

**Economic Summit on
“China’s 11th Five-Year Plan and the Development of Hong Kong”
Logistics and Maritime Services**

(Translation)

Purpose

This paper presents a preliminary analysis, from the perspective of the Government and public sector, of the opportunities and challenges brought by the 11th Five-Year Plan to Hong Kong’s developments in logistics, air cargo, port and maritime services. The paper aims to initiate discussion in the community with a view to developing a practical “action agenda” in the next few months.

Background

2. Historically, logistics referred generally to the transportation of goods. With the rapid expansion of global sourcing and increasing specialization in production over the past decade, the supply chain has been extended to cover more and more regions around the world. In parallel, there has been rising demand for integrated logistic services, especially those in support of transportation and complemented by holding and processing of goods. This movement towards concurrent and convergent activities underlies value-added logistics (VAL). There is no consensus definition of VAL. Typical examples of VAL involve labeling and packaging, light assembling between pickup and delivery, cargo tracking and tracing, IT and inventory management support.

3. Generally speaking, VAL can best be understood as a profile which incorporates processes designed to efficiently support and facilitate different elements in the supply chain. In the same way that supply elements are 'chained', activities and services are inter-related and inter-dependent within the VAL profile. With changes in technology, economic-socio-political environment and modus operandi of business organizations, the VAL profile will continue to evolve, covering different processes at different times.

Global Trend of Logistics Development and Competition

4. In the past, trade meant coordinating exchange and logistics merely transportation. Globalization and the rise of the Mainland China as a manufacturing base and then as a large market have led to a facelift of the trading and logistics services in Hong Kong. Technological improvements, notably in information technology, have also made it possible for firms to enhance their competitiveness by reducing inventory cost and turnaround time through improving the efficiency of their supply chain. Hong Kong companies, taking advantage of the enormous growth in manufacturing in Mainland China, have specialized more and more in supply chain management. They now source raw materials, co-ordinate the production, consolidate and distribute products, and manage inventory for large chain stores in Europe and the United States in a timely and efficient manner.

5. To meet the global demand in procurement, transportation, documentation and distribution of raw materials and finished products, the logistics industry has progressed from first party to third party logistics. The expansion in market size and the increasing sophistication of the whole industry have made it possible for a third party to provide logistics support to users in a cost effective manner. In order to achieve a seamless supply chain from the sourcing of material to timely delivery of finished products, logistics service providers have to ensure against any disruption or delay in the whole process, especially if high-value and time-critical merchandise is at stake. Faced with this global trend, Hong Kong does not only need to provide effective logistics services to South China exporters, but also needs to provide multinational chained corporations and large manufacturers with one-stop supply chain management service, in order to become a regional procurement and distribution centre. With the rapid transmission of electronic messages and the rise of e-logistics, Hong Kong also needs to

compete with other Asian and Mainland cities in the development of virtual logistics.

Economic Contribution

6. Trading and logistics is a major industry in Hong Kong. In 2004, this sector generated HK\$346.9 billion in value added, equivalent to 27.7% of GDP (Annex 1). Persons engaged in trading and logistics numbered 804 600 or 24.3% of the employed population, of which 198 400 were in logistics (Annex 2). The value added of the logistics sector increased at an average annual rate of 5.9% during 1999-2004, reaching HK\$67.2 billion. The percentage share of logistics in Hong Kong's GDP also increased from 4.2% in 1999 to 5.4% in 2004. It should be noted that trading and logistics create demand for other services such as banking, insurance and a wide range of professional services. Such indirect economic contributions are not included in the above-quoted figures.

7. In Hong Kong, the Census and Statistics Department conducts surveys on the economic contribution, in terms of value added in GDP (GDP VA), of the six logistics sectors, namely land freight transport, water freight transport, air freight transport, ancillary services, storage and postal and courier services. The figures from 1999 to 2004 are shown in Annex 2. Logistics services for water freight transport and air freight transport together accounted for 80% of the total income generated. In particular, air freight transport registered the highest per capita income and the fastest growth among the different modes of freight services.

8. In terms of per capita GDP VA, maritime services (i.e., shipowners and operators of sea-going vessels and shipbrokers) had the highest VA per capita, especially for 2003 and 2004 (Annex 3), because maritime services provide high yield with a relatively small number of employees. The soaring freight rates and global demand for maritime transport services in recent years have also contributed to the substantial growth of this sector. In terms of ratio of GDP VA to business receipts of major elements in the sub-sector, specialized service-oriented activities such as shipbroking, ship management and cargo inspection services, and infrastructure-based activities such as container terminals, airport and air cargo terminal services produced relatively high margins (Annex 4).

9. Apart from the above measures, another crucial factor for gauging the economic significance of individual sub-sectors within the logistics

industry is their ability to generate employment at different skill levels. In terms of job opportunities generated, sea freight transport had made greater contribution to Hong Kong than air freight transport. The number of establishments and persons engaged in the various sub-sectors of logistics industry are at Annex 5. More importantly, VAL services integrate the core transport functions along the supply chain. Integration, innovation, comprehensiveness and economies of scale are all keys to sustaining the competitiveness of Hong Kong's trading and logistics sector.

Support from the Central Government

10. The country's 11th Five-Year Plan (2006-2010) outlines the long-term visionary plans for social, economic and infrastructural developments up to 2020. In this plan, the Central Government recognizes HKSAR's strategic position, and expressly supports Hong Kong in the development of our logistics industry and in consolidating our status as an international maritime centre. Making full use of Hong Kong's strength as a regional economic centre, in the promotion of the four pillars of Hong Kong's economy (i.e. financial services, tourism, trading and logistics, and professional and producer services), will have profound implication for the future development of HKSAR, the Pearl River Delta (PRD) and the country.

Opportunities Brought by the 11th Five-year Plan

11. Under the auspices of the 11th Five-Year Plan, Mainland China's industrial production, consumer spending and external trade are expected to maintain a steady yet relatively fast-paced growth. Its overall import/export business will continue to provide ample opportunities for Hong Kong's trading and logistics industry, despite keen competition from other Mainland cities. Closer to Hong Kong, infrastructure developments in the PRD region and the gradual evolution of geographical clustering of economic activities in South China will also provide opportunities for Hong Kong as a logistics hub in future.

International positioning of logistics, air services, port and maritime services

World's Busiest Air Cargo Centre

12. Since 1996, Hong Kong has been the world's busiest air cargo centre. Annex 6 shows that in the past 10 years, the average annual growth

rate of air cargo volume reaches 9%. Air cargo is time-critical, so frequent flight schedules, worldwide network, efficient cargo handling system, and simple and clear customs clearance procedures are all the more important. Hong Kong has advantages in all these aspects. There are currently some 80 international airlines at the Hong Kong International Airport (HKIA) operating about 5 200 scheduled flights between Hong Kong and some 140 global destinations (including 36 Mainland cities) per week, providing speedy and efficient air cargo services. The flow of people in Hong Kong is vigorous because of its superior geographic location, and the resulting frequent passenger flights provide enormous air cargo space. At present, around 43% of the air cargo volume is transported by passenger flights. Cargo transport and passenger transport compliment each other, enabling Hong Kong to become the regional hub and world's busiest air cargo centre.

Challenges

13. The regional cooperation of Pan-PRD will further expand Hong Kong Port's (HKP) and airport's cargo hinterland. It will also speed up the economic development of the inland provinces and western region in the Mainland. Nonetheless, Hong Kong has to strengthen its water, road and air connections with most cities in the Pan-PRD region.

14. Continuous liberalization of the air transport service industry in the Mainland will lead to a growing number of direct international flights between Mainland cities and overseas countries, which will impact Hong Kong's position as the major gateway to the Mainland. Neighbouring regions have also stepped up their investment in airports (such as Seoul and Bangkok) in a bid to become the premier transshipment hub for air cargo in the Asian-Pacific region. Moreover, the high concentration of airports within the PRD region, the limited airspace for civil aviation and the defective designs of air routes and flight procedures have constrained the capacity of air traffic management, and may hinder the further expansion of Hong Kong's aviation industry. Our cost of transporting air cargo is higher than Mainland airports'. We have to maintain our frequent flights schedules and operation with economies of scale to reduce cost and prevent loss in cargo volume.

Sea Transport

15. Hong Kong Port (HKP) is one of the busiest container ports in the world. The nine container terminals, with a total of 24 berths, in Kwai

Tsing provide a handling capacity of over 18 million TEUs per annum. In addition, mid-stream operation, the River Trade Terminal and Public Cargo Working Areas provide alternative facilities for handling waterborne cargo. Our port handled 22.6 million TEUs in 2005. There are some 80 shipping lines operating about 500 calls per week to over 500 destinations globally. Some 232 000 ships, including about 39 000 ocean vessels and about 193 000 river vessels, visited our port in 2005. Our terminals boast a record of 40 lifts per crane per hour. Every minute we save in the turnaround time of a 6000-TEU container vessel (with a daily chartering rate at about HK\$1.56 million) at our terminals through efficient port operation means a cost reduction of HK\$1,083.

16. Since 1992, except for the year 1998, HKP has been the world's busiest container port for 12 years, with the largest container throughput. In 2005, Hong Kong ranked second to Singapore (Annex 7). Hong Kong and Singapore serve different hinterlands, so their growth of throughput is not at the expense of each other. There is no direct competition between them. Besides, Singapore's port is operated by the government's Maritime and Port Authority. The Singapore Maritime and Port Authority has investment in ports worldwide (including Hong Kong), and with its own shipping company. All in all, its mode of operation is different from the private-sector terminal operators in Hong Kong. Its Maritime and Port Authority also has greater influence over port charges and port operation than the Hong Kong Government.

17. Hong Kong's loss its status as the world's largest port is actually due to the rapid growth of Mainland ports, which alters HKP's premier position in the handling of South China cargoes (Annex 8). In face of competition from the South China ports and the Mainland container trucking industry, the share of South China container cargoes handled by Hong Kong's cross-boundary container trucking sector has been decreasing since 2003. The rise of Shenzhen ports is posing direct and severe challenges to HKP.

Opportunities

18. HKP is one of the lifelines of the HKSAR economy. The core port industries' direct and indirect economic contributions constitute around 4% of Hong Kong's GDP. About 110 000 jobs or 3.2% of the total employment are closely linked to the port. With sustained growth for more than a decade, Hong Kong has established itself as a world leader in

port management and operation, thereby laying a solid foundation for future development.

19. Due to cost consideration, the cargo source has extended from the eastern to the western side of the PRD region in recent years. This trend will continue into the future. Continuous port developments in the PRD region will substantially enhance its capacity in water freight transport. Until the supporting road connection is fully developed, river trade transport will remain the key transport mode for cargoes from the western PRD. This is expected to bring new opportunities to the HKP.

20. Meanwhile, the region's economic and trade growth in the medium to long term will give momentum to cargo growth and present growth opportunities for HKP. The construction of the Hong Kong-Zhuhai-Macao Bridge will establish on top of water freight transport, direct road link between Hong Kong and the western PRD; upon the commissioning of the Bridge, cargo can also be trucked directly to Hong Kong for shipment to other countries. This will expand HKP's cargo hinterland and help strengthen Hong Kong's position as the hub port and logistics centre in the region.

Challenges

21. New ports in Shenzhen, with operation and management largely modeled after Hong Kong terminals, pose keen competition for direct ocean cargo to and from South China. In fact, with the rapid growth in external trade of South China, its total trade volume has far exceeded the capacity of HKP. In 2005, HKP and Shenzhen ports together handled 39 million TEUs. The capacity of Shenzhen ports is expected to almost double within the 11th Five-Year Plan period, intensifying the competition between Hong Kong and Shenzhen for South China cargo.

22. Port expansion and ever increasing vessel capacity of vessels will provide more options for transshipment cargo. For instance, at present there is no direct competition for direct cargo between Hong Kong and Shanghai, as the latter's cargo source is the Yangtze River Delta region. However, the development and expansion of Shanghai ports will attract more direct shipping calls, enabling it to become a transshipment centre. In the long run, it might compete with Hong Kong for transshipment cargo.

23. The Mainland and Taiwan reached a consensus in mid-2006 to

extend the Spring Festival passenger charter flight services to the Ching Ming, Dragon Boat and Mid-Autumn Festivals, and allow the operation of cargo charter flights for specified purpose. The first cargo charter flight arrived at Shanghai from Taiwan in late July. The arrangement is definitely a breakthrough toward direct cross-strait cargo flow. However, cross-strait merchandise trade is still dominated by sea freight transport. Thus when direct link between Mainland China and Taiwan is fully established and extended to sea freight transport and scheduled services, the impact on Hong Kong's status as a transshipment hub for cross-strait passenger and cargo flows will be more apparent.

24. In 2005, a total of 0.9 million TEUs* transshipment cargo between the Mainland China and Taiwan went through the HKP, accounting for 5% of our laden container throughput. Of all the transshipment containers handled by HKP from both sides of the strait, 80% are related to the South China region, with the remaining 20% coming from or moving to ports outside the PRD region.

25. Once direct sea link for cross-strait freight transport is established, Hong Kong's position as an entrepot for cargo between Taiwan and non-PRD ports will bear the brunt of the impact, due to geographical and cost considerations. These transshipment cargoes, nevertheless, accounted for only 1% of Hong Kong's total laden container throughput. Whether the seaborne cargo between South China and Taiwan will continue to be routed through Hong Kong will depend on the competitiveness of HKP relative to other ports in South China.

26. Hong Kong/Guangdong cross-boundary trucking is an important segment of Hong Kong's logistics industry, representing a major link between Hong Kong and the South China cargo source. The "Study on Hong Kong Port – Master Plan 2020" (HKP2020) commissioned by the Hong Kong Government in late 2004 noted that it costs about US\$300 (HK\$2,340) more for a container from Dongguan to the US to be routed through Hong Kong than through Shenzhen. The cost comparison is set out in Table 1 below:

* Apart from transshipment cargo, HKP handled 346 000 TEUs of direct imports from Taiwan and 90 000 TEUs of exports to Taiwan in 2005. According to the merchandise trade statistics, 80% of the import cargo from Taiwan was re-exported to the Mainland and 40% of the export cargo to Taiwan was imported from the Mainland.

Table 1: Total Through Cost Comparisons

Industry data as at mid 2004, US\$ (From Dongguan to the US west coast)	Via Hong Kong		Via Yantian		Via Shekou/Chiwan	
	20ft*	40ft	20ft	40ft	20ft	40ft
1 Ocean Freight Rate (Basic); +/- \$50**	2,000	2,700	2,000	2,700	2,000	2,700
2 Fees#	599	1,014	579	994	579	994
3 Truck to Port Terminal	308	333	128	154	141	167
4 Terminal Handling Charge (THC)	274	366	141	269	141	269
Total	3,181	4,413	2,848	4,117	2,861	4,130
Differential: HK Relative to Shenzhen	+\$333	+\$296				

Remarks: * 20ft means a 20 Foot ISO container (1 TEU), and 40ft means a 40 Foot ISO container.

** Average based on consultation with shipping lines – agreed rates between a specific shipping line and a specific customer may diverge from this figure.

Fees include Destination Delivery Charge (DDC), Fuel Adjustment Factor (FAF), Bunker Adjustment Factor (BAF) and Declaration Fee.

Source: Stakeholder consultations.

The key factors contributing to these cost differentials are the road haulage costs and the terminal handling charges. A main challenge facing HKP is how to narrow the difference in the transport cost.

27. In this connection, the Government has been discussing with the Mainland authorities to pursue on behalf of the industry relaxations of restrictions on cross-boundary trucking and extension of operating hours of inland control points, with a view to enhancing flexibility and efficiency of cross-boundary trucking. The industry will also need to increase its own operational efficiency to strengthen the competitiveness of Hong Kong. Yet the industry has different views over how to reduce costs; some advocate the importation of Mainland container truck drivers, others request that the container terminal operators and shipping lines to reduce the terminal handling charge.

28. Promotion of smooth freight flow through efficient customs clearance is an objective generally embraced the logistics industry. However, there are diverging views as to whether the establishment of an express customs clearance channel between container terminals in Hong Kong and specified logistics parks in the Mainland will serve the best interests of the industry and Hong Kong at large. Out of consideration

that saving customs clearance time will enhance cargo handling efficiency, terminal operators are inclined to support the establishment of such an express channel. However, the trucking industry worries that the proposal will take the long-haul trucking business away from them, leaving them with only shuttle service between Hong Kong and the specified logistics parks. Different sectors in the logistics industry are generally of the view that it is necessary to assess the cost effectiveness of the proposal, and to evaluate how an express channel connecting a designated logistic park in the Mainland will affect Hong Kong's cargo distribution, consolidation, delivery, storage and warehousing businesses.

Response Actions

29. Against the above mentioned challenges and opportunities, the Government and the industry have adopted a number of measures to strengthen Hong Kong's position as a logistics hub.

30. In an effort to strengthen Hong Kong's status as the most preferred international transportation and logistics hub in Asia, the Government is dedicated to promoting services integration in a seamless supply chain, moving Hong Kong further up the value chain, and providing infrastructure and business environment conducive to the development of the logistics industry. To gauge the actual needs of the industry, the Government engages business leaders through the establishment of the Hong Kong Logistics Development Council (LOGSCOUNCIL). We draw on their expertise and wise counsel in the formulation of initiatives for logistics development. In addition, from time to time the Government and the Mainland discuss and study issues related to the developments of cross-boundary transport infrastructure, with a view to ensuring that our infrastructure construction can tie in with the needs for social and economic developments.

Enhancing Cross-boundary Trucking

31. To enhance the competitiveness of Hong Kong's logistics industry, the Government seeks to improve cross-boundary trucking efficiency so as to strengthen Hong Kong's road connectivity with the cargo sources in Mainland China and reduce cross-boundary trucking cost. In the context of the Hong Kong/Guangdong Co-operation Joint Conference, both sides have achieved good progress in the following measures –

- The “four-up-four-down” and “one-truck-one-driver” rules were relaxed in 2005, thereby increasing the flexibility of the cross-boundary trucking industry in the deployment of equipment and drivers;
- The Guangdong Provincial authorities also agreed to extend the operating hours at four inland control points at Dongguan (i.e., Fenggang, Changan, Huangcun and Taiping) in 2005, taking into account the cargo volume and actual needs of different regions. To further enhance customs clearance efficiency, a new inland control point at Liaobu in Dongguan will be put to operation before end-2006, while the existing one at Huangcun will be closed. This new control point will adopt an improved clearance system for more effective and efficient inspection.

Harnessing Information Technology

32. Strengthening information connectivity is also key to smooth freight flow. As a matter of fact, modern logistics services and seamless supply chain management cannot be achieved without the application of advanced information technology. Hong Kong’s strength in its free flow of information has laid foundation for e-logistics development, which in turn can bring this strength into full play.

33. With these considerations in mind, the Government, through LOGSCOUNCIL, works together with the industry to promote the development of the Digital Trade and Transportation Network (DTTN) System. The DTTN, launched in December 2005, provides an open, neutral and secure e-platform to facilitate information flow along the supply chain in an efficient and reliable manner. DTTN can reduce paperwork, minimize human errors in the process and thus save time. DTTN can also help promote the adoption of information technology in particular by the small and medium-sized enterprises, and encourage the logistics industry to improve on the provision of high quality, high reliability and more efficient services, thereby enhancing their competitiveness in the market.

34. Through LOGSCOUNCIL, the Government also jointly runs a pilot project with the Hong Kong Productivity Council on an On-Board Trucker Information System (OBTIS) to improve trucking efficiency through advanced technologies. The pilot focuses on the application of

electronic communication technologies in the operation of container trucks, with a view to enhancing interconnectivity among truckers, carriers, shippers, terminal operators and potentially other stakeholders, increasing flexibility and effectiveness in fleet management, as well as maximizing the load factor and utilization of the entire trucking fleet in Hong Kong.

35. Besides, the “Hong Kong R&D Centre for Logistics and Supply Chain Management Enabling Technologies”, funded by the Innovation and Technology Commission and jointly managed by the University of Hong Kong, the Chinese University of Hong Kong and the Hong Kong University of Science and Technology, came into operation in April 2006. The Centre aims to assist the logistics industry to adopt technologies applicable to logistics services and supply chain management so as to boost their competitiveness. The focus at the initial stage is on the use of radio frequency identification (RFID).

Improving Air Transport Facilities and Efficiency

36. The Airport Authority (AA) and its business partners are making significant investments to further improve the facilities and efficiency of the Hong Kong International Airport (HKIA).

- To upgrade the airport passenger handling facilities, AA completed its expansion works at East Hall of Passenger Terminal Building (PTB) in March 2004 to increase the passenger handling capacity. The second PTB cum SkyPlaza, a multi-purpose development comprising retail, commercial and other passenger facilities due for completion at the end of 2006, will provide a variety of services to attract visitors from all over the world to use HKIA. In addition, AA constructed five additional taxi-in/taxi-out aircraft parking stands in 2005 to meet the airlines' request for lower operating cost and shorter turnaround time. With over 40% of air cargoes in Hong Kong being transported by passenger flights, frequent passenger flights will also contribute to the enhancement of freight services.
- On cargo handling facilities, following the commissioning of DHL Central Asia Hub with a handling capacity of 160 000 tonnes per annum in June 2004, DHL has further invested US\$110 million to expand the Hub. The expansion works, upon completion in 2007, will increase the Hub's handling capacity to 700 000 tonnes per

annum. Four additional cargo freighter parking stands were constructed by AA in 2005, bringing the total number to 25. Ten additional stands are expected to be in operation in September 2007. Asia Airfreight Terminal expansion works are also underway, which will increase the terminal's handling capacity from about 0.6 million tonnes to over 1.5 million tonnes per annum.

- Regarding other ancillary facilities, the Hong Kong Aircraft Engineering Company Limited (HAECO) commenced in August 2005 the construction works of its second hangar, which is expected to be commissioned at end-2006. The construction of a third one is under planning. Meanwhile, AA is carrying out resurfacing works on the runway.

37. The Government also continues to progressively liberalize our air services to further expand our aviation network.

- There are currently some 80 international airlines at the HKIA operating about 5 200 scheduled flights between Hong Kong and some 140 global destinations (including 36 Mainland cities) per week. We will continue to proactively implement the policy of progressive liberalization of our air services with a view to further expanding our aviation network.
- Hong Kong has so far concluded bilateral air services agreements (ASA) with 55 civil aviation partners and initialed texts with seven others. We also review our air services arrangements with our civil aviation partners from time to time. Over the past three years, Hong Kong has concluded five new ASAs and initialed two others. In addition, we have removed all the restrictions on bilateral passenger and freight transport with 14 civil aviation partners, and have conducted over 40 rounds of negotiations and reviews to expand the air services arrangements with more than 30 civil aviation partners.
- Meanwhile, the air transport arrangements between Hong Kong and Mainland China also saw significant expansion in recent years. Following a 40% increase in total capacity in 2004, a further increase of 10% was recorded in 2005. New arrangements were concluded in 2006, lifting the limit on passenger capacity for over

60% of destinations and increasing the total passenger capacity for the rest of the destinations by 40%, starting from the summer of 2007. With regard to freight transport, the capacity limit between Hong Kong and the great majority of destinations in the Mainland will be lifted. Such arrangements will further strengthen the aviation links between Hong Kong and the Mainland, enhance the competitiveness of HKIA and maintain Hong Kong's status as an international and regional aviation centre.

38. The Government coordinates closely and proactively with the civil aviation authorities of the Mainland and Macau to explore ways to achieve more efficient use of limited air space and to bring overall improvement to air traffic flow by optimizing airspace layout and enhancing coordination of air traffic control, in order to cope with the increasingly rapid development in civil aviation.

Enhancing HKP's Attractiveness and Competitiveness

39. In face of the rapid growth in our neighbouring ports, the Government is committed to making HKP more competitive. The Government completed the HKP2020 Study in late 2004. The main objective of the HKP2020 Study is to formulate a competition strategy and a master plan for Hong Kong's sustainable port development over a 20-year time frame. In light of the recommendations of HKP2020, the Government seeks to address the cost differential between HKP and the neighbouring ports, improve customs clearance efficiency and provide more cross-boundary freight transport facilities and port back-up land. In parallel, the Government has launched a series of measures to enhance the attractiveness and competitiveness of HKP.

40. With the development of mega container vessels, hub port operations are more important than ever before, as these vessels call at fewer ports and with lower frequencies. To enhance HKP's attractiveness as a hub port, to encourage the use of Hong Kong's freight transport services by other Asian countries, and to attract more ocean-going vessels (especially intra-Asia vessels carrying transshipment cargoes) to use our port, the Government amended the relevant legislation to reduce anchorage dues and port facilities and light dues early this year. With these measures in place since 1 February 2006 (the day the relevant legislation was gazetted), a medium-sized vessel calling Hong Kong for two days can save about 25% of anchorage dues and 5% of port facilities and light dues.

41. In view of the significant growth in the volume of river trade cargo in recent years and upon the industry's request, the Government has expanded the mid-stream cargo handling capacity by establishing new anchorages in the north of Lantau and in the western part of Victoria Harbour. The Government will continue to respond flexibly to market needs by providing more anchorages, so as to facilitate shipping companies' service scheduling and meet port operators' requests.

42. For the purpose of enhancing port productivity, the Government, after consulting the industry and gaining the support of the Hong Kong Port Development Council, provided the industry with back-up land adjacent to the Kwai Tsing Container Terminals in order to increase the cargo handling capacity and productivity of the terminals. The first batch of two barge handling facilities was put out for open tender in May 2006.

43. In addition, with a view to enhancing the efficiency of river trade operation and attracting more river trade vessels to call at HKP, the Government is making legislative amendments to introduce multiple entry permits for river trade vessels, such that the application procedures will be streamlined and permit fees lowered. With the enactment of the new legislation, a river trade vessel using a multiple-entry permit can save up to 50% of the entry permit cost. This measure will not only increase the river trade vessels' operational efficiency, but also lower their operating cost at HKP.

Maritime Services

44. With the success of its shipping and maritime industry, Hong Kong is one of the world's major maritime centres. Currently, about 900 renowned and experienced maritime service providers are operating in Hong Kong, providing a wide range of maritime services ranging from ship owning/management, registration, financing, insurance, brokerage, maritime arbitration, surveying, repairs to replenishment.

World's 5th Largest Shipping Register and the Global Trend of Maritime Services and Competition

45. Hong Kong is a world maritime centre. As at 1st January 2006, Hong Kong Shipping Register (HKSR) is the world's fifth largest shipping register, with a gross tonnage of 29.83 million GT and 1070 registered

ships. As shown in Annex 9, Hong Kong is still far behind the world's top shipping register in Panama. Nevertheless, the maritime industry widely regards the top four shipping registers as "flags of convenience", which have different standards in shipping services and control, and are not comparable with shipping registers with proper control. Instead the industry widely recognizes that Hong Kong should enhance the quality, standard and reputation of its shipping register in order to attract high quality vessels. Hong Kong Shipping Register also brings business opportunities to other maritime services. However, for historical reasons, many international maritime service providers are based in those maritime centres with long history, such as London and New York. Meanwhile, some places offer various favourable treatments, such as reduction in tax and registration fees, in order to get a share in the market of maritime services. Therefore, we have to examine how we can raise the standard and reputation of Hong Kong in the provision of international and regional maritime services to achieve a breakthrough.

Opportunities

46. With its growth in trade, Mainland's demand for sea transport will increase and its shipbuilding industry will expand rapidly, progressing towards the league of the world's largest shipbuilding countries. The number of ships built in Mainland China continues to rise. In 2005, new ships built in Mainland China reached 1200 million GT. Due to the proximity in geography, language and culture, the development of Mainland's sea transport will bring business opportunities to HKSR and our maritime services.

Response Actions

47. To further develop Hong Kong's maritime industry, the Hong Kong Maritime Industry Council (MIC) was established in 2003 to advise the Government on the formulation of maritime policies and initiatives. It also assists the Government in promoting Hong Kong's comprehensive maritime services and Hong Kong's position as an international maritime centre. Two task forces have been set up under the MIC to further enhance Hong Kong's attractiveness as a base for international maritime enterprises. The Human Resources Task Force addresses the education, training and manpower supply issues, while the Maritime Services Task Force focuses on formulating measures to promote the various sectors within the maritime cluster.

48. HKSR is reputable for its excellent services and is a world-class quality register. In 2004, its reputation as a quality flag was reaffirmed by the recognition under the “US QUALSHIP 21 Scheme”. To further enhance HKSR’s reputation and standards, the Marine Department continues to introduce improvement measures to attract top quality tonnage to register in Hong Kong. The HKSR crossed the 31 million gross tonnage mark in mid-July this year, with a registration of 1 100 vessels. It is now among the world’s top five shipping registers.

Manpower training

49. In the course of its expansion, Hong Kong’s maritime industry is faced with shortage of manpower. Both the shipping industry and the Government need to give some thoughts to the issue of manpower training, especially for senior management with sea-going experience, to meet the demand for such services as professional ship management and brokerage. To ensure an adequate supply of local talents with sea-going experience for the shipping and maritime industry, the Government launched the “Sea-going Training Incentive Scheme” in July 2004 to provide financial incentives for qualified youngsters to take up sea-going training as cadets. The training paves the way for them to become shore-based professionals and ensures quality human resources for the industry.

50. To attract more quality ships to register in Hong Kong on a long-term basis, thereby maintaining a stable number Hong Kong registered ships and further developing HKSR as a quality shipping register in the world, the Government introduced an Annual Tonnage Fee reduction scheme in early 2006. Under the scheme, ships that have continuously registered with the HKSR for two years without any record of detention during that period will be entitled to a six-month fee reduction. This arrangement will not only attract more ships to register in Hong Kong and enhance the quality of HKSR, it will also encourage shipowners to further improve the safety and quality of their ships.

51. In choosing a shipping register, apart from the flag’s international reputation and service quality, tax concession is also a major consideration of shipowners. Singapore is ahead of Hong Kong in offering tax concession. Hence, to boost the competitiveness of its maritime industry, Hong Kong has been actively negotiating with its trading partners over the avoidance of double taxation arrangements for shipping income. So far, Hong Kong

has made double taxation relief arrangements for shipping income with 13 tax administrations, namely Belgium, Germany, the Netherlands, Norway, Singapore, the UK, the USA, Sri Lanka, Denmark, New Zealand, the Republic of Korea, Thailand and the Mainland China.

Recommendations

52. The 11th Five-Year Plan expressly supports Hong Kong in our development of the logistics industry and as a maritime centre. With the firm support from the Central Government and the robust economic development in Mainland China, the industry is making continuous improvement on the basis of existing foundation and strengths of Hong Kong. Members are invited to comment on the following proposals and to offer other worthy recommendations.

Coordinated Development

53. The layout of the national comprehensive transportation system has made clear that under the premise of maintaining Hong Kong's status as an international maritime centre, initiatives should be taken to realize fully the strengths of the container transport system rendered by HKP and other coastal ports in the PRD region. The idea is to have Shenzhen, Guangzhou and Xiamen as main ports, Fuzhou, Quanzhou, Shantou, Humen, Zhuhai, Zhanjiang, Fangchenggang, and Haikougang as second-tier ports and others as feeder ports. Shenzhen, as a main container port in South China, and Hong Kong will complement each other to achieve mutual development. Under the above premise, Hong Kong and Guangdong should map out a clear division of role in port development. The positioning and scale of development for different ports should be considered in the context of the overall development of the region. Linkages between the sea and land transport systems should be further enhanced to raise the efficiency of freight transport between the ports and the sources/destinations of cargoes. This can also avoid wastage of resources and unhealthy competition that hurts the national interest. Furthermore, it is recommended that Hong Kong should strengthen communication and coordination with different regions and cities in the Mainland on the preliminary planning and study of transportation infrastructure. It is necessary for Hong Kong to have more frequent, in-depth and comprehensive exchanges and cooperation with the Mainland to boost regional development through improvement on transportation facilities, so as to contribute to the development of the country.

Sharpening Competitive Edges

54. Under the “one country, two systems” principle, the HKSARG shall continue to adopt economic, social and political systems distinct from those in the Mainland after the reunification in July 1997. The Basic Law, as the constitutional law of the HKSARG, firmly protects this principle. The HKSARG shall continue to uphold the rule of law, maintain an effective executive-led Government, keep a clean and efficient civil service, promote free enterprise and free trade, maintain a stable public finance system and a sound financial system, practise prudent public finance, and adopt a simple and predictable tax system with low tax rates.

55. These systems are the cornerstones of stability and prosperity of Hong Kong, which create a favourable business environment that inspires confidence in foreign investor. They also ensure the well-being of Hong Kong people. Thus the Government should continue to make every effort to sustain such advantages and further enhance these systems. In particular, maritime, logistics, tourism, financial, and professional and producer services are the high value-added sectors which exhibit the best competitive edge in the Hong Kong economy. The Government should strive to reinforce Hong Kong's competitiveness as international financial and maritime centres and logistics hub through streamlining the procedures to attract more international corporations and business operators to expand their markets and to provide services in Hong Kong.

Avoidance of Double Taxation Agreements

56. As air transport and shipping are international business activities, incomes derived from such operations are more likely to be subject to double taxation. The Government will continue to negotiate agreements with its major trading partners for the avoidance of double taxation on shipping and air transport incomes, with a view to easing the overseas tax burden of local shipowners and airline operators and boosting their international competitiveness, as well as strengthening Hong Kong's position as international maritime and air transport centres. Currently, the Government is negotiating such agreements with India, Israel and the Philippines. Double taxation relief provisions have also been incorporated into some of the bilateral air services agreements. In response to the request of the industry, the Government has also taken the initiative to contact other trading partners including Indonesia, Malaysia

and Poland, inviting them to negotiate such agreements.

Promotional Activities

57. Being an international maritime centre, Hong Kong has a world-class maritime cluster which readily provides support and ancillary services for Mainland China's fast-developing shipbuilding and maritime industries. Due to the rapid rise of its shipbuilding industry, the Mainland's shipbuilding tonnage has ranked third in the world for 11 successive years. To further promote the quality services of Hong Kong's maritime industry to Mainland shipowners, MIC has organized a series of promotional activities and seminars in Hong Kong, Xiamen and Shanghai. In the coming year, the Government will join the MIC, the Hong Kong Trade Development Council and the China Classification Society to visit major port cities in the Mainland to promote the related services, and attract Mainland shipowners to register their ships in Hong Kong, make use of the services provided by our maritime cluster, and set up branch offices here. The visits will also provide an effective platform for the industry to explore business opportunities and form business ventures.

Shipping Register

58. The Marine Department reviews the shipping register service from time to time, with a view to further enhancing the HKSR. The purposes are to raise the service quality, expand the service scope, and meet the demands of shipowners and other clients. Moreover, to strengthen Hong Kong's position as an international maritime centre, the Government will host maritime seminars in collaboration with international organizations, such as the Baltic and International Maritime Council, to equip local and Mainland maritime professionals with knowledge of international maritime requirements and the latest developments.

Maritime Training

59. To reinforce Hong Kong's position as a maritime centre, it is extremely important to attract international maritime service providers to establish their regional headquarters in Hong Kong. Apart from capitalizing on the strengths of our systems, the Government is also keen on training local talents and upgrading the knowledge and technical skills of our professionals, such that the manpower resources can meet the market demand. In this connection, the Government will set up a maritime

studies scholarship shortly to train local talents, as well as to attract Mainland talents to study post-graduate maritime courses in Hong Kong and stay behind to work. The initiative will not only raise the standard of home-grown maritime professionals, but will also provide quality human resources to multinational corporations to set up offices in Hong Kong. Taking a broader perspective, the initiatives can strengthen Hong Kong's position as a maritime centre, which will provide further impetus to our thriving economy and hence more job opportunities for the local workforce.

Air Services

60. The HKSARG will continue to work towards further expansion of air services arrangements between Hong Kong and the Mainland, to allow more airlines from both sides to enter the market and provide them with increased business opportunities, with a view to strengthening Hong Kong's connections with provinces and cities in the Mainland and hence Hong Kong's position as a major gateway of air freight transport to the Mainland. In parallel, our international connectivity will be strengthened to enhance the role of the HKIA as a major aviation hub in the region.

61. In addition, the Civil Aviation Department continues to regularly review the air traffic management control system, and strengthen coordination among the civil aviation authorities of Hong Kong, the Mainland and Macau, with a view to facilitating the opening up of more civil airspace to support the long-term development of the local civil aviation industry.

Efficiency of Cross-boundary Trucking Operation

62. The validity period of the licences for operating cross-boundary trucking business has been extended from three to six years, which helps reduce the administrative cost in licence renewal. In response to the industry's request for the Mainland to consider lowering the licence fee paid by Hong Kong/Guangdong joint-venture cross-boundary trucking companies, the HKSARG will continue to liaise with the relevant authorities.

Enhancement of the Overall Infrastructure Planning

63. Looking ahead, to ensure that the industry can keep abreast of the

international logistics development trends and to further enhance the competitiveness of Hong Kong's logistics industry, the Government will make available more back-up land for the logistics industry. This will provide them with a suitable operating environment and facilitate the integration of various logistics services.

64. The Government is planning to introduce a pilot scheme to dispose of sites which are suitable for logistics use on a long-term basis through public tender. Meanwhile, the Government will review statutory land use plans from time to time to assist the development of logistics centres and related facilities.

Development of E-logistics

65. The Government will work together with the industry to further develop e-logistics and promote information connectivity, including monitoring the implementation of DTTN services and carrying out the pilot project of OBTIS.

66. To cultivate manpower resources for meeting the needs of modern logistics development, the Government will continue to collaborate with training institutions in the provision of training programmes. The training aims to equip employees in the logistics sector with the necessary skills and techniques in e-logistics applications, especially for those working in the small and medium-sized enterprises.

Advice Sought

- (i) Is this paper comprehensive and thorough in its analysis of the international competitiveness of our logistics, port, and maritime industries? Is supplement necessary?
- (ii) Is this paper comprehensive and thorough in its analysis of the opportunities and challenges brought by the 11th Five-Year Plan to our logistics, port and maritime industries? Is supplement necessary?
- (iii) Is this paper comprehensive and thorough in its analysis of the opportunities and challenges of our logistics, port and maritime industries in the context of Guangdong's 11th Five-Year Plan and regional development? Is supplement necessary?

- (iv) Are the response actions of the government and public sector to consolidate and develop our logistics, port and maritime industries relevant? Which strategic directions require adjustment?
- (v) Are the recommended topics for further studies and exploration aiming to consolidate and develop our logistics, port and maritime industries appropriate?

Economic Development Branch
Economic Development and Labour Bureau
September 2006

Value Added of the Four Key Industries

Four Key Industries	Value Added at current prices in 2004 (HK\$Mn)
1. Financial services	152,900 (12.2%)
a. Banking	100,500
b. Insurance and other financial services	52,400
2. Tourism (inbound & outbound)	36,900 (2.9%)
a. Inbound tourism	27,400
b. Outbound tourism	9,600
3. Trading and logistics	346,900 (27.7%)
a. Trading	279,700
b. Logistics	67,200
4. Professional services and other producer services	132,400 (10.6%)
a. Professional services	46,800
b. Other producer services*	85,700
Four Key Industries = 1+2+3+4	669,100 (53.3%)
GDP at factor cost #	1,254,500

Notes: Figures in brackets are the percentage contributions of the respective industries to GDP.

* Other producer services refer to producer services other than financial services, trading and logistics, tourism and professional services.

To facilitate comparison of the contribution of the four key industries to GDP, GDP at factor cost is used. This is slightly different from the GDP figures commonly used, which is compiled on market price basis.

Source: Census and Statistics Department

Annex 2

Value Added and Employment in Logistics

	1999	2000	2001	2002	2003	2004	AAGR*
Logistics							
Value added (HK\$billion)	50.5	56.0	53.4	54.8	58.5	67.2	+5.9%
Employment ('000 persons)	187.0	195.8	195.6	186.8	188.9	198.4	+1.2%
VA per person (HK\$'000)	270.1	286.0	273.0	293.4	309.7	338.7	+4.6%
- Land freight transport							
Value added (HK\$billion)	6.1	6.5	5.8	5.6	5.7	6.3	+0.6%
Employment ('000 persons)	66.2	70.0	67.9	60.4	62.5	67.1	+0.3%
VA per person (HK\$'000)	92.1	92.9	85.4	92.7	91.2	93.9	+0.4%
- Water freight transport							
Value added (HK\$billion)	22.8	25.4	25.0	24.9	28.1	31.0	+6.3%
Employment ('000 persons)	73.9	74.5	77.6	75.2	75.9	79.2	+1.4%
VA per person (HK\$'000)	308.5	340.9	322.2	331.1	370.2	391.4	+4.9%
- Air freight transport							
Value added (HK\$billion)	14.5	16.9	16.4	18.2	18.4	22.7	+9.4%
Employment ('000 persons)	22.9	26.0	25.1	26.2	25.9	26.1	+2.7%
VA per person (HK\$'000)	633.2	650.0	653.4	694.7	710.4	869.7	+6.6%
- Ancillary services (e.g. cargo inspection)							
Value added (HK\$billion)	0.3	0.4	0.3	0.4	0.5	0.6	+14.9%
Employment ('000 persons)	1.8	1.4	1.2	0.9	1.0	1.0	-11.1%
VA per person (HK\$'000)	166.7	285.7	250.0	444.4	500.0	600.0	+29.2%
- Storage							
Value added (HK\$billion)	1.2	1.3	1.1	1.0	1.0	1.1	-1.7%
Employment ('000 persons)	4.7	5.0	5.3	5.1	5.1	5.2	+2.0%
VA per person (HK\$'000)	255.3	260.0	207.5	196.1	196.1	211.5	-3.7%
- Postal and courier services							
Value added (HK\$billion)	5.5	5.4	4.8	4.7	4.7	5.4	-0.4%
Employment ('000 persons)	17.5	18.9	18.5	18.9	18.5	19.8	+2.5%
VA per person (HK\$'000)	314.3	285.7	259.5	248.7	254.1	272.7	-2.8%
Percentage share to GDP	4.2	4.5	4.3	4.4	4.9	5.4	--
Percentage share to total employment	6.0	6.1	6.0	5.8	5.9	6.0	--

Note: * AAGR : Average annual growth rates in 1999-2004

Source: Census and Statistics Department

Annex 3

Value Added to Persons Engaged in Logistics

HK\$ '000

Logistics sub-sector	1999	2000	2001	2002	2003	2004	AAGR*
Shipowners or operators of sea-going vessels	661	907	663	488	1,456	2,605	+31.6%
Shipbrokers	498	625	617	657	807	1,128	+17.8%
Ancillary services to air transport	718	801	814	884	836	993	+6.7%
Airlines companies**	861	890	743	990	825	949	+2.0%
Ancillary services to water transport	649	665	624	613	608	672	+0.7%
Cargo inspection, sampling and weighing services	350	372	342	473	605	642	+12.9%
Inland water freight transport	376	336	416	453	429	511	+6.3%
Sea cargo forwarding services	380	430	394	420	458	447	+3.3%
Ship agents and managers	329	374	336	337	373	426	+5.3%
Air cargo forwarding services	356	411	417	407	385	415	+3.1%
Packing and crating services	166	180	192	213	188	261	+9.4%
Storage	257	261	229	212	244	253	-0.3%
Miscellaneous communications services (e.g. courier services)	250	280	232	230	242	250	0.0%
Land freight transport	200	199	179	186	175	196	-0.4%

Notes: * AAGR: Average annual growth rates in 1999-2004

** Include passenger transport

Sources: Annual economic surveys on various sectors conducted by Census and Statistics Department

Ratio of Value Added to Business Receipts in Logistics

Logistics sub-sector	1999	2000	2001	2002	2003	2004	AAGR*
Logistics	0.31	0.30	0.29	0.28	0.27	0.25	-3.9%
- Land freight transport	0.46	0.49	0.48	0.48	0.47	0.46	-0.0%
- Water freight transport	0.30	0.28	0.28	0.26	0.27	0.24	-4.6%
Shipbrokers	0.52	0.54	0.45	0.63	0.58	0.73	+7.1%
Ship agents and managers	0.67	0.68	0.64	0.62	0.67	0.69	+0.7%
Inland water freight transport	0.38	0.30	0.44	0.42	0.46	0.51	+6.0%
Shipowners or operators of sea-going vessels	0.08	0.09	0.07	0.05	0.13	0.13	+9.6%
Sea cargo forwarding services	0.16	0.16	0.16	0.17	0.15	0.12	-5.5%
Ancillary services to water transport including container terminals, stevedoring, haulage of containers	0.56	0.54	0.57	0.56	0.55	0.55	-0.2%
- Air freight transport	0.28	0.27	0.27	0.28	0.25	0.24	-2.8%
Airlines companies**	0.37	0.33	0.33	0.36	0.30	0.30	-4.4%
Air cargo forwarding services	0.10	0.10	0.11	0.10	0.11	0.10	-0.3%
Ancillary services to air transport including airport and air cargo terminals	0.63	0.68	0.69	0.70	0.68	0.73	+3.2%
- Ancillary services (e.g. cargo inspection)	0.54	0.55	0.46	0.58	0.61	0.63	+3.2%
Cargo inspection, sampling and weighing services	0.56	0.56	0.45	0.59	0.67	0.69	+4.1%
Packing and crating services	0.40	0.48	0.61	0.54	0.39	0.45	+2.7%
- Storage	0.31	0.31	0.32	0.36	0.41	0.38	+4.5%
- Postal and courier services	0.49	0.42	0.37	0.28	0.25	0.26	-11.7%
Miscellaneous communications services (e.g. courier services)							

Notes: * AAGR: Average annual growth rates in 1999-2004

** Include passenger transport

Sources: Annual economic surveys on various sectors conducted by Census and Statistics Department

**Number of Establishments and Number of Persons Engaged
in Logistics in 2004**

Logistics sub-sector	Number of establishments	Number of persons engaged
Shipowners or operators of sea-going vessels	76	2 121
Shipbrokers	33	187
Ancillary services to air transport	24	9 519
Airlines companies*	67	19 769
Ancillary services to water transport	3 578	19 612
Cargo inspection, sampling and weighing services	32	513
Inland water freight transport	471	3 076
Sea cargo forwarding services	2 012	15 087
Ship agents and managers	245	7 135
Air cargo forwarding services	701	15 407
Packing and crating services	24	309
Storage	275	4 189
Miscellaneous communications services (e.g. courier services)	606	12 819
Land freight transport	9 078	31 172

Notes: The sum of the number of persons engaged **does not** equal the employment of the whole logistics sector. It is because the employment of whole logistics sector is based on a number of survey estimates, which can better reflect a comprehensive and accurate picture.

* Include passenger transport

Sources: Annual economic surveys on various sectors conducted by Census and Statistics Department

Hong Kong Air Cargo Throughput

‘000 Tonnes

Air Cargo throughput	
1996	1 563
1997	1 786
1998	1 629
1999	1 974
2000	2 241
2001	2 074
2002	2 479
2003	2 642
2004	3 090
2005	3 402
Average annual growth rates in 1996-2005	9.0%

World Top 10 Container Ports

	‘000 TEUs ⁽¹⁾	
	2004	2005
Singapore	21 329 (+15.9%)	23 192 (+8.7%)
Hong Kong	21 984 (+7.5%)	22 602 (+2.8%)
Shanghai	14 554 (+29.0%)	18 084 (+24.3%)
Shenzhen	13 659 (+28.2%)	16 197 (+18.6%)
Busan	11 492 (+10.4%)	12 521 (+9.0%)
Kaohsiung	9 714 (+9.8%)	9 471 (-2.5%)
Rotterdam	8 292 (+15.9%)	9 287 (+12.1%)
Hamburg	7 003 (+14.1%)	8 088 (+15.5%)
Dubai	6 429 (+24.8%)	7 596 (+18.5%)
Los Angeles	7 321 (+2.0%)	7 485 (+2.2%)

Notes: () Year-on-year rate of change.

⁽¹⁾ TEU refers to Twenty-Foot Equivalent Unit.

South China Container Cargo Base Analysis

	2001	2002	2003	2004	million TEUs 2005
South China Container Cargo Base (including Hong Kong)	13.81 (+1.4%)	16.07 (+16.3%)	19.13 (+19.0%)	21.44 (+12.1%)	23.72 (+10.7%)
- handled by Hong Kong port	10.51 (-4.4%)	11.07 (+5.4%)	11.37 (+2.6%)	11.86 (+4.3%)	11.32 (-4.6%)
- handled by South China ports	3.31 (+25.5%)	4.99 (+51.1%)	7.76 (+55.4%)	9.58 (+23.4%)	12.40 (+29.5%)
% share of South China Container Cargo Base					
Hong Kong port's share	76.1%	68.9%	59.4%	55.3%	47.7%
South China ports' share	23.9%	31.1%	40.6%	44.7%	52.3%

Notes: () Year-on-year rate of change.

World Top 10 Shipping Registers⁽¹⁾ as at 1 Jan 2006

	'000 Gross tonnage	Number of vessels
Panama	139 458	5 790
Liberia	58 017	1 545
Bahamas	36 460	1 204
Greece	30 788	1 269
Hong Kong	29 825	1 070
Singapore	29 153	1 185
Marshall Islands	28 581	722
Malta	22 724	1 172
China	21 046	2 515
Cyprus	18 791	895

Notes: ⁽¹⁾ Based on statistics released by Danish Shipowners' Association, which includes only merchant ships of 100 GT and above, where the figures for HK are slightly different from those recorded in the HK Shipping Register.