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1. Mr. Coler ~~Mr~~ ^{2.} _{2.}
2. Prime Minister

You may like to glance at the
conclusion on p. 11, which is an interesting
indication of how people outside are beginning
to perceive the future of Hong Kong.

Dear Robert

Knowing how little your boss has to read, it
 occurred to me that she might be interested in the attached
 memorandum by a specialist on mainland China, but I am not
 sure; so let me know if you want the usual second copy.

FERB
2.12.

Yours
Victoria

THE FUTURE OF HONG KONG

I INTRODUCTION

1. Chinese intentions towards Hong Kong after 1997 have at last become clear. This paper endeavours to examine the extent to which Hong Kong's financial viability can continue in face of these intentions.
2. At the present time the most important factor for Hong Kong's financial stability is human confidence. International investors' confidence can be secured through Chinese diplomatic guarantees. The confidence of the Hong Kong Chinese, who have reasons to distrust China, will be more difficult to sustain. As it is ultimately the Hong Kong Chinese who create the wealth of the colony, this paper concentrates on their disposition.
3. The time frame of this paper is limited to the immediate decade ahead. Long term predictions in human affairs are seldom reliable. A ten year time span already strains credibility. In the case of Hong Kong the matter is further complicated by the possibility of increasing participation in Hong Kong's affairs by the Chinese Communist bureaucracy whose competence is dubious. Moreover, prediction beyond ten years is unnecessary as financial commitments in Hong Kong normally seek satisfactory return of capital within a much shorter period.

4. In assessing the likely financial viability of Hong Kong, this paper assumes that there will be no political upheavals in China or political intransigence in Britain in the course of the next decade. Although the conclusion reached by this paper is optimistic, because of human propensity to political folly, this optimism needs to be tempered with caution.

II BACKGROUND

5. In the summer of 1982 the Peoples' Daily in Beijing (Peking), followed by the Chinese Communist press in Hong Kong, carried prominent photographs and news items of a meeting between China's leader, Mr. Deng Xiao Ping, and an internationally known Beijing publicist stationed in Hong Kong, Mr. Fei Yi-Ming. Normally such a meeting would not have warranted front page attention by the Chinese Communist press, for Mr. Fei meets Chinese leaders frequently as a matter of routine. On this occasion it was obvious that Beijing wished to draw attention to Mr. Fei's meeting with Mr. Deng in order to lend authority to what Mr. Fei had to say to the Western press immediately upon his return to Hong Kong.
6. Mr. Fei's message was that China envisages a future Hong Kong that would continue as an international financial centre, but under Chinese sovereignty. Subsequently Chinese embassies in the Western world confirmed Mr. Fei's message, and Beijing too joined the chorus, remarking that a

Sino-British accord on the future of Hong Kong needed to be reached within the next two years. However, the sense of threat implied by the short time frame of two years was later mollified by informal statements by the Chinese Prime Minister that China will take no action to resume the responsibility of Hong Kong until after 1997.

7. Throughout it all Hong Kong rocked. The colony was shaken. Many felt that the party was at last over.

III CHINESE INTENTIONS

8. To date, Chinese official statements regarding their intentions towards Hong Kong have been limited to principles. More detailed descriptions of the Hong Kong they envisage were left to informal briefings by Chinese officials to carefully selected non-Communist individuals and publicists. What has been "leaked" claims that:-
- a) Hong Kong would continue as an international metropolis beyond 1997;
 - b) Hong Kong would remain a free port;
 - c) Hong Kong would seek to maintain its position as an important world banking centre;
 - d) Hong Kong capital would remain mobile;

- e) foreign and local investors in Hong Kong would continue to enjoy financial and property rights;
- f) Hong Kong currency would be distinct from Chinese currency; but, Hong Kong notes that carried symbols of British sovereignty would be replaced;
- g) the Hong Kong police would remain in force; but the British army would be withdrawn;
- h) the Hong Kong administration would continue more or less in its present form but the Governor would be a "patriotic" Hong Kong Chinese;
- i) the question of sovereignty would be beyond discussion. It would be Chinese.

9. China's statements regarding Hong Kong should be taken with utter seriousness. It is a Chinese Communist practice to issue prior warning before participating in international adventures. Thus, in the early fifties General MacArthur was repeatedly warned by China that the Chinese forces would enter Korea should the Americans cross the 38 parallel. In the sixties India was given notice by China of her impending attack if India did not cease border provocation. In the seventies Beijing announced her intention of carrying out punitive operation against Vietnam weeks before her soldiers crossed the Sino-Vietnamese border. Now, in the eighties, China is giving notice of her intention to cross yet another international border, that which separates China from Hong Kong.

IV HONG KONG'S INITIAL REACTION

10. Whilst Hong Kong's New Territories were leased from China, Hong Kong island was ceded to Britain in perpetuity by the Treaty of Nanking in 1842. It was this perpetuity clause which gave many in the colony hope that by the time the New Territories lease expires in 1997 some form of compromise could be reached with China that would permit a renewal of the lease and the continuation of British sovereignty and British colonial administration. The sudden assertion of Chinese intransigency over the question of sovereignty shattered Hong Kong's financial confidence in late 1982. To the Hong Kong Chinese, what China envisages for the future Hong Kong denies them the political protection (British sovereignty) of the judicial machineries (colonial administration) that provide them with their present unique existence which sets them above the horrors of arbitrary rule that characterises China.
11. But was the expectation of the continuity of British sovereignty over Hong Kong ever founded in reality? Sovereignty, when it coincides with geographical and ethnic integrity, is tantamount to the primaeval territorial instinct, and politicians who have relinquished territorial sovereignty are historically condemned. The Treaty of Nanking that relinquished Chinese sovereignty over Hong Kong is regarded by the Chinese as the first incident of national humiliation by the West that precipitated more than half a century of foreign domination.

None of the revolutionary Chinese governments since 1911 were ever reconciled to the legality of the Nanking Treaty, and no modern Chinese politician could afford to appear to recognise it; least of all the present elder generation of Chinese Communist leaders who, as Marxists, cannot enjoy the solace of a belief in religious afterlife, but must instead seek immortality through the pages of history. Their need for a desirable image in the annals of Chinese national history is probably paramount. To stain this image would deny them the only form of a sense of afterlife that true Marxists can entertain, and rob them of the very accolade that they consider as their ultimate reward after a life long career of historical significance.

12. The expectation that China would permit a continuity of British sovereignty over Hong Kong beyond 1997 was, therefore, unrealistic. That the disappointment caused by this realisation could so adversely effect Hong Kong's financial market in 1982 is an indication of the extent of human vulnerability to self delusion, not a manifestation of the beginning of the end of Hong Kong's prosperity.

V DISPOSITION OF THE HONG KONG CHINESE

13. Nevertheless, the reaction of the Hong Kong market in late 1982 to China's sovereignty claim reflects its unpopularity. Would there, therefore, be a mass exodus of individuals, a rush of outpouring

capital, and a fatal crippling of the will of those remaining behind? Would Hong Kong soon be reduced to the same empty apathetic shell of a once great city that is Shanghai today?

14. In 1976 a Chinese residing in the West remarked in private after a visit to China that if the Chinese were free to leave their country, the only thing that would be left standing in the streets of Chinese cities would be the electricity poles. The instinctive reaction of most Hong Kong Chinese residents towards a Chinese Communist takeover of Hong Kong is no doubt similar to that of their compatriots in China; to leave as rapidly as possible. But, like their compatriots in China, only a very few could in reality achieve mobility.

15. The poor, who constitute the vast majority of the population of Hong Kong, simply will not be able to move. Their desperation, coupled with aspirations of a better life that could be available for them under the British colonial administration, had always been responsible for much of Hong Kong's remarkable achievements. Their very immobility in fact nourishes a fanaticism for survival and self improvement. As long as there are reasons for them to believe that, despite eventual Chinese sovereignty, the dead hand of Communism will not touch that aspect of Hong Kong's environment which enables them to seek advancement, their industriousness and ingenuity will continue to fuel the prosperity of the colony.

16. Ever since the advent of Communism on mainland China, it has been the tradition of the Hong Kong rich to maintain residences in safer havens overseas. They are known as the "tooth brush" brigade, because when the contingency arises all that they need to do is to pack a tooth brush and go. Thus the Hong Kong rich can remain on the island until the eleventh hour. This may now be a necessity for much of their wealth in recent years has been concentrated in property investments that are undisposable in the present climate. For the time being, it is to their advantage to remain in Hong Kong to maintain confidence lest the property value falls further. Besides, where else in the world can they make money as freely as they can in Hong Kong?
17. The middle class, who cannot share the instant mobility of the rich, but who need not necessarily surrender to Chinese Communist rule with the passivity of the totally immobile poor, is the section of the Hong Kong society who will most likely seek immediate emigration. However, they are replaceable. Once Hong Kong's continued stability has become apparent, expatriates could be engaged in place of the absent Hong Kong Chinese professionals. In any event, many of those who leave now are expected to return once they have solved their problems of residences in the West, and, thus join Hong Kong's "tooth brush" brigade.
18. Exodus of talent and outflow of accompanying capital have in fact been familiar phenonema to post Second World War Hong Kong. Whenever the threat of

Communism has loomed large across the Chinese border in the past three decades a number of those who could leave Hong Kong left. But, inevitably, those who remained ensured that Hong Kong continued to prosper. Providing that the right political climate continues, this same pattern could repeat itself in the years to come.

VI POLITICAL CLIMATE

19. The right political climate may well continue. The present Chinese policy towards Hong Kong is not solely motivated by the amount of foreign exchange China derives from the colony. If it were, it would not have been adequate guarantee for Hong Kong's future stability, for economic pragmatism is the logic of the mercantile West, not the Feudal East where political power is paramount. Long term political calculation dominates Chinese Communist thinking. Unless this dimension is considered, Chinese intentions towards Hong Kong cannot be properly determined.

20. Political power, exclusive of economic consideration, devastated Maoist China and made a mockery of China's pretension to greatness. Present Chinese Communist leaders now realise that they cannot achieve their ultimate political objectives of a great China without pragmatic economic planning. It is fortunate for Hong Kong that this realisation took place at a time when Hong Kong's own future needed to be formulated. To the Chinese leaders Hong Kong now suddenly represents an example of modern sophistication which, once under Chinese sovereignty, the rest of China can emulate at will.

21. As Hong Kong now has a potential role in China's political programme of modernisation, it is in China's vested interest to preserve Hong Kong's present prosperity. Without it there can be no future prosperity, and since China desires Hong Kong back as a glittering prize, she will want it returned undamaged. To ensure this, Chinese Communist institutions in Hong Kong have recently instigated various actions to sustain the financial viability of Hong Kong, and to convince the Hong Kong Chinese that their valued pursuit of individual aspiration could continue under Chinese sovereignty.

22. There is another secondary political consideration why China may want to preserve the climate of successful free enterprise in Hong Kong. China has often linked Hong Kong's potential fate with that of Taiwan's. Senior Chinese officials have now suggested in private conversations that as China has exhausted her persuasiveness for attracting Taiwan to the fold, she may be able to demonstrate to Taiwan, through her treatment of Hong Kong, the innocuousness of becoming part of the People's Republic. If China's Hong Kong policy is indeed intended in part as an enticement to Taiwan, then China will do her utmost to protect Hong Kong's present life style. Whether Hong Kong could realistically be a bait for Taiwan is beside the point. What matters is that as long as such thinking is prevalent in China, capitalism is likely to remain in Hong Kong.

VII THE UNKNOWN

23. But what would happen after the next decade, when the Hong Kong Chinese rich decide that the eleventh hour has arrived? And what would happen once China had assumed sovereignty over Hong Kong? Could the greed of poverty-ridden Communist China restrain itself from incursions into the economic success of the private individuals and institutions of Hong Kong? Could Communist Chinese officials, who were bred in the system of arbitrary power where the final reward for attainment of office was often the privilege to abuse this very office with impunity, refrain from interfering with the independent judiciary system of Hong Kong? No doubt as 1997 draw inexorably closer the deterioration of the quality of life in Hong Kong will accelerate. The worst may well happen then. Much will depend upon the extent to which Communist China can achieve a mature comprehension of the complex prerequisites essential to the successful governing of a modern international metropolis. Obviously, the situation of Hong Kong needs to be reassessed again before the end of the ten year period covered by this paper.

VIII SUMMARY

24. In summary, Hong Kong's future financial viability can only be assessed within a context of acceptance of eventual Chinese sovereignty over Hong Kong, not from market trends that were caused by initial disappointment in unrealistic expectations that

precluded Chinese sovereignty. The inevitability of Chinese sovereignty caused unease amongst the Hong Kong Chinese. Henceforth there will be emigration and flight of capital, but not of the magnitude that will irreparably damage Hong Kong's financial viability. Because China's present policy of national economic development envisages a role for Hong Kong, it is advantageous for China to foster, rather than cripple, the enterprising spirits of the Hong Kong Chinese. In the circumstances, new talents will soon emerge and new wealth will soon be amassed to replace those that have left. China's claim of sovereignty, therefore, should not be perceived as a threat to Hong Kong's future financial viability. On the contrary, because of this claim, it is now in China's political interest to protect the colony's prosperity prior to, and after, 1997.

VII CONCLUSION

25. In conclusion, the party is not over!

21st March, 1983.