WORLD VIEW

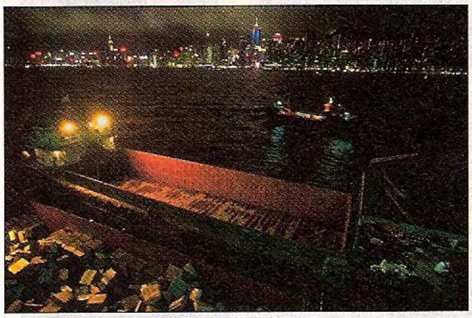
HOW TO FIX HONG KONG

The city must allow property values to fall, and encourage intellectual capital to rise

BY SIN-MING SHAW

HONG KONG HAS FALLEN. IF it wishes to aspire to its former glory, it must purge its fixation on real estate, just like an addict trying to kick an opium habit. And Hong Kong must embark on a long-term commitment to rebuilding its depleted intellectual capital; if it does not do so, it has no future.

The economic downfall of Hong Kong is a sad but predictable tale. Because the peak of Hong Kong's bubble coincided with the Inauguration of Tung Chee-hwa as chief executive of the Special Administrative Region, many blame Tung for the city's current woes. That is unfair; the roots of today's problems go much deeper. Broader community needs were rarely considered. Because land sales were restricted, a world-class bubble was created, helped by years of negative real rates of interest. The disastrous misallocation of capital, financial and human, has eroded a Hong Kong which was once a vibrant, diversified manufacturing and trading city, and a tourist's paradise. Artistic and literary talents flourished; small entrepreneurial firms prospered.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Nightfall? *The formerly Fragrant Harbour*

Now more than 50 percent of GDP and the stock market is property related. At its peak last year the market value of HK property companies was more than 40 percent of all listed property companies in the world. (For comparison: Hong Kong accounts for less than 1 percent of world output.) The place had gone mad.

The lure of easy money pulled the best talents into a marginally productive activity. Many more went into supporting businesses, like stockbroking and banking, that live off the property sector.

If Hong Kong is to reinvent itself, it must not allow asset inflation to distort its values. The bubble, 15 years in the making, has destroyed incentives for young people to pursue a more creative and productive line of work. If Hong Kong is to be true to its market principles, it must allow property prices, and wages, to fall to wherever they must. Once these prices have adjusted, Hong Kong may become a more sensible place with a brighter future.

This won't be easy; for Hong Kong has a glaring absence of intellectual capital. The British failed to build a first-rate educational system, and the current administration made things worse by insisting that Cantonese become the language of instruction in hundreds of high schools that had been bilingual. Cantonese is widely understood only in the southern province of Guangdong; this thoughtless policy will isolate future generations of local youngsters from the mainstream of Chinese intellectual advancement. In 20 years' time, the young of today will have problems understanding a lecture by a Nobel laureate from Beijing.

Hong Kong's higher education, too, is a disaster. University educators openly lament low reading and writing levels in both English and Chinese. Employers complain about the poor quality of fresh graduates. Hong Kong has not a single university that is world-class—no equivalent of Stanford or MIT—even though there is sufficient wealth to endow scores of such institutions. The city desperately needs privately funded universities that would offer competition to public institutions for both students and professors. But with such high property prices, establishing such an institution is prohibitively expensive.

The irony here is that Hong Kong once depended on intellectual capital for its success. In the postwar years, Hong Kong benefited from the influx of Shanghainese industrialists who brought textile technology to the colony. Other penniless refugees came with a wealth of knowledge ranging from shipping (Tung's late father was a legend) to sophisticated construction techniques. Wages and property prices were not a business consideration. Entrepreneurs and industrialists concentrated on creating value, thus building a strong export economy of manufactured goods and services.

The city now is too expensive for start-up entrepreneurs without a deep pocket. Tourism has shrunk. The grossly overvalued Hong Kong dollar and high real-estate prices have driven away visitors and snuffed out local leisure business initiatives. Pollution levels are often unacceptably high; the Fragrant Harbour is a giant sewage plant.

Hong Kong's real-estate prices must fall an additional 50 percent before small businesses can start up and prosper. So the government should stop supporting the property market. And Hong Kong must thoroughly reform its education system. Education is too important to be left in the hands of bureaucrats, especially when their own academic qualifications are in doubt. More schools and universities should be privatized. Children should be free to select their own public schools, so that mediocre public schools will be punished by declining enrollment.

Tung must reach out beyond the self-perpetuating civil service to bring in talents to better manage the existing bureaucracies, some of which desperately need a cleanup. Most important, Hong Kong must admit to structural flaws due to bad government policies. Its leaders need a clear vision of where the city should be headed, and the will to implement their strategy firmly and boldly.

Without intellectual honesty and a credible strategy, it will be difficult for Hong Kong to reinvent itself. Hong Kong was a creative and vibrant place before the years of the overvalued dollar and property addiction. The Pearl of the Orient now risks becoming an economic and intellectual wasteland.

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