to the cliché that dissatisfaction exists because C.H. Tung is “not a politician”. However, his many decisions push Hong Kong in one direction (towards absolute plutocracy) rather than another (towards representative democracy).

That the majority of the people disagree with the direction is probably a fair assessment. Yet the political parties have failed to articulate this disagreement into a clear alternative. This is because their leaders keep aping the mentality of the former colonial elite. So far, blinded by the myth of Hong Kong, they refuse to expose many fallacies. In a way, they too are dreamers.

DOES CHINA CARE ABOUT THE ANTICS OF C.H. TUNG?

The local opponents of C.H. Tung are not the only ones to have a dire view of Hong Kong. The Prime Minister of China also joined the rank of the critics. Early in December 2002, during his last trip before his retirement, Zhu Rongji repeatedly said that the Hong Kong government was only dealing with administrative solutions to its problems while what was required was a political vision. It was the strongest statement ever made by a Chinese official about the performance of the Hong Kong political system.

Since 1997 China has been watching the development of Hong Kong carefully, most certainly with dismay. The Beijing government has been extremely cautious not to interfere with Hong Kong affairs and even the most ardent critics of the regime admit today that their fears were misguided.

Nevertheless, beyond the control of the Chinese central government, the Chinese factor still has a negative influence on the natural development of Hong Kong's system of governance. It was probably unavoidable. But how deep it affects the system is debatable.

'If someone asked me to describe Hong Kong today, says Alan Lung, the Chairman of the Hong Kong Democratic Foundation (HKDF), I would first emphasize that we are in China. It is a factor one has to recognize. We belong to a country and it is a new feeling for most of us, and a positive one. But we should not fool ourselves on our relative importance. The general feeling among our members is to admit that Hong Kong is very small. We have this comparison coming back all the time that Hong Kong is like the tail of the dog, trying to wag it but making little difference. It does not mean we are ignored. Hong Kong's values are relevant to China. The irony here is that we believe that the Chinese leadership has a better understanding of what those values are than our leaders. But to please the Central government we believe that we have to act differently. We think that we have to please them at all costs. I doubt it pleases them at all. In that respect, the attitude of the officials about the implementation of article 23 was a perfect example. I have serious doubts that the central leadership would have handled it the way they did. The first draft that was floated was probably harsher than what Beijing would have done. China wishes us well but we do not understand what it means. We second-guess our role and we mess up.'

We have seen what Alan Lung alludes to as regards the article 23 saga. But his views are not shared by everybody. For Emily Lau and her colleagues, as well as for Martin Lee, the former leader of the Democratic Party, Beijing acts in a more insidious manner.

'We have to accept the concept of "One country-Two systems", Emily Lau says. Our expectation is that under this concept Hong Kong will have a high degree of autonomy. Our Basic Law provides that we will have a democratically elected government, so we hope to pursue that goal. We fully realize that we need to have a dialogue with the central authority. The problem is that they don't want to talk to us. Some believe that China is not interfering into our affairs. Maybe, but I believe that we have seen a big erosion of the rule of law. The biggest blow to our independent judiciary has been the reinterpretation of the Basic Law, done by the Hong Kong government. I am convinced it was done at the instigation of the authorities although I can't prove it. However, at the time, quite a number of mainland members of the drafting committee of the Basic Law became vocal again to justify what was happening. They were putting pressure on the government to seek the arbitration of Beijing on the right of abode in Hong Kong, while I still consider that it was purely an internal matter and a fundamental right of the Hong Kong people. In the end, they won since the government overturns its own court to seek Beijing's views, and it was a sad precedent.'

The right of abode has been at the center of an emotional debate. Before June 1997, the British restricted the entry of Hong Kong in such a way that many children born in China but whose father was a Hong Kong citizen, were not allowed to live in the city. Since Hong Kong was no longer a British territory, but a Chinese city, the split families expected that their next-of-kin would be allowed to live in Hong Kong in a matter of months, the High Court having given the

green light for the abode seekers to stay as soon as they were in Hong Kong. Strictly applied the ruling would have resulted in the possibility of 560,000 people moving to Hong Kong without further delay and without proper control in China. A sense of panic developed among the majority of the Hong Kong population, and even among some of those split families as it was not uncommon for a businessman to have two wives, the official one in Hong Kong and the unofficial one across the border.

The main worry was that the sheer number of abode-seekers, most of them expected to be poor, would depress wages when seeking jobs and would flood the education and the health care systems. Indeed the administration declared that it would destroy the Hong Kong economy to receive so many refugees at the same time. It was those economic considerations rather than legal ones that pushed C.H. Tung to seek the arbitration of Beijing with a view to delay and administer in an orderly fashion the immigration of such a number of abode seekers. Beijing too was worried that the decision of the Hong Kong High Court would trigger an uncontrolled migration within China towards the border of Hong Kong. (Ironically, C.H. Tung is now pushing for relaxation in China of the rules of emigration so that Chinese high-income earners might be allowed to settle in Hong Kong.)

The case rapidly became politicized with the pro-China supporters agreeing with the decision to bring the matter to Beijing and the pro-democrat camp arguing that it was a litmus test of the independence of the judiciary, notwithstanding the fact that the final interpretation of the badly written Basic Law rests anyhow with the Standing Committee of the National People's Congress.

'That case highlighted the erosion of our civil liberties, insists Emily Lau. The unconditional right of abode was a basic right that was guaranteed under the Basic Law. Then the reinterpretation added conditions to it. It set a bad precedent and since then we have been sliding. To change the terms, for whatever reason, the proper avenue is to amend the law but then we don't even have a proper mechanism for that.'

Maria Tam disagrees. She was one of the drafters of the Basic Law and currently a Hong Kong deputy at the National People's Congress. *'The Court of Final Appeal had the option under article 158 of the Basic Law to refer to the Central Government and ask what exactly was meant, she says. Furthermore article 22 subsection 4 says that persons coming from the mainland will have to obtain permission to leave China and the number has to be agreed between Hong Kong and the Central government. They concluded that it had nothing to do with the article 24. That was wrong. We had in 1990 perfectly understood the situation and we had passed a resolution that had been agreed by the National People's Congress (5).'*

Emily Lau remains adamant. The government was wrong to bring the matter to Beijing, because it set a bad precedent. *'Some lawyers argue that even the method used by the government to bring the matter to Beijing was improper. The Basic Law does not provide for the Executive authority to go to Beijing directly. The Executive authority can argue its case for an interpretation during a hearing in court. This is in fact what the government did. But afterwards, because the government had lost the case, it took a second bite at it, taking the case out of the hand of our highest court. What should and could have happened was that, during the court hearing, if the judge agrees, the case be adjourned and Beijing asked for advice. Then the judge makes the final judgment based on the interpretation. The point is that the Basic Law*

does not really provide for the Executive to go on its own and ask for an interpretation whenever it suits the Chief Executive.'

Albert Chan, who was an early companion of Martin Lee for whom he has a lot of respect, has a much more subdued view of China than his former colleagues of the Democratic Party. *'The Chinese factor is much better than what was predicted, he admits. China has really surprised us. We were expecting the worst; therefore comparatively the central government has been quite fair. In most cases it did fulfil its promises not to intervene.'*

He also agrees with Alan Lung as to where the danger lies. *'The unfortunate thing is that some pro-Chinese people in Hong Kong stir China up into action whenever they want to get some support, he says. That is quite bad. The first person in that league that comes to my mind is of course C.H. Tung himself, but he is not the only one. There are a number of other influential Hong Kong people, not very well known to the public, owners of unglamorous but very successful listed companies, people with cross-border businesses peddling their influence whenever they feel threatened. I do not know though how the Central government reacts to that kind of pressure. Maybe it just ignores it.'* (6)

China, after the handover, worried that Hong Kong would be destabilized by a high rate of immigration and the drying-up of foreign investments, kept her promise and was thus out of the way as much as possible to let C.H. Tung build the credential of the "One country-Two systems". If on the political front, as we have seen previously the alliance with the civil service had produced result, the unexpected arrived in the most unexpected place: the economic front with a major home-grown crisis.

It was totally unexpected because China had been led to believe that the city was immune to economic crisis as long as the elite that made its fortune was in charge. China had been brainwashed into believing that the plutocrats could do no wrong, on the argument that they had an expertise that no one else had in China. To discover, it was a falsity must have been a terrible shock. It was of course a worrying development.

'Clearly the Chinese are watching us more and more, Christine Loh says, and what they see does not really please them. Zhu Rongji was very outspoken. What he said about supporting Hong Kong by all means was not new. He said the same on many occasions. But what was significant the last time he came was that he decided to come back on the topic several times without praising anyone as he did in the early days of the handover. That was a sign of how far we had fallen in his opinion.'

There is a saying in China: the less you talk about something, the better. In other words, the more one talks about you, the worse it is for you. In a way, Hong Kong is too often in the news for its own good. Constant controversies and arguments with its neighbors, about a bridge or a road, 24-hour-cross-border operations that took five years to organize, all the snipping between officials and the media did not make Hong Kong very popular among the Chinese administration, but this was vintage provincial grumbles that the central government has learnt to live with a long time ago. What was more upsetting was that public opinion was starting to turn against C.H. Tung. His approval rating, for whatever it was worth, was dangerously low. When such a thing happens in China, the government promotes or removes the Governor, but in Hong Kong, it could do nothing short of asking C.H. Tung to resign, which was not an option.

What was happening in Hong Kong was in clear contrast with what was going on in Macao that reverted to China in 1999. There was hardly any news about Edmund Ho, its Chief Executive. Macao was, in spite of the poor international economic environment which, according to C.H. Tung was responsible for the dismal economic performance of the city, booming. It was an indication either that Edmund Ho was a Superman, or rather that he had quickly integrated Macao into the Pearl River Delta economy (7). But that phenomenon had yet to be understood in Hong Kong.

In the early days of the C.H. Tung's administration, the central government of China made clear that it was quite displeased to see that the Chief Executive was criticized for one reason or another, not only by the democratic camp (that was expected) but by his own camp. Soon the message to the elite of Hong Kong passed to shut up and work together for a smooth transition. Anson Chan went to Beijing expecting to be congratulated to discover that she too was asked to shut up. Ultimately, China agreed to C.H. Tung's request to let her go when it was convinced that her forced departure would not jeopardize the public image of Hong Kong in the international media. Indeed, most of the world had lost all interest in Hong Kong. C.H. Tung, at last, could then take full control of the administration, with the expected result that Hong Kong would then be better managed. It did not happen.

C.H. Tung's popularity sank further. The chatter never stopped even among people considered close to China. It went on for months. The background noise had reached such a level that, by the time Zhu Rongji was coming, the central government had certainly started to admit that Anson Chan was not the sole culprit and that there was a more fundamental problem of governance. Hence the clear warning issued by the Prime Minister during his trip that tackling the perception besetting C.H. Tung's poor leadership by the introduction of the ministerial system was unlikely to bring improvements in the governance of Hong Kong if it was not accompanied by a political vision. Three months later, he was proven right.

As we have outlined so far, it is not in fact that C.H. Tung has no vision at all, but that his vision that we will study further on does not fit with a modern economy and a modern city. Hence the difference between his vision and what Zhu Rongji, the architects of the Chinese economic reforms, had in mind for Hong Kong.

It is in fact this difference between aspiration and reality that gives a sense of irrelevance. *'You can feel that Hong Kong is somehow directionless,* says Albert Chan. *There is no sense of leadership, or the leadership does not make sense, thus the lack of real long-term decisions on many issues. It will last until C.H. Tung has gone.'*

Could the ministerial system make a difference? Albert Chan, Christine Loh and Emily Lau don't think so. The most articulate on the reasons why it can't make any difference is probably Albert Chan. *'The majority of the so-called ministers are actually former civil servants,* he explains. *They have not changed jobs, but titles. That is the first difficulty. In order for the system to function you must have people with a common platform and a common ideology, not a group of individuals lumped together, who, a month before their appointments had nothing in common and no political vision. The way the ministerial system was setup, it is clear that there was no real common political objective. It is not that I doubt the ability of the five ministers who are not former civil servants. But to run a government, it is not solely a matter of ability; you have to share common belief and orientation, especially when there is a need to strike a balance between conflicting interests. You need a glue. People coming from the private sectors*

will have their views and it is welcome, but the others too will have their views. In politics, it is an ideology that is the backbone of a direction. C.H. Tung, by inclination, does not bring an ideology. So the direction will remain chaotic at best, until an ideology gives a sense of direction.'

James Tien, who leads a party supporting the Chief Executive, does not agree with Albert Chan. He believes the ministerial system could make a difference, but he admits that it is too early to tell. *'There are signs that things are moving in the right direction, he argues. For example, the mindset of the six former civil servants who are now ministers is already changing. While they are still protecting the civil service, they start to understand that their head is on the chopping board. Eventually, after a couple of years, such a mentality will sink in. The ministers have targets; in particular they must downsize the expenditures of their department. And there are signs that oversized public bodies such as the Housing Authority will shut down. It is a good idea because whatever that authority has been doing, it could have been contracted out. Therefore the shape of the government is changing and a new mentality will eventually sink in.'*

But there is obviously some wishful thinking in those remarks, for the authority of the ministers remains limited and frustration might come rapidly. They all have to work with the civil service that a cast-iron protection enshrined in the Basic Law put out of touch with realities. More often than not, they must be like the hero of "Yes, Minister", full of good ideas that are thwarted one by one by their permanent secretary. Without major political reforms, the ministers are quite powerless. As one minister lamented recently to James Tien: *'why do I have three thousand staff while I could do with a few hundred?'*

Therefore the biggest challenge for the system of governance is to be free from the interference of the civil service. It requires a profound change of mindset and a total redefinition of the civil service. Yet, although C.H. Tung has received China's backing to proceed ruthlessly if needs be to put back Hong Kong on an even keel, the deficit issue provided signs are that a reform of the civil service may never take place as long as plutocrats are in power. This is probably because to enter into such a process, one needs a clear political orientation. C.H. Tung has only the goal to maintain the traditional privileges of the Hong Kong elite. Such a goal does not deviate enough from the goals of the civil servants to distinguish himself from their mindset, for they are the best guarantor of the status quo. The ambiguity that lies at the heart of the relations between the plutocracy and the bureaucracy is now coming to the fore because of the public deficit.

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Chapter 3

- 1.- Speech during the Fortune Forum October 2002 - Hong Kong.
- 2.- "DAB" stands for "democracy" and the "betterment of the Hong Kong society". According to the party manifesto, the DAB logo gives expression to its determination to contribute to the democratic development of Hong Kong, and to build a better place for everybody to live in. The logo symbolizes the readiness of the party to embrace the return of Hong Kong to the motherland. The party was set up in 1992. It was during the 1990's presented as a pro-China party. In view of the poisoned atmosphere Chris Patten had created towards China, its electoral success in 1998 came as a surprise as it was expected to fare poorly. The true reason for its appeal was that it positioned itself as a grassroots party as opposed to the Democratic Party, which was popular among the Westernized population of Hong Kong.

3.- The Democratic Party was established formally in 1994. It was born out of the merger of two other parties, the United Front and Meeting Point. It can be said that it was the first fully-fledged political party of the colony. Its leader was Martin Lee, a successful barrister, who was presented as the champion of democracy against the repressive Chinese government. Albert Chan, who is extensively quoted in the book, was a founding member of the Democratic Party. A popular legislator, he has left the party when Martin Lee, who could not be re-elected Chairman of the party, was replaced by Yeung Sum, an university lecturer in a process that was less than democratic.

I respect Martin Lee, he says, but now (in 2003), the party has considerably changed. It have always resented the secretive manners that led to its formation in 1994. A small group led by Martin Lee and others decided that it would be better to form an united front of democratic minded members. UDHK (United Democrats of HK) and Meeting Point met secretly Martin Lee and others. I was not informed at that time, and suddenly out of the blue we had this coalition. The grassroots members were very angry. They were right to be angry and to accuse the leadership of undemocratic manner. The merger was done in a very high-handed way. Nevertheless, because 1997 was looming ahead, nobody wanted to be accused of undermining the democratic coalition. So no one left, but the seeds of dissent had been planted. There is a fundamental difference between the two groups. Meeting Point membership was mostly among the academic world and the non-governmental organizations, while the members of the United Democrats had less formal education and were from the grassroots. It is not the same mindset. If one use the analogy of a marriage, it was a blind one. I had the feeling that it would fail in the long run.

Over the years, I criticized and made strong statements here and there, but respecting Martin Lee's leadership I did not leave the party, although it had absolutely no input in my electoral campaign. Then about tow years ago, I was asked to leave with a number of others. The media called us the young Turks, but really very few were young, and we were rather old-timers. Martin Lee was not even aware that we had been asked to leave. He patched up things for a while, but today 80% of the young Turks have left. By Hong Kong standard, they had a long experience of Hong Kong politics. It left the party all the more poorer. Those people were committed especially in Hong Kong where the choice was between a career and politics, especially when you know you are not going to be a ruling party for a very long time if ever. I was disappointed to see that some of the key party members did not appreciate their works and were just happy to let them go. I thought what kind of a party is this? The last straw came when I learnt in the newspaper that Yeung sum had agreed to be the leader of the party. There had been no process, no vote. It was a back room arrangement. I became not only angry with the party but totally disillusioned. None of the committee members had discussed with me about the change of leadership or the future direction of the party. It was the work of a small circle. There was no dialogue or communication before the general meeting of the party. Everything had been lined-up. That was the way actually the party operated for the past few

years. There is a small clique, the so-called ‘mainstream’ that believes that there is no need to speak with those members who have different views. They just ram through their ideas. The party being small and getting smaller by the day, whenever they want a vote, they get it their way. I decided that it was time to go. The party up to now has been unable to operate as a true political party, with what one would call political ambitions. I have been saying that for years. I was expecting things to settle down after 1997, to become more professional. The handover had gone and we had to learn from what had happened. But the party was not prepared to learn anything. It kept issuing blind criticisms of the government public policies. It just wanted to pressurize the government, but it failed to operate as a political party per-se, with a social conscience. I have now resigned myself today that it will never do, not under its present leadership anyway. The party has forgotten that it needs to focus on its electorate, on organization and mobilization. The Democratic Party has less and less the ability to move people. Ask the party to mobilize two hundred people for a specific issue. It can't do it. After so many years in public life, it is quite ridiculous. It is a sign that the party is going in the wrong direction. When the Democratic Party was formed I had a lot of reservation, so what is happening now is not surprising. My commitment was with the UDHK, now the party is lost in the wilderness. Four years ago, we had to define what in terms of social orientation the party would be. It was said we will fight for the middle-class, because the DAB is extremely good among the poor. But in actual fact, the party does not know what the middle-class is, or does not want to be part of it. I raised the issue of the negative asset holders. The most affected by this tragedy is the middle-class. The party should take up the issue and fight the government for its disastrous and careless housing policies. I was told not to support the claimants. I said I would do it as a private citizen, not as a legislator from the party. I got criticized for that. But what has the party done for those people? Nothing. It can't get its act together. Its immediate concern is just to prepare the re-election of a few of them in their constituencies. The party has lost its conscience.'

Not surprisingly, the memberships of the Democratic Party collapsed after 1998, as it is neither a grassroots party nor a middle-class one, and in the upper spectrum the Liberal Party is now starting to get established. That leaves the Democrats with no real constituency among the Hong Kong population.

- 4.- C.H. Tung has established a Council of International Advisers as soon as he was in power. There are currently 19 Advisers. The Executives that have been nominated represent the following companies: Intel Corp, Siemens, Llyods TSB, ABN-Amro, Power Corp Canada, Oracle, Motorola, AIG, Unilever, AOL Time Warner, Suez, News Corp, Goldman Sachs, with four retired Executives from HSBC, GM, the US Federal Reserve, Bank of Tokyo and Toyota. The Advisers are supposed to meet once a year in Hong Kong but very few have attended regularly. Some have never been to the annual meeting. The legislators have criticised the exercise as a publicity stunt and a waste of taxpayers money. Indeed, it is doubtful that the contribution of the Advisers is in any way relevant to the Hong Kong situation, as among them, only Williams Purves, the former Chairman of HSBC, has worked and lived in Hong Kong in the past (he was actually an Executive Councillor as the Hong Kong Bank was the acting monetary regulator of the British administration).
- 5.- In Asian Affairs n°7 (vol 2 n°3) – Spring 1999 – Interview with Maria Tam, Hong Kong elected deputy at the National People's Congress. Maria Tam, who was a member of the drafting committee of the basic Law, emphasized that the article 24 was written in 1990 before the concept of right of abode was completely delivered. She accused the Court of Final Appeal of Hong Kong of ignoring three facts in its judgment in favor of illegitimate children, the first one that the joint-liaison group had already looked into the issue, the second one, that the preparatory committee had already passed a resolution which had been accepted by the National People's Congress and thirdly, that the provisional Legislative Council had already passed a law to restrict the right of abode. She accused the Court of Final Appeal of trying to define its territory in its first ever judgment to the highest possible limit of its judicial

authority, disregarding the article 158 of the Basic Law which provides for the Central government to be seized in case of confusion as to the intent of the law. In the same interview, Maria Tam admitted that the government of Hong Kong did not know how many cases it was dealing with but that the number was staggering. One government official mentioned in the media that more than 1.6 million people could be entitled to the right of abode if the ruling of the Court of Final Appeal was upheld. The number was an extrapolation based on the fact that there were 520,000 people born out of wedlock that benefited in the first place, and that their children might benefit as well. Currently, more than 150,000 people have been reunited.

- 6.- It is interesting to note that when the Chairman of the CPPCC, Li Ruihan, came to Hong Kong on November 7, 2002, the Chief Executive, C.H. Tung invited to a reception 150 personalities. Not all legislators or political figures were invited, and close to a hundred of the selected group were businessmen with no official functions in Hong Kong. Yet, Li Ruihan was visiting Hong Kong in his capacity of n°3 in the Chinese political hierarchy. Albert Chan, Emily Lau, Martin Lee and many other well-known political personalities, directly elected by the Hong Kong people, were not invited while wealthy businessmen were.
- 7.- Furthermore Edmund Ho and his team have been quick to open up Macao's casino industry, still the main source of income of the city to outsiders, forcing an overhaul of an industry tightly controlled in the past by Stanley Ho. To have a similar overhaul in Hong Kong would imply that the Jockey Club be dissolved to let the same industry be awarded by open tenders to two or three companies rather than one. C.H. Tung went the other way. When the government decided to legalize soccer gambling, it awarded without competition the franchise to the Jockey Club, entrenching further its monopoly.

CHAPTER IV - THE DRIFTING BOAT

4.1. - THE QUEST FOR THE PAST

4.2. - THE C.H. TUNG'S GOSPEL

4.3.- A CARELESSLY ENGINEERED CATASTROPHE

4.4. - THE DEFICIT CONUNDRUM

4.5.- THE LOPSIDED TAX STRUCTURE'S POLITICAL DIMENSION

4.6.- DILLY-DALLYING WITH THE CIVIL SERVICE

C.H. TUNG'S QUEST FOR THE PAST

In C.H. Tung's vision, Hong Kong owed its phenomenal economic success not to opportunities that presented themselves one after the other at its door, such as the embargo against China in 1949, which delineated its own world-economy, the Korean war which filled the coffers of some families, or the Vietnam war with the same result, or ultimately the open door policy of Deng Xiao-ping, but to the wisdom of its merchant elite.

That the merchant elite was in control of Hong Kong after the departure of the colonial power appeared not only legitimate, but prudent, for it had the knowledge and the ability to keep it successful. An important consequence of such a belief was that Hong Kong would be nothing if not for the competence of its plutocracy.

That it is entirely a fantasy does not really matter, for the strength of one's faith in a myth is always based on the power of imagination. After all, we have always admitted that a thing is said to be explained when we can classify it with other things with which we are already acquainted. Thus C.H. Tung explains Hong Kong to his own satisfaction every time he classifies it along with London or New York.

Distortion and manipulation of data to an end is not the privilege of Hong Kong. Well-chosen statistics can lie. In Hong Kong, with a weak system of balance and check, where the bureaucracy has for so long been used to being insulated from the needs of the indigenous population, it is not surprising that reality has all but disappeared.

For that reason, it is also excessive to believe that C.H. Tung happens to be a conservative solely by natural inclination. It is more probable that he is so fascinated by the story of Hong Kong that he does not want to change it. He sees no reason to alter its system of governance because, from the perspective of the myth, it delivered a successful strategy.

The goal then becomes evident. Changes are a source of danger. They should be entertained as a last resort. One should never be pro-active. The future is in the past, so to speak.

As an administration is adverse to change, there is always a common ground and a meeting of minds between plutocrats and civil servants, whether in Hong Kong or in other communities dominated by their elite. Changes are regarded by both not as a positive development but always as a dangerous undertaking. If they can be avoided, they should be, regardless of any other consideration.

Unfortunately, two fundamental facts conspire against the status-quo and the quest for eternal youth. The first one is that Hong Kong is ageing and it is an irrevocable process. The second fact is that the wealth disparity of the city is, sooner rather than later, a recipe for social disorders.

As regards the nature of the city, C.H. Tung has not yet understood that Hong Kong has no chance to remain the world-city it was. This is because his knowledge of the attributes of a "world-city" remains quite limited. From his discourses and actions, it appears that he believes that a world-city is defined by its competitiveness. It is not so. A city becomes indispensable an

thus acquires the status of world-city for a variety of reasons that cannot be reduced to monetary considerations.

Many analysts took comfort in the fact that C.H. Tung has been a forceful exponent of the necessity for Hong Kong to become competitive. Unfortunately, he has yet to use the argument genuinely. For the time being, it is merely used as a fig leaf to cover the true reasons of the current deflation. To give a positive spin to a negative development engineered by careless policies in the late 1990's, C.H. Tung presents "competitiveness" as the key to return to prosperity.

But to believe that Hong Kong became a world-city because it was more efficient and better at managing opportunities is about as misguided as his housing policy was. Yet he is unlikely to change his opinion on the matter because, beyond the validity of the claim, it is the legitimacy of the elite as the rulers of Hong Kong that is at stake. Only if Hong Kong returns to its old former glory, could it be justified that it is ruled as it was in the past, that is without public participation in the business of the government.

The constant surveys paid for by the government to reputable consultants to justify that Hong Kong is competitive, remains ahead of Shanghai and is better than any other city, except New York and London (a little modesty gives some credibility to the rest of the claims) (1), have only one purpose: to provide the necessary proof as to the validity of the paradigm that only the elite has the competence to run the city. If the elite could prove that Hong Kong remains Hong Kong, it would prove too that to transfer the power of the Governor to a Chief Executive was somehow justified.

But those surveys prove little. They mainly deflect the attention on the real issue of anti-competitive practices within the domestic economy.

Competitiveness is a much-debased concept. There are no scientific works behind high-sounding indices that purport to rank the different regions and cities in terms of competitiveness. All of them use entirely different criteria. All have little to do with the real state of the city and its community. Most target only trade figures, investments in financial instruments and transnational companies.

It would not really matter, were it not for C.H. Tung to devise his policies with no other a view than climbing up the ladder, with little regard to realities that affect the livelihood of the majority of the population. Indeed, what does it matter for the people, if Hong Kong is ranked with the best airport of the world when it takes hours back and forth from their job place to their home because the government would not invest in subway lines (while Guangzhou invested recently in three new lines), when they can't live in a clean environment because discarded containers and rubbish are everywhere in the New Territories (because the land regulations are in a shamble), when Lantau island is cut in two because there is no decent road to go from north to south (because the government would not invest in a tunnel deemed to be too expensive), when there are not enough public car parks because they are not built (ordinary people are not supposed to buy cars and the absence of public facilities can only discourage them from doing so)?

Notwithstanding, C.H. Tung is quick to point out that Hong Kong has risen from being the tenth largest trading entity in the world to the ninth, as if government policies had anything to

do with that performance. Such a rise has, as we all know, little to do with Hong Kong and a lot more to do with China, since 80% of the Hong Kong trade is to or from China (2).

Fernand Braudel, looking at the characteristics of world-cities, has visited the competitiveness argument more than once and expressed his skepticism about it. Hong Kong would furnish him further reasons to dismiss the Ricardo theorem as a charade.

If competitiveness was by essence a key element of trade pattern, then one would agree that Hong Kong, year after year the top spot as the largest container port of the world, handling in 2002 18.6 million Teus (20ft equivalent units), must enjoy a competitive advantage. It certainly has, but it is not linked to cost-competitiveness as a recent report issued by Civic Exchange, the think-tank run by Christine Loh outlined.

In it, her think-tank exposed that Hong Kong's terminal handling charges (THCs) are the highest in the world. After its publication, a legislator from the Liberal party, Kenneth Ting, questioned the government's wisdom to let the franchised port operators and shipping lines work at a 40% net profit margin, a level that a competitive environment would not allow.

Table: Terminal Handling charges HK\$ per 40ft container

Port	US	Europe	Asia
Hong Kong	2855	2750	2650
Shenzhen	2087	2100	2087
Taiwan	1589	1450	1386
Singapore	1170	1020	1170
Japan	936	2680	1030
Indonesia	1557		1557
S. Korea	891	840	891
Malaysia	880	710	880
Thailand	718	710	718
Shanghai	680	180	175
Philippines	113	340	669
Germany	1110	-	
Netherlands	790		

The worrying trend for the elite is that the geographical advantages of Hong Kong are in fact waning. Shenzhen, its neighbor that had no port that could compete with Hong Kong in the 1980's has been handling more than 7.6 million Teus in 2002 (+49%), and is expected to handle 11 million Teus by 2005 and 18 million by 2010. It is launching a new terminal that would have a further 8 million Teus by 2020. Shenzhen is already a larger container port than Los Angeles, and Shanghai has leapfrogged Kaoshiung to become the fourth largest container port of the world.

Some members of the elite have already drawn their own conclusion and are starting to move out of the fortress Hong Kong. One of the biggest investors in Shenzhen facilities is Li Ka-shing, who already controls 50% of the Hong Kong port facilities. Another mythical tycoon of Hong Kong, Henry Fok, is now investing in a container terminal in Nansha, an island just nearby Guangzhou. For that reason, he is resolutely opposed to the construction of the bridge

between Macao and Hong Kong. The bridge would undermine his strategy by driving more business to Hong Kong while he sees no future role for the city in the development of the Pearl River Delta.

This above facts points to one reality. The only competitive advantage Hong Kong ever enjoyed was to be the only port available in the 1980's and 1990's with the appropriate facilities to handle large ships. Trade patterns have always evolved around convenience rather than costs.

Shipping costs are not the only area where the rule of competitiveness reduced to cost advantages looks like an empty formula. The airport of Hong Kong has enjoyed in 2002 the best year of its short existence (it was inaugurated in 1997). It registered a record 19.6% growth in cargo at 2,48 million tons. Yet, it is a far more expensive facility than the Macao, Shenzhen, or Guangzhou airports. The trade pattern here is related to aviation rights rather than costs, since even for the cargos going to China it would be more convenient to use a Chinese airport in the heart of the Pearl River Delta.

Nevertheless, it is of fundamental importance for C.H. Tung to keep telling the Hong Kong people that 52 months of deflation have "improved" the competitiveness of the city. It gives a reason for it and deflects the attention as to the true cause of the economic collapse. It also offers signs of hope under the flawed inference that Hong Kong by getting its costs down will again be a world-city. The public is left with the conclusion that it is good for the future (3).

Thus C.H. Tung's vision of Hong Kong's future has so far little to do with the reality. Projecting the flawed assumption that competitiveness was at the core of the city's past success and the reason behind its world-city's status, he furthers the idea that the domestic economy would somehow become an extremely competitive one the day it is a cheap one. This is an unproven assumption, and in any case a fallacy as far as Hong Kong is concerned.

Some might be tempted to conclude that due to a lack of understanding or a poor judgment, C.H. Tung rushed to the wrong conclusions. However, the Chief Executive, of all people, is probably in the worst position to evaluate the difference between reality and delusion. Admittedly, being a beneficiary of the system, C.H. Tung, like his peers, is unlikely to investigate the myth upon which his privileges were built, but even if he was inclined to do so, his main informers on the state of Hong Kong remain the civil servants who devised the myth of the city. They too are unlikely to discern where the fantasy starts and thus are totally unhelpful.

But not all the elite is as insulated as the Chief Executive is. James Tien says that many among the businessmen are starting to feel that Hong Kong is more or less going awry. And although a member of the elite, his propositions read increasingly as an indictment of the system.

But whose fault is it, if the system is in disarray?

'In my view, the people are complaining too much, James Tien ponders. Our level of education is quite low, far behind Singapore or Taiwan. So, we don't really deserve our status.'

'Hong Kong was really above what it should really be' he says. That is a recognition, albeit an indirect one, that it was all a myth, isn't it?

That a myth would eventually collapse is inevitable. In Hong Kong, it took five years only for it to be punctured badly on two accounts: the quality of its civil servants, and the size of its government.

C.H. Tung has yet to admit squarely what James Tien says openly. If he was doing it, turning away his government from the myth, he would then give a sense of direction and legitimacy to his actions. But there is a dilemma. The elite has been an ardent supporter of the myth in the past. It never thought that it might one day have to account for it. If it does, then what would be a legitimate justification for its hold on power? As long as the question is unanswerable, it is better to cling to a fiction.

In the 1990's, for political expediency, the British coined two slogans to wage their war of words with China: the local administration was the best of the world (the implied meaning was that the Chinese one was the worst of the world) and the colony was run by a small government (meaning the Chinese one was a big monster). Such claims, as we have seen, do not now stand close scrutiny. The colonial system was as chaotic as elsewhere.

The elite went along with the British fantasy, yet they knew first hand that the only concern of the British government was that Hong Kong should not cost a penny to the Treasury, and that Hong Kong Bank, Jardine and Swire, to name a few old "Hongks" kept their privileges as long as possible (4) as they were generous contributors to the British political system. The elite knew how the British governors, one after the other, devised several ways to pursue such a goal.

The merchants too knew that the colonial administration had always been interfering everywhere. They could have exposed that, when the basic rule in Hong Kong was that everything was forbidden unless authorized by legislation and administration rules, Hong Kong could not be run as a modern and efficient economy. The elite could have exposed that the list of regulations restricting intercourse was, from growing pineapples (to protect a Jardine monopoly), to al fresco dining or the construction of balconies in more than one side of a house, indeed a very long one that was affecting the natural development of the economy of Hong Kong in an unacceptable manner.

The elite knew that the success of the colony was recent. Most of the fortunes were made between 1954 and 1990. Hong Kong has been a British colony for close to a hundred and fifty years, but it is only after the 1980's that it reached the status of a world-city. The elite knew it did so by chance.

'The development of Hong Kong is the result of coincidence, says Albert Chan. When Mao took power in China, Hong Kong had no capital and was a dire city. The embargo in 1949 was a great boon, and then we had the Korea War, the Vietnam War, the Cultural Revolution, all these historical events playing in favor of Hong Kong. Finally Deng Xiao-ping started the open door policy in the late 1970's. All these events had nothing to do with the Hong Kong colonial administrators. What was happening was that external developments elsewhere served Hong Kong very well. The truth is that the British never had any economic plan for Hong Kong in the first place. Hong Kong grew into a world-city because of historical circumstances. What happened was not the product of a grand design. The colonial government did nothing wrong or right. It just kept out of the way and did not interfere with the merchant elite. How could it anyway? Everything was happening outside its control. Nevertheless the British took the credit for everything and some misinformed people believed them.'

The local business community even with 1997 looming at the horizon had little time for any political vision. *'I try to convince them to take a close interest in politics, says Emily Lau. But they said they were too busy. In fact, they were used to their back room deals with the government and they believed that after 1997 it would remain the same. I am not sure it is. In any case, it is important that they participate in public life in an open manner, so that problems can be argued publicly.'*

It is probably vanity that got the better of the business community. In the end, it went along with the British story on the assumption that the myth could not do any harm. In any case, the immediate dividend was to ingratiate itself with China.

Such a lack of foresight now has a price. Hong Kong being in the doldrums, the system of governance has lost its legitimacy. China, under a delusion for five years, has started to reckon that the city is badly managed. More importantly, it certainly has growing doubts that the elite has any understanding of its management at all. It may conclude one day that the price for stability has been too high and that Hong Kong has now to face the future. The deficit issue might just speed up the day of reckoning.

THE C.H. TUNG'S GOSPEL

'The economic situation we are facing is severe and unprecedented in decades, C.H. Tung said in January 2003. First, despite the recent signs of economic recovery, deflation over the past 50 months has accumulated to 13%, and there is no indication that it will disappear in the short term. Confidence in local investment and consumption has suffered. For some, incomes have continued to drop. Second, people's wealth has shrunk with declining asset values, with some facing the hardship of negative equity. These distressing consequences have become more obvious in recent years. Third, economic contraction and restructuring have led to changes in the employment structure and resulted in increasing unemployment, a prime concern of the community.'

Because C.H. Tung has always dismissed the idea that the economic downturn in the domestic economy might have been triggered by one of his own initiatives, he is left with no other cause to justify a prolonged deflation and a collapse of the property prices than saying that Hong Kong became addicted to some irrational economic exuberance, which actually is an intrinsic characteristic of a world-city.

'For various reasons, a bubble economy emerged in Hong Kong, he further argues. It gave rise to superficial prosperity, driven by the combined effects of surging asset values, wages and prices. This in turn led to inflated costs, which seriously affected people's livelihood and weakened Hong Kong's competitiveness. Many of our citizens speculated on stocks and property and this "quick money" mentality undermined their entrepreneurial spirit.'

That description is of course exonerating the elite of any responsibility in the process. Notably, C.H. Tung is making a difference between the "quick money" mentality and the other one, the benevolent mentality that is the hallmark of the elite. Thus, the elite is blameless. It would never ramp up prices beyond what is reasonable. As James Tien is quick to say *'People are unreasonable. They expect too much from Hong Kong.'*

There is only one problem with C.H. Tung's explanation. It is entirely fictitious. As Stephen Brown, the head of research in a brokerage house of Hong Kong pointed out, the re-export business rose threefold between 1990 and 1997. That was not a figment of the imagination but the result of the migration of the Hong Kong factories to the mainland in the 1980's. Thus an enormous amount of capital was transferred to China in the preceding decade and the 1990's were payback day. It was in the 1990's that Hong Kong switched to a service-oriented world-city and during that period the GDP doubled. That was hardly a superficial economic performance or as he said "a bubble" that had to be punctured.

But by claiming that the economic performance was a mirage, C.H. Tung lays the ground for his next fictitious conclusion: that property prices were a mirage induced by speculators. Whether they were too high is furiously debated. Many think so, mostly on the basis that by comparison to other places, they don't make sense.

But as Fernand Braudel wrote, world-cities have their own rules. They only apply to them, not to others. Property prices in Hong Kong compared to other world-cities are not that high. What really matters is that C.H. Tung attributes the pricing to speculative activities while it was the result of politically motivated decisions. The British were quite good at extracting as much as they could from the fact that the government was the ultimate owner of the land. On the other hand, his government made an appalling job at it as we are going to see.

Land prices in Hong Kong always had little to do with the external forces of the global economy, but everything to do with the characteristics of a world-city and the level of control of the elite or the colonial power over it. The British system of land tenure, where the ultimate ownership of the land always remains with the Crown made it easier for the British to devise a cunning way of extracting money from the fact that everyone needs a home.

James Tien attributes today the imbalance between the supply of land for housing and the demand for homes to the Sino-British agreement of 1984, that restricted the sale of land to the public to 50 hectares a year (with 50% of the proceeds going to a land fund) at a time where the population was increasing rapidly.

'There was no mechanism to revise the 50 hectares' rule that remained in force for 14 years, he explains. It would have been wise to link it to some kind of population index so that the supply could be adjusted to the demand, but it was not done or discussed. Inexorably the prices of properties went up. The spillover effect was to trigger inflation. Salaries started to skyrocket to keep up with speculative gains made by your staff. If someone was making ten thousand dollars a month working for you and, thirty or forty thousand through speculative activities, it was hard to discuss. People jumped jobs like there was no tomorrow. All sectors of activities got infected. Business people that were not developers started to add such an activity as a source of income.' (Actually, his family empire did just that, switching from the garment industry where it remains a major actor to real estate development where it is a minor player).

That chain of events, although plausible, distorts the reality. It leaves aside the main reason behind the rise. It was not a physical shortage of land that triggered the process, but an artificial one. The government could have curbed the price of land any time by various administrative means, or by investing in a complete revamping of the land system, allowing for example the owners of existing land plots to redevelop them as they saw fit. If such measures had been adopted, the law of the market would have prevailed, but it would not have served the purpose

of the government, which was to extract as much money from the Hong Kong people as it could before 1997.

The British had clearly understood that pricing in a world-city was not an issue. Competitiveness had no bearing on the role of Hong Kong in Asia. Hong Kong was Hong Kong for being Hong Kong, at the right place at the right time. Admittedly prices were very high because they were expressed in a dollarized currency, but they had no effect on the economic development of the world economy surrounding the city, which was what mattered. On the contrary, they were increasing the value of the collective wealth of the community held by the government.

Yet, C.H. Tung is adamant. *'No place on earth, however well endowed, could sustain a growing bubble over a long period of time, he argues. The question was no longer whether a crisis would strike, but when, how serious and for how long. The Asian financial crisis in 1997 punctured the bubble, precipitating our economic reversal.'*

Not only is his assessment wrong, but C.H. Tung does not see that he contradicts here his own pet argument that Hong Kong was and remains a world-city. World-cities can sustain their own bubble as long as they remain the heart of their world-economy. If their world-economy crumbles, as was the case for Venice, Amsterdam or London at some points of their history, then, indeed the bubble deflates, but it never happens before. What makes the case of Hong Kong peculiar, and therefore what points to another cause is the fact that the world-economy of Hong Kong kept performing so well that its own growth started to be delinked from the economic performance of the city. It is all the more obvious that Hong Kong struggling with negative to nil growth for the past couple of years is surrounded by cities that keep registering double-digit growth year after year.

'The besetting sin of these pulsating capitalist cities was their high cost of living, Fernand Braudel wrote, not to mention the constant inflation resulting from the intrinsic nature of the higher urban functions whose destiny it was to dominate adjacent economies. Economic life flowed spontaneously towards their high price.' Indeed, history books will remember Hong Kong as a world-city in the twentieth century because property prices were by far the highest of Asia.

As soon as the British government could, it started to extract as much capital as it could from the only asset of the colony, its land. As a result, in all its short history, the city has always been to an absurd proportion more expensive than any other place in the region. That had been the case before of Venice, Genoa, Antwerp, Amsterdam, London, or New York. When it ceases to be the case, then the reasons to remember a world-city slowly disappear.

Who today remembers that the most expensive city of Asia in the 1820's was Macao? In fact, by asserting that the Hong Kong property bubble was no longer sustainable in the long term and therefore the current crash was inevitable, C.H. Tung did not see that he was claiming that Hong Kong had lost a fundamental characteristic of a world-city, while he actually thought he was laying the ground to justify a return to this glamorous status. The error could not have been greater.

There is little substance in the claim that Hong Kong could not sustain its property prices past 1997 on the ground of economic considerations or affordability. Property prices in a world-city

were as much a matter of prestige as the result of draining within the city wealth that had been created far away.

What we learn from the explanation given as to the causes of the "unprecedented crisis", is that C.H. Tung and his team have absolutely no knowledge of what a world-city is. While he and his team see a five-year deflation period as a positive development on the reasoning that it might increase the competitiveness in the long term, which in turn would maintain Hong Kong's status as a world-city, it is in fact the reverse that is likely to happen. By the time deflation is over, other cities will become more expensive than Hong Kong and yet attract economic flows as Hong Kong did in the past. Hong Kong, it must be forcefully argued, cannot be cheap and a world-city at the same time. It is either one or the other.

But does it matter for the population? Actually not, the people would probably be better off if Hong Kong had no other ambition than to be a pleasant, modern and environmentally friendly place. But that would not satisfy the elite who has much to lose if Hong Kong becomes just another city.

The second inference brazenly presented by C.H. Tung is a link between the Asian crisis and deflation. Like the first inference, that one does not stand scrutiny, denying the role of the peg as an efficient fire-wall against contagion. It is all the more strange, that C.H. Tung engineers the protection of the peg at the height of the speculative fever among currency traders. If the peg had collapsed as a result of such speculative attacks, then he would probably have a legitimate case to present to the public as to the role of the Asian crisis affecting directly the domestic economy, but the attack failed for reasons that do not need to be looked at here.

If on the purely economic angle, C.H. Tung's explanations make no sense, they can only be understood in a political context. In his statement, he did not intend to analyse the "unprecedented crisis" on economic grounds. He could not do that because that would mean discussing the reasons behind the collapse of the housing market and they would point out to his wrong decisions on the matter. As the admission of a mistake would challenge the omniscience of the elite, at the heart of his legitimacy, it would be a dangerous course to pursue.

It is however difficult to assess whether C.H. Tung believes in his own rhetoric on the matter. Subsequent events seem to prove that he has realized how fundamental the pricing of the housing market was for the future of Hong Kong but whether it is because of the correlation between the status of a world-city and this factor, or because of the budget deficit is unclear.

It is of course politically impossible for him to declare that a return to an artificial shortage of land is advisable, but as we shall see, the foundations have been laid once again for such a practice.

A CARELESSLY ENGINEERED CATASTROPHE

As we wrote earlier, land and property prices in Hong Kong have never been the result of a property market that would have been free of political consideration. The price of a piece of land or a small flat, anywhere in Hong Kong never had economic rational. It was not the result of supply and demand but the consequence of a carefully crafted policy to extract as much money as possible from the people. It was a matter of public policy.

When Hong Kong became a colony, the crown assumed ownership of all the land, and therefore in later days, became the sole supplier. This was in line with the primitive practice of getting wealth through the sword. That practice was recognized in those days as the only honourable source of wealth.

To further control the market, the government introduced a variety of rules and zoning regulations, all designed not to serve the interests of the community at large but solely the Treasury.

It is easy today to blame C.H. Tung for being unaware of the situation. Yet, before the Asian financial crisis of 1997, his current critics were among the people arguing that Hong Kong had a tight land bank and a large population. Economists were quick to deliver wonderful graphs where everyone could see that the supply and demand were going in opposite direction. Even today, people like James Tien explain the current downturn by blaming the Sino-British agreement for limiting the supply of land to 100 hectares a year for 14 years, which was obviously too little.

Taking as true another fallacy, C.H. Tung is likely to have worked out that the Hong Kong people were not buying flats because none were available or affordable. His judgment was impaired by a belief common among the elite that land-related ownership is the ultimate goal of the poor. He then came to the wrong numbers and the wrong decision.

Some might think that the mistake is further proof that the leadership of Hong Kong is of an exceptional political incompetence, but there is another way to look at the rational surrounding his flawed decision.

The mindset of the Hong Kong elite has always been quite similar to that of the elite of Europe at the time of Charles Dickens. While the city is in all appearance a modern one because of a plethora of sky-scrapers near the harbour and the financial center, it is in fact a community of people living in a time-warp, its social and political covenant being quite close to the one prevalent in bygone days where class distinction was an accepted god-given fact. The problem of the housing market in Hong Kong derives from it. Compounding the error was the fact that social inequality has always been an essential component of world-cities.

Class distinction no longer expresses itself through land. But it did for a very long time. In the case of Hong Kong, it still does. This is probably due to the fact that the colonial merchant elite of the city acquired wealth not through the noble art of killing the previous occupant of the land it possessed, the honourable way for an aristocrat to become wealthy, but by being drug-dealers and smugglers. No matter how wealthy the drug-dealers became, they would get less respect than a penniless aristocrat, until they became landowners, which would transform them into "colonial" aristocrats.

From a practical point of view, this attitude allowed the colonial government to create a myth, that of the scarcity of the land. The logical inference was that land was an expensive commodity because it was in short supply. It was a charade but over the years, it became an absolute truth. It was of course a big lie. 80% of the Hong Kong land remains underdeveloped and could have been put to better use. Many devices were used to reinforce the apparent scarcity of the land. Roads were not built, water was not distributed, while the creation of country parks allowed

large tracks of land to be taken out of the map with the added benefit that no investments whatsoever were required in those areas, not even reforestation. A country park was just a no-man's land.

C.H. Tung, whose social position in Hong Kong was inherited from his father, received the prejudiced education that makes rich children believe that the economic system in which they were born, in which their family made their fortune, is the best possible. The Hong Kong setup, with all its characteristics, is thus assumed to provide an optimal situation. To question it would be to question the legitimacy of one's own position.

It was therefore inevitable that, as regards the housing market, a core component of the Hong Kong wealth and the largest single source of income of the government until 1997, C.H. Tung came to the wrong conclusion. This is because his focus was not on the mechanisms of a system that was designed to rob the poor and increase the wealth of the government, but on its most apparent consequence: an endless queue of people without proper accommodation, and a three to five-year waiting list for a place in a cheap and generally derelict subsidized housing estate.

C.H. Tung was not an elected leader. His peers had chosen him and he has been anointed by China. Perfectly conscious that he had little legitimacy in the eye of the Hong Kong masses and the international community, he had to find a set of policies that would have broad support across the community.

'One of his main concerns is to be popular, says Christine Loh. Even if he can't be voted out of office, it is important that he gets the people to agree with his policies.'

The question, as he saw it in 1997, was: what policy would have a popular appeal? It is important to remember that in those days Hong Kong was riding on a decade of spectacular economic growth, that had not been generated by the government but by the merchant elite, and more precisely by China's open door policies. C.H. Tung, during his five years as an Executive Councillor, had seen the government cashing in obscene surplus, without the matter being seriously debated by the government. It is conceivable that he had concluded that Hong Kong had no need of any kind of economic policies. He might have been convinced that some sort of magic formula (the acumen of the elite) was at play. It was all the more magic that no one had a clear idea of what was going on and no one really cared.

That perception would have been reinforced by the high marks granted to Hong Kong by institutes such as the Heritage Foundation or Nobel price winners of great reputation, such as Milton Friedman. The present economic system was, in the mind of C.H. Tung, definitely the best. The delusion was total.

The reality was somewhat different. In the last five years of its reign, the colonial power had left a number of issues festered, those that are now haunting Hong Kong. It had also created recurring expenditures and legal roadblocks that are now making it difficult for the government to impose decisions. Governor Patten put, in some cases, at the last minute, a number of mine fields (such as an environmental law that, in absence of a definition of what public interest is, precluded the government from building an essential road to South Lantau in 2000).

It is under those circumstances that C.H. Tung focused on housing shortage and announced his intent to solve this chronic problem. For that, he announced that Hong Kong needed to build

85,000 flats a year and that 2/3 of the Hong Kong people would become owners of their flats in the not-too distant future. There has never been any explanation as to how the 85,000 magic number was arrived at.

The intent was clearly to get the support of the poor who, in his mind, could not purchase a flat because it was too expensive. When things are expensive in a free market, economists conclude that it is because the supply is in short demand, thus by increasing the number of flats, he concluded that prices of cheap accommodation would go down.

It is on such an assumption that C.H. Tung, who wanted to be popular among the masses, decided that Hong Kong needed to build 85,000 flats a year. Governor Wilson, who was not a politician, had in the late 1980's considered that a long term target should be at about 30,000 for a decade. Thus, C.H. Tung was proposing to increase by more than 250% the rate of construction. Some officials expressed reservation.

It is not surprising that the risks associated with a surge of 250% in the supply of flats, which indeed created the current economic crisis, were rejected out of hand under the argument that they were unlikely to trigger a collapse in the entire market. It was not due to a lack of understanding of those mechanisms, or as some commentators said, that C.H Tung's capacity for abstract reasoning was weak, but because of a bias.

C.H. Tung has been educated in a very conservative world where the spirit of inquiry is always replaced by beliefs in unfounded economic dogma. One of them is that the poor are inferior to the rich in all aspects, and thus are not suspected of having sound economic judgments. This is so because the elite is convinced to have the monopoly of having them, a quality that can't be shared with other segments of the society (otherwise how could the legitimacy of a plutocracy be justified?).

Among the prevalent humbugs that color many of elite's remarks, the most common is that it has achieved its position by hard work, frugality, and scrupulous honesty. Another is that all the appointees use their position as a public trust with an eye for the general good. The international press, the academic world and famous think-tanks are, as Bertrand Russell pointed out a long time ago: *'filled with the praise of the very rich and the man in the street is taught to believe that virtue is proportional to income.'*

The first objections to C.H. Tung's housing policies came not from the poor but from the developers of Hong Kong who are deriving their wealth from the housing market for the poor. They knew from experience that the poor were not going to buy properties solely for the sake of land-related ownership. They wanted value and although they had little education, they were indeed making rational economic decisions.

In other words, the developers had doubts that quantity was going to solve anything. They believed that it would only compound a problem created by the government through ill-conceived regulations. In their view too, a spillover to other segments of the market was inevitable. They proposed their own solution. Left to its own device, the private sector was able to provide enough flats for the poor, according to the demand. The government could provide specific pieces of land earmarked for that in the future and the property developers would regulate the market.

It certainly would have worked, as the property developers have been extremely good at reading the demand for the past twenty years. They had also been complaining for years that antiquated regulations on land usage had to be scrapped to allow the architects to introduce innovative ideas and to allow the recycling of old abandoned factory buildings. Their ideas were rejected because they did not provide the political dimension that C.H. Tung wanted. Thus his goal was not so much to solve the housing problem as it was to use it for political mileage. That is how good ideas are generally transformed into bad policies.

To have introduced further relaxation in the mass housing market and let the private sector adjust to the demand would have only achieved one thing: the reduction of the waiting list for cheap accommodation. It would not have achieved the essential goal: popular support for C.H. Tung. Furthermore the media had already stressed that C.H. Tung owed his elevation to some wealthy tycoons. There was the possibility that further relaxation in the property market would have been interpreted as a payback to his supporters. It would have been a public relation disaster. Hence, the best political approach was to stick to a public policy supposed to target the 20% poorest people of Hong Kong. On that ground, good and bad objections were rejected out of hand.

C.H. Tung saw his ratings soar without looking any further to what the developers had said. But they were quickly proven right. The first result of his ill-fated policies was an increase in the bureaucracy and the ensuing inefficiency. Waste, corruption and scandals set in at a rapid pace, but it was not visible immediately. Administrative red-tape means that it takes five years in Hong Kong for a project to be completed. In the meantime, prices started to drop across the board. Unfortunately, it happened when the Asian crisis was roaming around.

Although the two issues had no relation, since the Hong Kong market was insulated from the currency melt-down and the developers had little debts, economists and market analysts made an unfortunate and unproven link between the two. Another year was lost in speculation about the magnitude of the spillover effect. In the meantime, Donald Tsang, the Financial Secretary, forecasted a drop of HK\$8bn in the revenue of the government. Coming after obscene surplus, it was considered manageable, because it was supposed to be a one-off event. His budget forecasted a rapid recovery, with a revenue coming from the land supply and property-related duties over to the level of the old days within a year or so. But the following year, the drop was a further 20bn, and today the total loss of revenue is close to HK\$140bn (the price of the airport which was considered a pharaonic undertaking).

If C.H. Tung and Donald Tsang, the then Financial Secretary had had a better understanding of the social structure of Hong Kong outlined at the beginning of this book, they would have been quickly aware that, while the 20% poorest were not buying those new cheap poorly built flats in remote and inconvenient location, the 30% with a per capita income between US\$4,000 to US\$8,000 were moving down market. That was setting a catastrophic chain of events that the property developers had rightly identified quite early in the process.

Nevertheless, for close to five years, C.H. Tung stuck to his guns, finding a myriad of excuses for the plunge in property prices. Even today, he has yet to publicly admit that his 1997 decision was ill conceived. Nevertheless, in 2002, a new set of policies was announced in a rush. It reversed every decision made in 1997 and followed to the letter what the property developers proposed in the first place. However the carnage has been such that the government still has 28,000 flats to unload at giveaway prices before a return to normality sets in. With land

sales frozen and a total review of land allocation on the way, the government probably has every intention of returning to the land scarcity paradigm.

The price of the ill-conceived policies implemented in 1997 against all advises has been astronomical. The Hong Kong people had seen their assets divided by two, more than 110,000 households are technically bankrupt. (6) To add insult to injury, available data prove that today the level of affordability had never been so high. Yet, the market remains in the doldrums and the government is so far unable to raise any kind of revenue from land-related transactions in the near future. All rational has been lost.

The attitude of the poor and the middle class has in fact tested the idea that given the opportunity they would not buy anything anywhere but would make a rational decision. There are probably three reasons for them to stay on the sideline. The first one is that property prices are only an element of the housing budget of those families. With transport costs skyrocketing in Hong Kong (+31% in five years while deflation has been running at -11%), each potential buyer has to assess whether the move from one location to another remote one is not without financial consequences beyond the price of the flat itself. In most cases, it was with severe constraints.

Then a second element is the speculative element, which is a powerful incentive to buy. That incentive, missing in a falling market, is that the purchase of a flat, seen among the poor as much as among the rich as a mean rather than an end, would allow the purchaser to go up the social ladder. It is because prices were going up that people were investing.

The third element is psychological. By flooding the market with cheap subsidised flats, regardless of the real demand, C.H. Tung has broken the trust the public had in the housing market as a mean to protect their savings from inflation. It is in fact the most damaging consequence. It will take years of non-interference to repair the damage done.

So basic economic rules have always been at play in the decision process of the poor. C.H. Tung reducing the problem of shortage of housing rather naively to one of a gift that a poor was not expected to refuse, triggered the biggest crisis Hong Kong has ever known. There is a lesson to learn in the process. Basic economic rules had been considered irrelevant because they were not supposed to apply to the poor. For C.H. Tung, Daniel Kahneman, 2002 Nobel Prize winner, who proved that the poor do make rational economic decisions (7), came to late.

'Since he can't be voted out, the political price is not the same as for an elected government, says Christine Loh. In Hong Kong, the worst that could happen is that someone will refuse to shake hands with him. It happened once. I think C.H. Tung was shocked.'

There is no doubt in the eye of the public that C.H. Tung is the ultimate culprit in the fiasco of the housing policies. For a man who is saying that the Hong Kong people should work together and not to be divided, his vision was based on the unethical concept of inequality.

That failed experiment has taught that the less fortunate members of the Hong Kong community are not prepared to agree to whatever is proposed to them in order to defend further the existing social status quo. Yet, as we shall see further on, it is on this wrong assumption that the government is trying to solve the deficit budget. The move could have far reaching political

implications if once again the poor perceive such proposals the same way they looked at the fraught housing policies.

THE DEFICIT CONUNDRUM

As Jasper Tang said, Hong Kong never had a low tax base. The colonial government had carefully crafted a policy of raising 50% of its revenue from a forward levy on land. Because it was a forward levy it was inevitable that it would generate a vast surplus - the cash hoard coming directly from land sales between 1984 to 1997 was worth HK\$211.4bn in 1998 (the value of the Land Fund). In accordance with the rules laid down in the Sino-British agreement of 1984, only 50% of the proceed would go to the Exchange Fund, therefore the total revenue raised by land sales had been about HK\$422bn over 13 years, an average of HK\$32bn a year. That represents a forward taxation of about HK\$5,500 a year per person. (In addition the government had accumulated US\$115bn in financial reserves).

As a government can only derive its main resources from a taxation of a kind or another, it is difficult to reconcile such an enormous amount of reserves per person with the attributes of a low tax economy. But because C.H. Tung does not want to challenge the myth of the past, that after all the government was creaming off about 30% of the wealth of Hong Kong every year, he has today to explain why the revenues have dropped so much. Without puncturing the myth surrounding Hong Kong, he can't do it, and it is easy to understand why.

If we compare the average amount raised in the past from land sale, about HK\$32bn a year, to the land revenue target released by the Financial Secretary, Anthony Leung, when presenting the budget 2003/2004, we see that the government plans to raise HK\$2.5bn in 2003/4, then 13.3bn in 2004/5, 19.3bn in 2005/6, HK\$20bn in 2006/7 and 20.6bn in 2007/8. The total over 5 years comes to HK\$75.7bn. It is 50% of the amount that would have been raised over the same period of time in the 1990's. And Anthony Leung's assumptions are considered to be on the high side.

Because the land revenue together with associated derivatives represented in the past about half the total revenue of the government, it means that the C.H. Tung government is trying to balance the budget with a revenue that on average is expected to be 25% lower than in the past.

The immediate consequence of this disastrous state of affairs has been to bring under scrutiny the public finances of the city.

It was in fact a long overdue exercise, which has been on and off of the agenda since the early 1990's but since the budget was generally generating a surplus, it was politically wiser to emphasize that prudent management and frugality had paid off. It was, of course, nonsense. The budget was neither prudently managed nor frugal.

There were obvious signs that problems were building up. The number of people paying taxes was insignificant and most of the income was unpredictable, thus the surplus was a matter of speculation and the joke was to measure up how wrong the Financial Secretary was in his calculation. The main reason was that land sales were also a matter of speculation as well as the revenue derived from the levies on the stock market. Both accounted at some points for 60% of the total revenue and 100% of the surplus. Since the inflation was high, the stock market

booming and bidding at land sales brisk, the income kept increasing at an unabated pace between 1990 and 1997. That it was an unsustainable approach to public finances was obvious.

Yet, none of the actors that were to stay beyond 1997 made a serious attempt to pave the way for a more serious approach to public finances. The reasons were of course political. The last governor, Christopher Patten, was a political appointee, not a civil servant, with a political agenda. He had no interest in an issue that was not going to affect one way or another his future political career but that could wreck his relationship with the civil service. Nor had the administration any interest in opening a can of worms, which would have outlined the many defects that are now laid bare because of the collapse of the property market.

The mindset was that Hong Kong had sound public finances backed up by enormous financial reserves. When Patten boasted that the British would hand over to China the biggest dowry since Cleopatra handed over Egypt to the Romans, no one questioned the wisdom of such a remark in particular when one considers that the Hong Kong budget is a crude cash accounting system, rather than an accrual one, and that the dowry was left in bank accounts, serving little economic purposes.

A crude cash accounting system means that the payable bills at a future date were never accounted for. That was quite an interesting consequence because it meant for the British that unpaid bills before June 1997 would be accounted for after they had left. In short, they were passing the buck to the next management team.

The wise thing for C.H. Tung would have been to carry out an inventory as early as July 1997 to get a proper balance sheet of Hong Kong. It would have been full of surprises. For example, the Hong Kong people, who are now subjected to a Mandatory Pension Fund (MPF), have yet to realize that the pensions of the civil servants, who are not subjected to the MPF, are accounted for on a cash basis with no provision for the future payments.

There were many reasons for the colonial government to use a crude cash accounting system. One of them was that, Hong Kong being a colony, all future public liabilities were of no interest. A colony lives by the day. Anything could happen tomorrow. Another compelling reason is that the myth of a small government means that, to be consistent, the government lives on a small budget. If over the year the liabilities start to become of a respectable size, it would undermine the myth. A cash accounting system has no memory, so to speak. Thus, there was no political incentive to look into the matter carefully.

'The current deficit reflects a cash-flow problem rather than a situation out of control, says Christine Loh. If I was the government I would switch the way we account for expenditures into accrual accounting rather than the cash accounting currently used. And to clean up the slate, the government would probably have to payoff government pensions.' (8)

James Tien disagrees. For him, the government is clearly overspending and the budget deficit is not a mere cash-flow problem. *'If we look at Hong Kong compared to other city-states or small economies that compete with us, such as Singapore or Taiwan, he says, the government has the incomparable advantage of not needing to pay for its defence or its diplomacy. This should save a large chunk of money, yet our government is eating up 23% of our GDP. We should be spending about 16 to 17% at the most. As we are clearly overspending, we should try hard to*

control our runaway expenditures. Currently salaries eat up 66% of our budget. It is a big burden. We ask them to reduce it. But they refuse.'

Indeed, a report commissioned by the Hong Kong General Chamber of Commerce has in fact established that the civil servants of Hong Kong, which account for about 70% of the expenditures, are overpaid by a margin of 40 to 200% compared to the average pay for a similar job in the private sector. Jake Van der Kamp, a columnist at the main English newspaper of Hong Kong, the South China Morning Post, has worked out that the current deficit would have been HK\$7bn and not HK\$70bn if the civil servants had seen their pay frozen at the 1998 level. It is a HK\$63bn difference.

The civil service is disputing the findings of the HKGCC and asking for a new survey. Some have difficulties understanding how such a disparity was allowed to build up over the years. Others claim it is impossible. Not only is it possible, but there are many indications that everyone was aware of it, long before the deficit brought the issue to the fore. And it was justified with spurious claims that it was necessary or rightly deserved.

At the root of all those claims is the concept that quality means money.

Hong Kong had its own version of this unproven paradigm. It strongly believes that money means quality. In public policies, it means that since its administration was the best of the world, it was natural that it became the best paid in the world. Then came the circular argument that being the best paid in the world, it had to be the best administration of the world. *'The myth was that they were the best of the world and that would justify the pay of our civil servants'*, reckons James Tien.

Beyond the flawed rhetoric was actually an infernal mechanism. Speculation in the housing market, where prices were increasing by 40 to 50% a year, had pushed the salaries of the average people in the 1990's to an unrealistic level. As every tiny speculator was making a lot of money, regular pay became an accessory to a way of living that pushed the civil service pay scale upwards. Although it was clearly a dangerous development, the government had a vested interest in it and therefore no one paid a close look at the likely economic consequences beyond 1997.

Finally, by carelessness rather than design, a time bomb was set up when, under the Basic Law, the ill-gotten gains of the civil service were locked in under a provision that declared that *"public servants may all remain in employment and retain their seniority with pay, allowances, benefits and conditions of service no less favourable than before <30 June 1997>"*.

The public at the time was not informed of the far-reaching effects of such a clause and the legislators let it pass under the assumption that China would, without it, reduce Hong Kong's civil servants salaries to the level of their counterparts in China.

To organize in its basic constitution that a segment of the society would receive a protection not granted to the rest of the population and a blanket immunity against the vagaries of the economy would in a democracy be shocking.

Hong Kong being an unequal society, the matter was not even discussed seriously among the political parties. Yet the effects of such an arrangement are far more detrimental to the cohesion

of the community that any legal text relating to subversion or treason that is currently attracting the attention of the media.

THE POLITICAL DIMENSION OF A LOPSIDED TAX STRUCTURE

There are of course various ways to present a deficit of the public finances. There is even the possibility of arguing that a public deficit is not necessarily a sign of bad management. In Hong Kong, however, the deficit runs contrary to the myth that the city has a small government, and therefore minimal expenditures. It looks all the more weird that the Hong Kong government had in the past accumulated vast financial reserves.

C.H. Tung's critics argue that he does not have the political will to engage into a serious debate on the matter or that his team has not yet understood that a new approach to public finances is required since the revenue structure might have changed for ever. But is it seriously the case?

Over the years, C.H. Tung has learnt that the public finances of Hong Kong are prone to large swings. During the past five years, they swung from a surplus of about 6% of the GDP to a deficit of the same magnitude. And in the Patten years, when he was an Executive Councillor, the surplus had the appearance of being unpredictable.

It is conceivable to consider that over time, things will not be as bad as they are nowadays. Somehow the revenue, which has dropped in 2003 to the mid 1990's level, is bound to increase as the economy recovers. For those who believe in economic cycles, it is a certainty. The only question is when. C.H. Tung takes the view that after five years of difficulties, the downcycle is already a long one. A cautious man, he is giving it another three years. An eight-year period of economic contraction is indeed a very long one. It is even a longer period than the last world war. It never happen before in Hong Kong.

Based on that shallow inference and not much else, C.H. Tung and his team are announcing that the budget deficit will disappear in 2007/2008. The clear implication is that the missing billions on the revenue side will soon materialize. An upturn in the property market could play the trick, but C.H. Tung has been cautious not to state it. However it is obviously his only hope because on the expenditures side, it is now clear that he has decided not to break the iron bowl of the civil servants.

The budget of 2003/2004 has been heavily criticized for its lack of political contents. Many have been saying it is more of the same, another budget without clear direction. But looking at what and who was targeted in the whole exercise, it appears that the budget is based on a strong political belief that assistance to others is a personal duty, not a matter for a political system to deal with and that public finances are not an exercise in redistribution of wealth.

This is an important statement, but because it was not associated with a political rhetoric, as is usually the case, the political parties failed to recognize its elementary political principles. And once again, one must admit that the initiative of the debate lies with C.H. Tung and not with his critics, yet they complain about his lack of leadership!

There have been at the end of the XIXth century considerable debates about the role of governments, with at the end of the industrial revolution, many supporting the view that "political caring" was necessary, as the dire conditions of the society described best by Charles

Dickens in the United Kingdom proved that a “community without politics” which emphasizes benevolence to help others through private charities, had failed. The debate could today be reduced to two models: the American model which emphasizes the role of private charities to help others, or the Continental Europe model (Germany, France), where political caring through the state is the preferred tool of the population.

Without looking at the merits or demerits of both models, it can easily be demonstrated that a world-city is always against political caring. This is so because, as we have seen, the population of the city is never the source of strength or wealth of the city. Hong Kong is in that respect a perfect world-city.

True to the tradition of the world-cities, Hong Kong's elite is against “political caring”. C.H. Tung is their representative, and his position on public finances reflects a political stand, not a result of incompetence or lack of comprehension. It is not the result of indifference or double-standard, as his opponents are quick to say. It is first and foremost a political inclination and it has to be recognised as such.

If it has to be challenged, it is on political ground. So far his opponents have failed to do so, focusing on peripheral issues or on personal attacks. They thus deprive Hong Kong of a much-needed political debate and all political parties deserve to be blamed for their attitude.

It has always been essential to the legitimacy of any plutocratic system to emphasize benevolence over political caring. Their champions, C.H. Tung (and the Heritage Foundation) among them, have always drawn the attention on the corrosive effects of welfare on the beneficiaries and the importance of benevolence as the measure of their moral worthiness. Great plutocrats have always been regarded as great benefactors (Bill Gates, today considered through his foundation a great benefactor, is a perfect example of the rational at play).

We have already pointed out that class distinction was an essential component of the political thinking of C.H. Tung. Conversely, he is a firm believer in the legend that attributes to hard work, frugality, and scrupulous honesty, the success of his peers. His elevation to the top post in Hong Kong is thus a natural outcome. The forgotten corollary of such a belief is that others do not have those qualities (hence their lower social conditions).

That many in Hong Kong amassed their fortunes through tricks, chicanery, dubious monopolies, political donations, and sometimes sheer illegality is forgotten. After all, the universities and the press are filled with the praise for the very rich. The university teachers themselves have no qualm to claim that if their pay is reduced, then the quality of teaching will suffer. As we said, in Hong Kong, it is considered an absolute truth that money is a sign of quality.

How would C.H. Tung be aware that it is a falsity? Since the media and the scholars are filled with the praise for the very rich, it is quite common, if you belong by birth to a class, which has hereditary social prominence, to believe that virtue is proportional to income. The Enron scandal, and many others before, has not dented what is primarily an act of faith that does not need proof. Like George W. Bush, with whom he shares many characteristics, C.H. Tung never amassed a fortune, he inherited one. He never created a reputation, he was born with it.

Now, if one believes in class distinction, it becomes quite natural to select in an advisory committee, a person whose only qualification is to be either the scion of a well-known family, the Chairman of General Motor, or a well-known billionaire, on the only ground that they are obviously endowed with the qualities associated in this world with money and power.

C.H. Tung, a member of the plutocratic society, was educated to believe in the power of command and many other humbugs. This class, pretty much like the aristocratic one, was trained in childhood to compete among peers and to practice social discrimination. C.H. Tung has a keen sense of competition, and in that respect he has so far outsmarted his opponents. This is because they fail to recognize such a quality on the ground that they disagree with his political inclination.

Once it is accepted and understood that the political platform of a member of the plutocracy is to maintain the plutocratic order, then many of C.H. Tung's actions that leave his critics wondering whether he is incompetent or plain stupid, appear in fact carefully crafted.

But his opponents seem to so far lack the sophistication required to understand his tactics. This is probably because C.H. Tung is not in appearance a man with strong or unusual desires. He looks complacent but he is not. He is decisive but does not like confrontation. His behaviour aims at minimizing friction between equals while, as Bertrand Russel, the English philosopher, would put it '*doing his best to delicately impress inferior with a conviction of their own crudity.*'

Such behavior conducts Emily Lau to consider that his working habits make him unsuitable for the position of Chief Executive. '*C.H. Tung is surrounded by sycophants, she says. They are generally pro-Beijing faces, which have never been there before. You can say he is doing the same as the British governors. In the past, if you were pro-British, you were part of the inner circle of power, if not, you were ignored. Today, the difference is that you have to be seen as pro-Beijing. C.H. Tung is responsible for such a bias. He could have done it differently because the process of appointments is entirely under his control. In fact, it is common knowledge that whenever the civil service prepares a list of appointments, he would sit on these recommendations for months, rather than make a direct observation. He gives the feeling he can't make up his mind. I remember one of the senior officials telling me that he likes people to second-guess his wishes. Because the appointments are up to him, the quickest way would be to comment or propose names. Then, it would be done. But he won't do that. So he lets the normal bureaucratic procedure take its course. It means the Home affairs prepare a list. Yet, there is no rule that prevents the Chief Executive from issuing a list directly. So here he is with a list on his desk. He does not like it because he can't find on it the names he wants. So he will just leave it on his desk for weeks or months, without saying "I want those names on the list".*

In the meantime, the civil service is waiting for instructions. None are forthcoming. C.H. Tung, a former official told me, will just wait until an inferior realizes that he does not act and something must be wrong. At that point, a second amended list is prepared and delivered to his desk. If the new names do not satisfy his wishes, he will do exactly what he did, that is to say nothing.

Ultimately someone becomes familiar with what he wants and second-guesses his wishes. So the right names come up on a new list, and so on and so forth for everything. He could have said from day one, "I want A, B, and C, or I want this and that, these are my ideas". But he deigns not to do it. He wants others to guess his wishes. That is how he operates. I don't think one can govern in this manner, but he is that type of person and it is quite terrible.'

C.H. Tung's attitude conforms to the letter to what the Oxford educated class called "Good form". Bertrand Russel said that it is an attitude almost as destructive to life and thought as the medieval Church. *'It renders fundamental open-mindedness, or inward readiness to give weight to other opinions, impossible, he wrote. As a political weapon for preserving one's privileges, it is an unsurpassable strategy, for it gives one the perfect assurance of one's own rightness and the belief that correct manners are more to be desired than anything. In particular, it makes sources of progress suspect, as the supreme goal is the preservation of the social structure.'*

Arthur Li, enjoying the same hereditary social prominence, has another description of the power of the "Good Form" attitude. *'The trouble, he said in 1998, is that if you say anything bad about C.H. Tung, you feel guilty. He is such a nice man.'*

An inevitable trait is that people holding such opinions lack the intensity of belief that goes with the wish for truth. It is such an intensity that produces real efficiency. If the C.H. Tung's government is perceived as highly inefficient, it is precisely because it is lacking in intensity. But it is also this trait that confuses his critics who attribute his perceived failure to a lack of personality.

As for democracy, an issue directly at the core of what public finances are about, there is no doubt that C.H. Tung shares the common belief among plutocrats that only "qualified" people can represent the interest of the community.

Who should vote and who should be the representatives has been much debated in the past, starting with the Greeks who practiced a very restricted form of democracy. While the world is slowly moving towards devolution to the masses and direct democracy, in Hong Kong such a debate has not even genuinely started.

The problem of the deficit provides however an opportunity to enter into it. And C.H. Tung brazenly did it and turned it into a one-sided argument with little resistance from his natural opponents.

This is because the core argument of the supporters of a restricted democracy rather than a direct one is that a government is accountable primarily to those who finance it and not to those who should be grateful for its benevolence or munificence. In Hong Kong, the argument is considered all the more potent that, by using it, the dominant class can easily demonstrate that it is (in appearance) the only one paying taxes.

In Hong Kong, few people pay an income tax. As we saw earlier, only 13,000 do so at the maximum rate of 15%, while the majority of the Hong Kong people are outside the tax band, and are thus taxed at zero. Furthermore, the top hundred companies of the city contribute alone to about 90% of the revenue raised through the profits tax.

Such admission would in a developed democracy ring an alarm bell as it would convey a rather negative social message. In Hong Kong, it is conveying the message that since the rich pay and the poor don't, the government is a caring one. It is of course a crude fallacy, as there are a myriad of other direct levies that hit the poor more than the rich. Looking at the housing market, we have already outlined that the premium paid to the government for the purchase of land was a forward tax collected by the property tycoons on behalf of the government (upon

which they were allowed to keep a fat fee). That the tax was way out of the means of the poor, was clear since they had to finance it by mortgaging their future. But it worked very well. The colonial government was able to tax in advance the community about HK\$30bn a year, which otherwise would not have been collectable at all.

James Tien, although a supporter of C.H. Tung, recognized, albeit without seeing the significance of his observation, that endless administrative fees and charges are hitting everyone for everything: *'Just in my enterprise, even before we know whether we have made any money at all, we have already paid a couple of millions of dollars of paper work to the administration, he says. This is taxation in advance.'*

Nevertheless, the Secretary of Finance, Anthony Leung, has no qualms about it. He tries forcefully, as the other members of the government, to make the people believe that they have no reason to complain. Only a few pay a full 15% tax. The aim of the government is to instill the concept that only those ones have a right to object to the government's policies. True to the tenet of benevolence, the others should just be grateful.

What is in modern democracies an academic debate consigned to the history dustbin takes in the city further significance because 50% of its legislators are currently elected through a system of restricted representation. Indeed, why would a functional constituency exist, if not for the reason that its members contribute to the society in a more important manner than others?

The supporters of the system, C.H. Tung being one of them, consider that a number of Hong Kong citizens deserve a special treatment. Like in the Orwellian farm, Hong Kong citizens are all equal but some are more equal than others. The concept fits very well with the tenets of the rule of law which has never meant to promote equality (as opposed to the civil code, which is an equalitarian mode of justice), but rather obedience and discipline. The rule is only there to underpin strongly an order of representation, not to provide a just or an equitable judgment (9).

The democracy of Hong Kong provides that a small number of people have the right to cast two or more votes. A vote, as we have seen previously, can weigh a hundredth of a seat in a functional constituency or only a hundredth thousand of one in a carefully crafted geographical constituency (10).

James Tien, who got elected through a functional constituency, admits that it is not equitable, but a typical plutocrat, finds it necessary because *'the businessmen realize that if you have one man-one vote then Hong Kong is bound to turn into a Scandinavian country with high taxes and high social welfare.'*

According to him, Hong Kong cannot afford a proper democracy. *'It is small and facing increasing competition from China, he said. The large businessmen dislike the idea of being overrun by the people that don't pay taxes in the first place.'*

Such a popular view among C.H. Tung's supporters has an undesirable consequence however. If to solve the deficit, the community were to increase its contribution to the government, then it would surely claim the same privilege currently attributed to the elite class, that is the right to make decisions. James Tien who also enjoys hereditary social prominence says he does not welcome such a possibility. For the elite who believes that the people should not be encouraged to take more interest in the political process, it is an unpalatable outcome.

Then, what needs to be done to raise revenue without increasing political awareness? This is precisely the conundrum C.H. Tung tried to solve.

It was actually to lower political awareness and political participation that the British government had adopted the rather devious way of excluding the majority of the Hong Kong people from direct taxation (by increasing the deductible allowance). It did not really matter, as far as the Treasury was concerned, because everyone was then caught up in the net of the land-related levies. One way or another, everyone was contributing to the coffer of the government, but the perception has been smartly blurred.

Some may disagree with such a judgment. Analysts and accountants published a myriad of papers to explain that the government miscalculated the allowances, while eventually outlining that such a blunder in the end was in favor of the poor. It was not a blunder. It was a political decision. This is why today they criticize the lack of decisive actions to redress the situation. They do not grasp the issue. Money is only a small part of it.

The democrats and grassroot parties do not fare better. They have this confused perception that it might have been a pro-poor policy, and to dispute it would undermine their pro-poor or middle-class credentials. But one should consider that a true pro-poor policy would address the problem of the forward tax on land rather than using deductible allowances to reduce the level of tax the poor had to pay. When 50% of the revenue was, one way or another, derived by the indirect and upfront taxation levied through premium and land conversion fees, tinkering with allowances was not going to reduce the true exposure of the poor to government levies through various means. But by putting them outside the basket that is the focus of attention, the government was building up a case for a political argument that has been used many times over to disfranchise part of a population of their rights to political representation.

Therefore the perception in Hong Kong, backed up by undisputable data, is that the poor are not paying. It is about as skew as the myth of a small efficient administration. Not everyone is fooled. *'There is this myth that we have a small government, Jasper Tang says. People have no idea. They just see that we have low salary taxes, so how can we have a large government since in Europe they have high taxes and a large government? They don't understand where the catch is.'*

This flawed perception has many consequences. It has given a free ride to the administration that plays the role of the benevolent and the munificent, while actually reaping off most of the gains made on land sales for it. The media is every day full of outrageous comments of officials reminding, inauguration after inauguration, that what the public gets, whether it is a hospital, a school or running water, is a gift, as if the coffers of the Treasury were filled with money that is not public money, but coming from others: the rich.

The Hong Kong government propaganda is so crude that in matter of public policies there is not the slightest inclination to consider that the people have equal views and equal rights. That is a legacy of the colonial mentality that has yet to wear off. It has yet to be disputed. Different solutions for different people, under the colonial system, were the norm. That it remains the norm is not yet challenged. In the meantime, C.H. Tung has indicated that people come last, business and businessmen come first.

Rights in Hong Kong have remained as they were ranked in the United Kingdom in a bygone era. They are according to status. Thus for the administration it is more important to solve a problem in Repulse Bay, an expensive location, than in a remote part of the New Territories. An amusing example of this pathetic mindset could be found in the way the government looks after the Disneyland park built with taxpayer's money on North Lantau (11). While the south and the north of an island as large as Hong Kong island still have to be connected by a double lane road open to all traffic (12), a new MTR link to Disney world was decided in a rush, launched and financed in less than a year. When the link opens in 2006, the government will still be restricting the traffic to/from South Lantau to residents, where more than 50,000 people live, because of a lack of proper infrastructure and public car parks.

By then, another 1.5 million people on Hong Kong Island will still be waiting for three MTR lines which have been on the drawing board for the past ten years (13). They are people that are precisely considered to be for the most non-taxpayers.

On what ground, says the administration which is fronting there for the government, could they complain since they do not contribute to the budget? Why should other people pay for them? But don't the people of Hong Kong then have a right to ask why they should finance Disneyland?

The deficit of public finance therefore has an evident political dimension. If, as would a government in a developed democracy, Hong Kong was to widen the tax bands so that the majority of the population became taxpayers, then political representation would become a central issue and political inclination would be in the open for all to judge and support or criticize.

But it was precisely to avoid that situation, that is a political awareness, that the entry point in the tax system has been based for one household to about 30% above the official per capita income of the city. That gap has therefore not just an economic consequence but a political significance as well.

Not surprisingly, very few people from the business sector favor a widening of the tax bands. Most, Christine Loh among them, favor a reform that would introduce some sort of consumption tax, coupled with a slight increase of the profits tax. Accounting firms, business organizations of one kind or another, financial gurus, and market analysts suggest the same. They all refer to various models, none of them taking into account the wide disparity of income of Hong Kong and the political dimension of public finances. Not surprisingly, they all espouse the view that "political caring" using an adequate budget is dangerous.

James Tien perfectly resumes the mood when he says: *'The Liberal Party is the only one among the political parties to say we should cut expenditures and increase the revenue. Both the DAB and the Democratic Party offer nothing on the cutting side. The Democratic Party proposes a progressive tax pretty much in line with what happened in the Scandinavian countries in the 1970's. Hong Kong cannot afford it. It would destroy our competitiveness.'*

However, it is well known, and many researches prove it, that a consumption tax of one kind or another hurts in relative terms the poor more than the rich, while in absolute terms, the reverse seems to happen. Indeed as the rich pay nominally more than the poor, it is quite an attractive proposition for those who claim already that they are the taxpayers while the poor are not. But

in reality, as a percentage of their disposable income they pay far less. Thus, it is not surprising that such an approach has the favor of the elite (14).

In view of the weak purchasing power of the majority of the population of Hong Kong, it would be probably an error to implement a consumption tax, for it is unlikely to raise enough revenue for the government, while it is likely to increase the wealth divide and impoverish further the middle-class of the city.

Having a limited access to credit and a weak income, the poor and the middle class are likely to offset the increased cost of a specific item by delaying another purchase, weakening further domestic consumption (15).

But beyond the economic arguments, the main reason to oppose it would be that it would deprive the political actors of legitimate goals. Hence it would thwart desirable political developments. By blunting the accountability system while serving the elite, a consumer tax would make it harder for the democratic minded politicians to raise awareness among the public. For that reason, the grassroot politicians, if they fail to oppose it, will face the prospect of becoming irrelevant.

Meanwhile C.H. Tung is already laying the groundwork for it, with a cosmetic increase in the profits tax, while ruling out a broadening of the tax base.

David Li, Arthur Li's brother, a family whose hereditary social prominence is incarnated by its tight control of the third largest bank of Hong Kong (Bank of East Asia) has already declared that a *'sales tax is definitely coming within the next five years'* and *'the government may reduce the salaries tax after it introduces the sales tax'*. Anthony Leung, the Financial Secretary, has also indicated that a consumption tax was under consideration and *'might be implemented at a later stage'*.

All these remarks are not innocuous. The elite is perfectly aware that the question of representation would be attached to any substantial widening of the tax band and that a change in the perception that the rich are benevolent and the poor must be grateful would be a dangerous political development.

This is why the Hong Kong government propaganda machine, a very well funded organization, is likely to further disseminate slogans to the public to reinforce the idea that the elite contributes more to the government revenue than the rest of the population. It is all the more important to entrench it further that the third legislature of the SAR HK (elected in 2008) will see thirty of its members being directly elected, six more than under the current format.

In theory, the change could give more weight to the community and to directly elected deputies. In practice, the administration is already studying what should or could be done to make the change ineffective, so as to prevent the emergence of a popular vote that in theory could control 50% of the chamber.

As for the argument that the rich have offered a raise in the profits tax, *'to share the burden between the people and the business community'*, there is a lot less in this decision than some believe. Of course, as James Tien, many use it to point out that by accepting a reasonable

increase of the profits tax, the business community demonstrates a sense of social responsibility (its benevolence).

However one needs not look very far to understand that it is an illusion. By Anthony's Leung's own admission, 90% percent of the revenue raised by the profits tax comes from just 5% of the profitable companies. It means that 95% of the profitable companies do not contribute to the budget. A 1%, even 2% increase among those companies does not go very far, and the question of the increase is to a point an academic one for most of the elite.

The questions that come to mind to those unfamiliar with the Hong Kong business environment is: why are so few companies subjected to taxes? Are they all cheating? What is going on there?

The short answer to those questions is that Hong Kong has still retained most of its privileges as a world-city in that particular domain. A fundamental difference with developed economies is that the taxation in Hong Kong is territorial. Since its companies are at the center of a larger economic zone than its domestic one, most of the companies derive the bulk of their profits in the larger economic zone, not in the domestic one.

To size up the problem, let's take two numbers coming from the International Monetary Fund. The GDP of Hong Kong, that is the value of the goods and services exchange in the domestic economy is in the range of US\$155bn, while its trading activities are about three times this size (US\$455bn). It is not therefore surprising to have 95% of the companies involved in the trade and 5% in the domestic economy.

In practice, the lines are blurred because the Hong Kong companies are highly integrated and cross-shareholdings is the norm. No one is purely inside or purely outside. Even the two utilities companies, China Light and Power and Hong Kong Electric, which operate under a franchise, have major developments outside Hong Kong. They provide ample opportunities for the management to massage their bottom lines.

The transfer of all substantial manufacturing activities in China has allowed the whole business sector to redesign its tax profile. This is what world-cities are about. That is where they have an unparalleled competitive advantage.

But the larger you are the more difficult it becomes to be 100% invisible. In the finance sector, banks and insurances have more exposure than a sprawling conglomerate. And there are, of course, the retailers and all the small actors of the domestic economies, from the real estate agent to the repair shop at the corner of the street. There are also the franchise companies that have 100% of their activities in Hong Kong, such as the franchised bus companies (although they all have for ultimate owners, sprawling conglomerates), the Mass Transit Railway system or the local telephone providers. These companies are the 5% that contribute 90%. Since Hong Kong does not have an anti-monopoly law, many of these companies generally manage high margin derived from predatory pricing.

Thus, the lopsided tax structure is a pure product of what world-cities are about. Competition is restricted, the divide of wealth is enormous, and the sense of social responsibility is not what it seems. All the signs are, especially after the presentation of the new 2003/2004 budget that the business community is already using the deficit issue as a political weapon to further entrench its position and the benefits associated with it (15).

DILLY-DALLYING WITH THE DEFICIT

While C.H. Tung is unconvincingly saying that the HK\$30bn drop in the government's revenue has nothing to do with his own policies, he is also trying hard to shift the responsibility of the runaway expenditures to the decisions made by his predecessor, Chris Patten. He has in particular singled out the welfare spending as if it was at the heart of the problem. On both accounts, he is misleading the public.

On the first point, it should be kept in mind that, for all his talks, C.H. Tung being a novice in politics, although it looks like he came to existence in 1997, was in fact appointed a member of the Hong Kong government in 1992. As an Executive Councillor, he had over the years to approve or object to the expenditures starting with the budget 1993/1994. That is a long way back since it means that he had a say in the last eleven budgets of the city (16).

Nevertheless C.H. Tung did not express any view on the social spending habits of the Patten government, while today he is quite adamant that too much resources have been diverted to the Comprehensive Social Security Assistance scheme, which has been cut by 11.1% in the budget 2003/2004, warning of further reductions in the future.

His point is that the CSSA expenditures are out of control, and indeed they are, but cutting them will not solve the budget deficit, nor will it solve the problem of poverty in Hong Kong. If more resources have been diverted to provide a safety net to an increasing number of recipients, the total amount of the expenditures in the year 2002/2003, while substantial, represented only \$32.1 billion, an increase of \$2.35 billion (+9%) compared to the year before.

Therefore, if the budget had been capped with no increase in the CSSA, the expected deficit of \$70 billion would have been reduced by only 3%.

For C.H. Tung, to single out in his Policy Address that welfare spending is at the heart of the imbalance between revenues and expenditures had thus no economic significance but a political one. To reckon that the budget deficit was due to the profligacy of the civil service would have served no political purpose at all. It would actually have alienated his willing partner in government and endangered his position.

His calculated diversions were further evidence as to the nature of his political inclination. However, by siding so publicly with the civil service on the matter of the deficit, C.H. Tung may have misjudged the consequences of expediency over substance.

His remarks did not surprise anyone. The cast had been set long ago, since it was discovered that the revenue would lose HK\$30bn in the debacle of the housing policies, and the expenditures were out-of-control due to build-in mechanisms in the civil service cost structures.

There were two ways to confront the situation. One was to have an innovative approach and look afresh at public finances with a view to dismantle the colonial heritage. It may have required an amendment to the Basic Law to get rid of the article 24 providing a cast-iron protection to the civil servants. China would have been supportive of such an approach. The government would have received massive support from the public. C.H. Tung would have been able to muster a majority in the Legco, while highlighting the inconsistencies of the Democratic

Party. The civil service would have opposed any such move but would have been undermined by its own excesses. However such a decision would have meant going into uncharted territory. C.H. Tung is a conservative by nature. Conservative people do not innovate. They tinker with existing systems, no matter how badly damaged or unworkable they are.

The only other avenue was therefore to tackle the budget deficit from within. That it would remain a cosmetic exercise did not matter. The first decision was to lower expectations and increase the time needed to sort out the problem. Thus, starting in late 2002 when the numbers started to startle the finance community, the officials subverted the debate by presenting their case as good and honest managers would do, using common clichés rather than dealing with substance. They did not have any short-term solution, therefore they came up with a medium-term outlook. The deficit would be solved in three to four years. One has to remember that only a year before such statements were made, the government had forecasted an increasing surplus over the next five years. The total deficit was parcelled out. No one mentioned that the cumulative deficit by 2007 might well be over HK\$250bn, which is more than a year of income.

Finally, Anthony Leung, the Financial Secretary laid the case to the Legco as follows: *'The share of public expenditure in the economy averaged around 16% in the mid-1980s, about 17% in the mid-1990s, but rose to 22% in 2001-02. This is due to the fact that, in the face of economic downturn since 1998, the Government has consciously adopted a counter-cyclical fiscal policy, by keeping expenditure growth above the trend growth of the economy. In addition, due to rigidity in the prices of public expenditure, they have continued to rise despite deflation in the economy.'*

It was a language that, in appearance, made sense. It gave the impression that the interlocutor knew what was talking about. The problem was framed as one of basic economics. The trouble is that it does not square with the facts, and not even with what was said the preceding year. It was an explanation, made with hindsight, designed to give some sense of inevitability to what was happening.

It makes all the difference between delusion and reality. Anthony Leung was deluding himself and the legislators when stressing that the government in 2000-2001 had consciously engineered a deficit. He was doing it so that the classic argument that a Keynesian policy was at work could take his place in the sequence of events he was describing. He wanted to convey the message that C.H. Tung and his government had decided, to sustain economic growth, that a deficit was needed.

But that has never been the case. When the Asian crisis had already receded from Asia, in 2000, Donald Tsang, the previous Financial Secretary, had presented a forecast for the next five years, and the budget was not only balanced but generating a surplus. And in 1998/1999 and 1999/2000, there was no Keynesian policy at work since no one had even conceived that the economy was in deep trouble. C.H. Tung had not yet realized that the collapse of the housing market had toppled the Hong Kong domestic economy. His eyes were on trade figures, and with them, Hong Kong had registered a 10% economic growth. The government then expected to see its revenue jump to HK\$270bn by the year 2001/2002. Actually it dropped to HK\$150bn.

Thus the idea that the deficit was due to *"a counter-cyclical fiscal policy"* was just a nice story but absolutely baseless. It was not the first time the government was daydreaming its economic

policies. Donald Tsang, the former Financial Secretary had shamelessly attributed the return to “*positive growth in the second quarter of 1999 and 2000, with a GDP registering 10.5% real growth, the highest since 1987*” (17) to government policies before moving up the administrative ladder to Chief of Administration. Again there was absolutely no serious data that could establish a correlation between the budget and the economic growth in Hong Kong.

What really happened was far less glamorous than pro-active Keynesian policies. The revenue had disappeared in the quagmire of the housing policies, while the core of the expenditures remained immune to the deflationary pressure exercised elsewhere because of a silly law enshrined in the Basic Law ().

If it can be argued that C.H. Tung has probably made his decisions based on his political inclination, there are also lingering doubts as to the competence of his economic team. This is outlined by its inability to understand the intrinsic inconsistency between its dual claims that Hong Kong is (or remains) a world-city, and that Keynesian policies have (or could) spurred growth. It can easily be demonstrated that it can only be one or the other, but not both.

The current confusion is all the more surprising that C.H. Tung was the first to recognize that a world-city is at the center of a world-economy zone larger than itself. He should today reckon that Hong Kong has little influence over it. He certainly knows that whatever influence it had in the past over the direction of its world-economy, it has never been through domestic public policies. And today, China has totally outflanked Hong Kong.

As Albert Chan said: ‘*Without the open policy decided by Deng Xiao-ping, Hong Kong would have been in trouble. We have only been good at seizing opportunities created by others.*’ To seize opportunities is quite different than controlling events. Any influence Hong Kong may have had on the development of China, and it seems that it had an important one, came through private investments that were mostly channelled through offshore companies (19). That was the true meaning of the myth of Hong Kong being a large economy with a small government.

Thus, there is today much unease among the business community and the people when the Financial Secretary, Anthony Leung, rests his case about the deficit as if the intervention of the administration had been a prerequisite for economic growth in Hong Kong. Therefore there is not the slightest doubt that the government is misguided when linking the two different issues, to explain the current situation.

The deficit was not in the past a product of overinvestments. It did not finance the future. It was primarily the result of the collapse of property prices in Hong Kong. The collapse meant that the government was unable to reach its revenue target by a wide margin, while the expenditures continued to increase because the civil servants cost more every year.

Thus the refusal to engage in a thorough reform of the civil service, one that would certainly bring C.H Tung in direct conflict with the civil servants, is a main source of concern.

A recent agreement to cut the civil service pay by 6% over two years, in 2004 and 2005 lacks credibility. ‘*We need a 30% cut*’ says James Tien. Christine Loh and Tsang Yok-sing say the same. The only political party dilly-dallying on the subject is the Democratic Party. It does so for good reason. Many of its supporters (and its current Chairman) are working in universities and other para-public organizations. They are de-facto civil servants.

The main objection to such a shallow and insignificant cut in the civil service payroll is that it will not reduce the gap at all but will rather entrench it further, for salaries in the private sector are likely to continue to fall faster.

Can Hong Kong remain manageable, and indeed any society, with such a difference between the public sector and the private sector? C.H. Tung has so far evaded the question. His reasoning is probably that it might be possible if Hong Kong remains a world-city. This is because the administration of world-cities is always paid by the wealth generated outside the city. We can think here of Venice paying its administration through the resources accumulated overseas.

But nowadays, there are two immediate problems with such a view. First, Hong Kong is no longer a world-city controlling the Pearl River Delta, and second, in the medium term a come back to its world-city status is unlikely. Whatever its status, there is no doubt that Hong Kong has from now on little chance to continue accumulating wealth from a world-economy increasingly dominated by its neighbors. This is not only because it lost its momentum but because its neighbors would today object to any such transfer of wealth. Indeed, the main argument surrounding the construction of a bridge to Macao is that the Pearl River Delta cities want to know who will benefit from it. If it appears that the main beneficiary is Hong Kong, it is unlikely to proceed. Power-sharing is therefore the new game. World-cities do not share their power. When they do, they are doomed.

If and when the Chief Executive is convinced that Hong Kong has lost its past privileges, then he might come to the conclusion that the current marriage of convenience between the elite and the administration is unworkable. C.H. Tung may never come to that conclusion during his own term, but the problem will not go away. In the meantime, to keep the coalition alive, he has opted for the path of least resistance and for cosmetic measures.

The 2003/2004 budget will probably generate a deficit quite similar to the one registered in 2002/2003 (HK\$70bn). On the revenue side, by raising the profits tax from 16% to 17.5%, the government expects to raise an additional HK\$3.5bn, while at the same time the taxpayers are expected to contribute a further HK\$6.8 billion to the government coffer. Only 90,000 new taxpayers will be brought into the tax net, thus confirming the aversion of the government for political representation.

Even though, the government reckons that it has a funding gap of about HK\$6bn. We consider that it is rather going to be HK\$20bn. The government was expecting that an economic recovery might somehow fill in its coffers. This was based on the assumption that when the economic grows, so does the revenue. In 2003, the impact SARS crisis is likely to push back the economic recovery of the city.

As the editor of the Hong Kong Standard points out 'in many ways, Hong Kong is no closer to dealing with the deficit than a year ago.'

notes of Chapter IV

- 1.- The government and many private think tanks are commissioning survey after survey to compare Hong Kong to perceive competitors. One of the most ludicrous is a regular survey commissioned by the Better Hong Kong Foundation to rate the SAR and Shanghai. On a scale from one to five, Hong Kong's overall competitiveness rating rose, we are told, to 3.93 from 3.75 the year before, while Shanghai's rating rose to 3.12 from 2.96. The global rating was a combination of five other ratings in governance, globalization, legal framework, human capital, technology and environment. Hong Kong is ahead of Shanghai in all five. Happily, George Yuen, chief Executive of the Better Hong Kong Foundation, concluded 'both have improved, there is no loser'. One of the most ridiculous statements made was that 'if Hong Kong does not improve its competitiveness, Shanghai's real GDP per capita may equal or even surpass Hong Kong's in six to seven years', as if there were a strong correlation between the two.
- 2.- A good way to understand the importance of the China trade in the Hong Kong economy is to look at the volume of containers shipped out of Hong Kong towards the United States, compared to others. Hong Kong domestic manufacturing facilities being quasi-non existent since all the factories have been relocated in the Pearl River Delta, the containers loaded in Hong Kong are unlikely to be filled with products manufactured in the city. While the total number of containers shipped out from China, including Hong Kong is above 500,000 Teus per month, Hong Kong accounts for about 120,000 Teus per month. This is three times the number of containers shipped out from Taiwan, which has much larger manufacturing facilities, and two times the number of containers shipped out of Japan. Left to its own industries, Hong Kong would be unlikely to ship more containers than Singapore, a leader in IT manufacturing facilities. Singapore shipped less than 10,000 containers per month to the US. In other words, the impact of China is probably to multiply by ten the number of containers that Hong Kong would ship if it was not the port of the Pearl River Delta. The inference is that 90% of the transport activities are dependent on China.
- 3.- Deflation has lately been blamed on China. If it were the case it would further reinforce the argument that Hong Kong has lost all the attributes of a world-city, as its domestic prices is now subjected to outside pressures, while world-cities are always immune to them. At the heart of the matter lies of course the housing policies of 1998. As the property market was the largest component of the domestic economy, the collapse of its price mechanism had a rippling effect across the board that has still to subside. Furthermore recent studies have shown that deflation has introduced further distortion in the wealth distribution, as public transport, school fees, medical care, utilities etc... have yet to fall significantly.
- 4.- Originally, the Hong merchant was a buffer between the Chinese authorities and the foreign governments. He was a Chinese, and at any one time, there were about eight of them. Over time, the name passed on to the British merchants that had secured by less than legal means the exclusive rights to the Hong Kong trade. Of the first companies to settle in Hong Kong, only two, Jardine and Swire, became bonafide conglomerates with sprawling interests in Asia. Hong Kong Bank was the de-facto central bank of Hong Kong until the mid-1990's. It was run as a private Scottish club as it had the peculiar statutory requirement that no one should control more than 1% of the capital and its first directors were from Scotland. During the British days, the Chairman of Hong Kong Bank was automatically an Executive Counsellor. In the 1990's Hong Kong Bank took over a London institution and then did a reverse takeover to move out of Hong Kong its holding company, while retaining its dominant position. It is now known as HSBC with its headquarters in London. Hong Kong Bank remains the single largest source of profit of HSBC. It also controls through its pension fund the third largest bank of Hong Kong, Hang Seng Bank which also contributes handsomely to the bottom line of HSBC.

- 6.- As early as 2001, the government had received unmistakable warnings that the housing policies were going to have far-reaching consequences on the poor and the middle-class. *'As we all know, the property price level of Hong Kong has fallen by up to 60% since the Asian financial turmoil,* declared A. Razak, a legislator, in the traditional motion of thank on October 18, 2001. *Price level of some private properties in the secondary market in the northwest of the New Territories is similar to those in Shenzhen (China). The price level of flats under the Home Ownership Scheme (HOS) is lower than that of private ones across the border. As the construction cost of these flats in Hong Kong is much higher than that in Shenzhen, such property price level in Hong Kong is really in a sad state. The collapse of the property market is due to a number of reasons:*
- a) The Asian financial turmoil burst the "bubbling" property market resulting in a sharp economic downturn;*
 - b) The housing policy of the Government of the Hong Kong Special Administrative Region is unclear. Government provision of public housing and HOS flats has directly intervened in the property market. The Hong Kong Housing Authority (HA) and the Hong Kong Housing Society (HS) he become the major competitor to the developers in the housing market. This has led to a drop in property prices and created an environment of uncertainty; and*
 - c) The future of the Hong Kong economy is not promising. The numbers of unemployed and the negative-equity property owners increase continuously. The general public has insufficient confidence in the property market and is, therefore, unwilling to invest the majority of his or her savings in owning a private property.*
- Currently, around 55% of households in Hong Kong are private housing owners. For a private housing owner who has taken a 60% mortgage on his flat, a 20% decrease in property price will lead to a 50% loss in asset value. Their asset value will become of zero value if the property price falls by 40%. Levels of residential property prices and rents at the second quarter of 2001 have fallen by 53% and 30% respectively, compared with the third quarter of 1997. Prices and rents of commercial office have fallen by 64% and 35% respectively; commercial units prices and rents on ground floor have fallen by 56% and 19% respectively, and property for industrial uses have fallen by 64% and 38% respectively. There is no indication that property prices will become stable as such prices are continuing to fall. In brief, the negative-equity problem will persist. For the economy as a whole, its effect is just like a hidden time bomb that will explode at any time. Under such situation, confidence of the general public is difficult to restore.'*

It took another two years for C.H. Tung to react and to reverse his original decision. In the meantime, the revenue of the government had collapsed. The reversal of his decisions resulted in a litany of criticisms, while in fact it was a long overdue decision. Many of the critics fail to understand the rational of the land policies of Hong Kong. They do not account for the fact that land premiums are an integral part of the tax system, and that without resources coming from land, the government is technically bankrupt. The question therefore is not whether housing prices are too high, but rather whether Hong Kong can keep its existing tax structure and enjoy low land premium. The clear answer is that it is not feasible and if that is the case, the debate should be about the amount of money the government can extract from the people, directly or indirectly. But the critics, in favour of cheap housing, reject at the same time any tax increase. They thus unwittingly subvert a necessary debate about the funding of the civil service, for there was a direct link between the extravagant remuneration of the civil servants and the sky-high land premiums of the past.

- 7.- Daniel Kahneman, who won the Economic Nobel prize in 2002 for having integrated insights from psychological research into economic science, especially human judgment and decision-making under uncertainty would certainly be interested in the housing policy fiasco which provide a wealth of data supporting his theory.

- 8.- Civic Exchange, the think-tank founded by Christine Loh, has issued a research paper about the budget suggesting that the actual deficit might be only half what the crude cash accounting system reveals. The report deals in technicalities rather than on substance and missed the point that public finances should reflect for clarity the policies of a government that is in power, when it is in power. Whatever the accounting method, the government currently spent about HK\$130 billion more than it raised through normal taxation channels over two fiscal years. It is an unsustainable development.
- 9.- Civil law may be defined as that legal tradition which has its origin in Roman law, as codified in the Corpus Juris Civilis of Justinian, and as subsequently developed in Continental Europe and around the world. Civil law eventually divided into two streams: the codified Roman law (as seen in the French Civil Code of 1804 and its progeny and imitators), and uncoded Roman law (as seen in Scotland and South Africa). Civil law is highly systematized and structured and relies on declarations of broad, general principles, often ignoring the details. Common law is the legal tradition, which evolved in England from the 11th century onwards. Its principles appear for the most part in reported judgments, usually of the higher courts, in relation to specific fact situations arising in disputes, which courts have adjudicated. The common law is usually much more detailed in its prescriptions than the civil law. Common law is the foundation of private law, not only in England, Wales, and Ireland, but also in forty-nine U.S. States, nine Canadian provinces and in most countries which first received that law as colonies of the British Empire and which, in many cases, have preserved it as independent States of the British Commonwealth.
- 10.- A good example of a politically motivated decision was the inclusion of the new town of Tung Chung, located on Lantau Island into the New Territories constituency, rather than in its geographical setting (Islands constituency). It was done to avoid purposely to have a Lantau constituency, that would have challenged the Home Affairs department hold on any development on the island. A constituency would have given a sense of identity to people who have always been considered by the colonial ruler as 'second-rated citizens'. It was a prospect that the administration would not entertain and therefore the north of the island votes are diluted into the New Territories constituency, while the south ones are added to the votes of other islands that have nothing in common with Lantau. Hence, it is difficult for an elected legislator to be identified with a specific territory (see note 29 for the consequences of the dilution of elected representation at government level).
- 11.- It was announced in 1999 that US entertainment giant Walt Disney was to build a theme park in Hong Kong, at Penny's Bay (Lantau North) under a \$3.2bn deal in which the Hong Kong government was investing US\$2.88bn and Disney only US\$320m. Yet, in the joint venture, the Hong Kong Government would hold only a 57% stake. C.H. Tung announced that the park would see an attendance of more than five million in its first year of operation in 2006, rising to 10 million after about 15 years. The MTR Corporation was then asked to build an extension to the Disney park to connect it to the MTR network.
- 12.- The north and the south of Lantau are currently connected by a 5-kilometre single lane road that was paved in the 1950's. The road was closed in 1992, and the islanders were told it would reopen at a later date after being brought to a dual-lane standard. However in 1997, after the opening of the new airport situated on north Lantau, at the end of the old road, the islanders discovered that no work had been carried out and that the Transport Department had the intent to keep the road permanently closed. A mass protest forced the government to back down, and the substandard road was open with restrictions between 6am to 8pm. In the meantime, the Transport Department promised that a new road would be built to link the south to the north. But in 2000, the new project was abandoned after the environment department objected. A new mass protest from the Lantau population forced the government to relax further the restrictions on the existing substandard the road. It is currently open to all Lantau

residents from 6pm to 8 am. Restricted permit holders can use it 24 hours a day. More than 60% of the permit holders are civil servants that do not live on the island, but who get the right to use their private car so as not to inconvenience them. A new promise was made to widen the existing road. Such a project had been ruled out by the Secretary for Transport in 1997 because 'it was too difficult'!. The road works are expected to be completed in 2005, thirteen years after the administration gazetted a "temporary closure for repairs". The population of South Lantau is about 50,000 people, while more than 100,000 live now in the new town of Tung Chung, in the vicinity of the new airport. The Tung Chung road issue is a good example of administrative inefficiency, incompetence and lack of accountability. It is also a good example of the complacency of the population. In a developed democracy, the simple fact that after twelve years of restriction, 60% of the traffic has been directed to the use of the administration would have forced the members of the legislature chamber to challenge the government in the Legislative Chamber.

- 13.- The MTR has proposed to build a South Island Line on Hong Kong Island, as well as a West and a North lines. They would serve more than 1.5 million people and would reduce the number of double-decker buses congesting Hong Kong island. Yet, the projects are held up by funding problems. The total investment is about HK\$27bn. In the past, the government was indirectly financing the project, by granting land banks at no cost to the MTRC, which in turn would resale development rights on top of the MTR stations. That funding model had the supreme advantage to shift out of public scrutiny the way public projects were financed. In the long run, it transformed the MTRC into the largest real estate developer and made the public transport network funding entirely dependent on the value of property prices. With the collapse of the property prices and the ensuing prolonged freeze on land sales, the government has torpedoed its own funding model without providing an alternative. To make matters worse, it has also transformed the MTR Corp, a public company, into a semiprivate company, by issuing shares to the public with a commitment to achieve a 1 percent to 3 percent return above its costs of capital, thus making it impossible for the MTRC to shoulder start-up costs of long term developments. One way out would be for the government to contribute directly towards the capital costs as it does for the funding of public roads, but so far, without a public debate, it has refused to do so. Yet, it is contributing directly to the development of the Disney Park, which is not a public company.
- 14.- There is already an interesting precedent in Hong Kong, with the Mandatory Provident Fund (MPF), which was made compulsory in the last year of the colony. The rules are such that an employee has to contribute 5% of his/her salaries to the compulsory retirement scheme, while the employer contributes the same amount. That system looks fair, expect that the employee has to contribute only up to 5% and the maximum contribution cannot exceed HK\$1,000 per month. Therefore a way to minimize one's exposure to a compulsory contribution (that is perceived as a levy among the population) has been for many to adjust their salaries accordingly. For example, if one earns HK\$9,000 per month, one contributes at 5%, then at the end of the year, one receives the traditional Chinese New Year bonus and pays HK\$1,000 (the maximum amount). The total amount paid in a year is HK\$5,950, with a contribution from the employer (oneself as the owner of the business) of the same amount. The total levy is HK\$11,900 a year, regardless of the final income. Therefore the full 5% is paid by people earning between HK\$9,000 and HK\$20,000 per month. Then the percentage decreases rapidly to become insignificant for the elite. The civil service has been excluded from the MPF system, which weakens its legitimacy from its inception and further divides the society. For its first two years of operation, the MPF funds have registered negative returns. The main beneficiary has been the financial sector, which collects upfront fees on the management of funds thus collected.
- 15.- A consumption tax may work in a cohesive community as a complement to a rational tax structure, but as the sole basis of taxation, it is an idea that has only caught up with the elite

because it would benefit from it. Incidentally, George W. Bush, the rightist American President, is also proposing an abolition of the income tax and salary tax and their replacement by some form of taxation at the consumer level. It is also part of the political manifesto of the far-right party Front National in France.

- 16.- C.H. Tung is not known to have expressed any dissenting views, in private or in public, on any matter between 1992 and 1997. It is also true that he could argue that he was bound by a confidentiality clause not to disclose publicly the deliberations of the Executive Council, for there is in Hong Kong an extraordinary unwritten law. Executive Councillors are required to keep confidential any proceeding of the Council and not to give their direct position on any decision made. However on more than one occasion, dissenting views have been expressed, and one Exco member (Lo Tak-shing) resigned his position to object to a decision he would not support. It was in the 1980's.
- 17.- Donald Tsang, in a speech to the Legco for his last budget.
- 18.- In the 1998-1999 budget, the government released a medium range forecast up to 2001-2002 using a 5% growth assumption. To understand the magnitude of the earthquake that the public finances sustained the following year, because of the collapse of the land sales, the government had planned that the revenue will only dip by HK\$8bn in 1998/1999 (because of the property prices contraction) then would recover to HK\$211,4 in 1999/2000 before jumping to HK\$242,9 in 2000/2001 and HK\$271,33 in 2001/2002. The expenditures were planned to jump from HK\$161,66 in 1997/1998 to HK\$258,57 in 2001/2002. Yet a surplus of about HK\$10bn was expected every year. But what happened is that the revenue collapsed to HK\$150,66bn in 2001/2002 a difference of HK\$120BN, (43% lower than the forecast) while expenditures were HK\$201,53, a difference of HK\$26bn (11% lower than the forecast).

CHAPTER V - CONCLUSION

Hong Kong is facing two issues. One is political, the other one economic. Both are linked through the deficit issue.

To solve the deficit, C.H. Tung has to reform the administration of Hong Kong in depth, but to do so means that his political alliance with the civil service has to come to an end.

Is it likely to happen? It is quite possible, but Hong Kong might need first to go through a major political crisis, once it is realized that the current government is unable to solve the deficit issue as long as the civil service is keeping its privileges.

The mindset of the elite is composed of elements that have been analysed in the preceding chapters. What appears in the first place is that C.H. Tung, as the champion of the elite, is not a rationalist but a believer. Even James Tien, who seems to have a better grasp of the core issue that threatens the viability of Hong Kong, is a firm believer in a chimerical image of the city. The elite, far from building its belief on reason, moulds reason to its belief in those images which are born of their imagination.

That is why, time after time, the speeches of the officials about one issue or the other of Hong Kong always give the airy feeling that they are only grasping the superficial relations of things (49). Although C.H. Tung's declarations are steeped in economic jargon, it appears on close scrutiny that he employs it very little, if at all, to forge his thought and his conduct.

What becomes apparent when looking at the decisions made, from the housing debacle to the 6% pay cut agreement with the civil service is that the Chief Executive and his coalition partners are never influenced by reasoning. Their vision of things limited to the imagery they have of Hong Kong, does not permit of their resisting the powerful impulse that guide them. All of them have forcible convictions.

Such mentality implied a rigid mind inaccessible to all criticism and to all consideration, as could be seen in the wake of the scandal surrounding the Financial Secretary's nondisclosure of a car purchase days before announcing a substantial increase in the first registration tax of brand new cars. That attitude condemns C.H. Tung to an extreme simplicity of views. The sequence of phenomena and their results seems to escape him, as can be seen in the matter of the housing market and its spillover effect on the budget.

But C.H. Tung is not the only dreamer. The political establishment is not really different. Only its dream is different, but not really closer to reality. To consider Emily Lau, Martin Lee, Christine Loh, James Tien, Albert Chan and many other leading personalities of Hong Kong truly rational in their criticism of the leadership actually make reason despair. This is because one can only consider C.H. Tung perfectly intelligible if one admits that he is a passionate and quasi-mystical leader, and not a blundering and incompetent politician.

Zhu Rongji, who is a much more experienced politician than the Chief Executive, had perfectly understood the predicament Hong Kong is facing. That is why he pointed that a political vision is required, not the pursuit of a dream.

C.H. Tung does not run for elections and he can't be toppled by the legislature, therefore it might be arguable that he could remain a dreamer until his term is up.

There is however a factor that could change everything. That factor is the peg, the mechanism that links the Hong Kong dollar and the US dollar at a fixed exchange rate of 7.8 HK\$ for 1 USD.

Currently, the deficit, which is slowly eating up the financial reserve of Hong Kong, has not been considered a threat to the stability of the currency. Rating agencies have so far taken a lenient view of the deficit problem, on the assumption that it will indeed be solved in the coming years.

But on monetary issue, everything is a matter of perception and anticipation. As the Asian financial crisis of 1998 revealed, sound economies are not necessarily safe because they are sound. Financial crises generally occur because the herd factor is a much more powerful fundamental in the process than any economic data. If the perception turns out to be by end of 2003, or in 2004, that the deficit issue is badly handled, then a new mood might ensue.

If between 2003 and 2007, the current trend in the expenditures and the revenue remains as it was between 2000 and 2003, the government-debt-to-GDP ratio of Hong Kong will come down to the same as Australia's. This is a worrying scenario because if that comparison is made in financial circles, Hong Kong will definitely have lost its world-city aura, while today C.H. Tung still benefits from a lingering ambiguity about it.

The Hong Kong officials hope that by 2006-2007 the budget will be balanced, projecting themselves as great economic reasoners. Yet, it is clear that their hopes are not guided by reason. The Financial Secretary has constantly failed to indicate how the gap will be closed in the near future, while arguing that the last resort would be the sale of some public assets. Such a move would not address a structural problem.

The government still denies that there is one. It considers that Hong Kong can afford to spend about public expenditures in the range of HK\$200bn and finance them through various levies. The 200bn mark has not been determined by any rational economic analysis, but by considering that the current expenditures can be cut by about 10%. Any other cut would hinge on the ability to cut further the cost of the civil service.

On the revenue side, the government needs to find HK\$60bn as it is currently hovering around HK\$140bn. If the property market were to recover to the previous level of the 1990's, the government could count on an additional HK\$35bn, bringing a total revenue of about HK\$175bn. The tinkering of the tax-bands would bring about HK\$10/12bn.

Obviously the numbers do not add up. A further HK\$10bn would be needed, provided that the expenditures are really at HK\$200bn, which is doubtful. In short, it appears that more tinkering would be needed on both the expenditures and the revenue side.

This is a poor strategy, for further tinkering year after year will inevitably create the perception that the government, after running 7 or 8 years of deficit, is unable to control the expenditures of the city, or that the officials are incompetent, or both.

The psychological impact among financial analysts would be devastating for Hong Kong. The rating agencies would start to be edgy and sooner or later the peg would come under stress. With its land fund depleted by the drain of the public finances, the government will not have the resources it had in 1998 to tackle any speculative activity around the peg.

Is a devaluation of the Hong Kong dollar inevitable then? It has been a perennial question since the peg was created in 1984. Some argue that the time will come where the peg will outlast its usefulness.

That the peg served Hong Kong well is undisputable. That it is no longer welcome is among the elite a quite popular topic. But the final decision on the matter is out of the hand of the Hong Kong government. One must here consider the usefulness for the central government of China of having one of its cities with a dollarized economy. On that basis alone, there is little doubt that the peg is going to stay for a lot longer than purely local economic consideration would require.

But that brings the inevitable conclusion that if the peg were under severe stress, the likely casualty would be C.H. Tung himself, for the credibility of the system lies on the credibility of the government itself.

Thus, if public opinions in Hong Kong are unlikely to affect the political career of the Chief Executive, financial markets may. In that respect, C.H. Tung is right to claim that Hong Kong is still a world-city, for no financial market would pay so much attention to the credibility of a provincial city.

POSTSCRIPT

Few months after the publication of Asian Affairs n°19, new signs emerged that C.H Tung was not going to last his full term. The old generation of Chinese leaders had given way in Beijing to a new team, and C.H.Tung had been left with no political support in the corridor of power. China was increasingly worried that the city would become more and more a liability, while at the same time many Hong Kong tycoons were pleading for a radical change at the top because the credibility of the government was at rock-bottom. Fairly or unfairly someone had to shoulder the blame and if the Hong Kong dollar was not a target, it was only because the Chinese yuan was the talk of the day.

In China a provincial governor can be pushed out quite easily, once the decision has been made that he is starting to be a liability. In Hong Kong, the problem was more complex, because the Basic Law does not provide for a scenario where the Chief Executive could be forced out by democratic or authoritarian means. He has not authority above his head. The British government had authority over the Governor, and the dismissal of Governor Wilson, to give way of Chris Patten by John Major, did not attract undue commentaries. It was classic.

Tung Chee-hwa could only resign. The question was, would he resign, and when? The Chinese government offered him an incentive. On February 28, 2004, he was appointed to Chinese People's Political Consultative Conference (CPPCC) and few days later, a vice-president. Furthermore, he would keep a rank of Vice-Minister in the Chinese government.

Unfortunately, if Tung Chee-hwa had proven that he was bungling politician, his departure proved that he had no sense of his position and its responsibilities. As the Chief Executive of Hong Kong, his constituency was Hong Kong, but while rumors were propagated in early February that he was about to leave, he did not consider his duties to answer the Legislative Assembly when asked. He tartly told the legislators and the Hong Kong public: "I will let you know when I see fit",

Finally, a communique informed the public that "for health reasons and exhaustion", he was resigning. He did not muster the courage to make a declaration in the Legco, which would have been the proper venue. Then he immediately left Hong Kong, some say going to China, others to the United States. Former governors were going straight back to London. Maybe, he did not want to break the tradition,

The final words belong to his wife. When asked upon their return to Hong Kong if her husband was feeling much better, she misunderstood the question. "Why?" she asked. He has always been in perfect health".

Hong Kong went back to its colonial days overnight. The highest ranking civil servant became interim Chief Executive. He is likely to remain Chief Executive in title for a long while,