

# WTO, CEPA, and the Greater Pearl River Delta Region

China's continuing process of economic liberalisation and opening will have an important influence on the economies of the Greater Pearl River Delta region. The two main features of this process are China's accession into the World Trade Organisation (WTO) and the Closer Economic Partnership Arrangement (CEPA) between China and Hong Kong. Under the accession agreement that brought China into the WTO in 2001, it is gradually opening up to both trade and investment for companies from around the world. The Closer Economic Partnership Arrangement (CEPA) was signed in 2003 by the Central People's Government and the Government of the Hong Kong Special Administrative Region and came into effect from 1 January 2004. China's commitments under CEPA in services included accelerated time frames for various market openings already committed to under the WTO, in effect giving Hong Kong companies a time advantage over firms from other places. Under CEPA I and II, zero-tariff treatment was extended to most products, and preferential access to the Chinese Mainland was granted across a broad spectrum of service sectors.

CEPA is an open platform for trade liberalisation that is being extended on an ongoing basis. With CEPA III, effective from 1 January 2006, all finished goods, except for prohibited articles and articles that are subject to special requirements, may be exported from Hong Kong to the Chinese Mainland tariff free, upon application by Hong Kong manufacturers and compliance with CEPA rules of origin.<sup>7</sup> CEPA III broadens access by Hong Kong service suppliers to Chinese Mainland markets in a variety of service sectors, including accounting, audiovisual services, banking, construction, distribution, legal services, tourism, and transportation. CEPA IV, effective on 1 January 2007

<sup>7</sup> Further details are available in Invest Hong Kong's booklet 'The CEPA Benefits', which can be downloaded from <http://www.investhk.gov.hk>.

includes 15 market-access measures in ten sectors including legal services, tourism, construction, information technology, conventions and exhibitions, audiovisual services, distribution, air transport and road transport services, and individually owned stores.

Both WTO entry and CEPA are best understood as steps in a reform process that started in China in 1979 and will continue well into the future. Given the international orientation of the Greater Pearl River Delta region, and the fact that the region has been operating at world quality and cost standards for years, it is not far-fetched to conclude that the region will receive a strong boost from greater liberalisation and openness in China's economy. In addition, WTO accession and CEPA should stimulate substantial growth in trade and investment in the Pearl River Delta region. Much of this trade and investment will involve Hong Kong, which also will be able to provide far more of the services to the Pearl River Delta region that major economic cities around the world provide to their surrounding areas than has been the case to date.

China's accession to the WTO will substantially increase the openness of the Pearl River Delta region's economy. One would expect that imports would rise in the region faster than in many other parts of the Chinese Mainland, given its affluence and its proximity to Hong Kong. Many multinational companies will find it worthwhile to extend their sales and distribution networks from Hong Kong into the rest of the region, as many Hong Kong-based firms are already doing. The greater openness in services called for under the WTO accession agreement will greatly open China's markets to multinational service providers. In this regard, the Pearl River Delta region, with its proximity to world-class service providers based in Hong Kong, should be a strong beneficiary. In light industry, WTO entry will allow the export-oriented firms of the Pearl River Delta region to expand their markets, while the industries in China that will potentially be hurt by greater openness are not generally found in the Pearl River Delta region. Thus openness is likely to be a boon to Pearl River Delta region consumers and the local,

Hong Kong, and foreign companies operating through Hong Kong into the region. By making it easier to import intermediate goods and capital equipment, greater openness should allow Pearl River Delta region production facilities greater scope to leverage their competitive advantages in local and global markets.

With CEPA, the Greater Pearl River Delta region is integrating even faster than was previously the case. The Greater Pearl River Delta region already exhibits a very high degree of integration between Hong Kong and the Pearl River Delta in light manufacturing. Powerful market forces favour a similar degree of integration in services that have historically run up against restrictions on outside firms in the Chinese Mainland. In many service sectors, CEPA is lowering barriers of entry into the Chinese Mainland for Hong Kong service providers before China's WTO commitments take effect, allowing firms based in Hong Kong an early mover advantage. Their pre-existing informal networks are facilitating the setting up of new businesses across the region. Meanwhile, Guangzhou, Shenzhen, and other Pearl River Delta cities are working to stay at the forefront of China's liberalisation in part because they see the benefits of greater interaction with Hong Kong. Pearl River Delta-based firms are also moving into Hong Kong. These trends are already resulting in new businesses, greater efficiencies, and a much broader portfolio of choice for customers. CEPA can be expected to benefit the Greater Pearl River Delta region relative to other regions in China for the foreseeable future.

The opening up of Chinese Mainland markets under WTO and CEPA will enable Hong Kong to serve as a high-end services base for South China. With the emergence of a consumer economy in the Pearl River Delta region, we expect to see high-end, international services provided from Hong Kong for South China, domestic services for the South China region provided from Guangzhou, and services for the manufacturing heartland of the eastern Pearl River Delta provided from Shenzhen.