

Box 2.1

The structural shift of Hong Kong's external trade towards offshore trade

Reflecting the prominent role of Hong Kong as a business and service hub in the region, offshore trade in Hong Kong has been growing remarkably over the past decade and has become an increasingly important growth driver of the Hong Kong economy.

Offshore trade covers the services of both merchanting and merchandising for offshore transactions provided by Hong Kong companies. In merchanting, goods are purchased by the Hong Kong companies from and then sold to parties outside Hong Kong without the goods ever entering and leaving Hong Kong. The Hong Kong company takes ownership of the goods involved. In merchandising for offshore transactions, the Hong Kong company provides services of arranging on behalf of buyers/sellers outside Hong Kong the purchases/sales of goods. The goods involved are sold by a party outside Hong Kong to another party outside Hong Kong without the goods ever entering and leaving Hong Kong. Unlike merchanting, the Hong Kong company, in its capacity as an agent or broker, does not take ownership of the goods involved. Earnings from offshore trade include the gross margin from merchanting and commission from merchandising for offshore transactions.

During 1996-2004, the growth in exports of merchanting and trade-related services (in which offshore trade constituted the bulk, of almost 90% in 2003), at 15.3% in real terms per annum, outpaced notably the growth in re-exports, at 8.1% in real terms per annum. This contrasted to their respective growth of 4.3% per annum and 23.8% per annum during 1986-95. Furthermore, it is noted that the total sales value of goods involved in offshore trade has exceeded the value of re-exports since 2002 when estimation on statistics of the former are first available.

Structural shift in Hong Kong's external trade (change in real terms)

	<u>Re-exports</u> (%)	<u>Exports of trade-related services</u> (comprising mainly offshore trade) (%)
Average annual growth rate :		
1986-95 (10 years)	23.8	4.3
1996-04 (9 years)	8.1	15.3

Value of goods involved in re-export trade and offshore trade

	<u>Re-export of goods</u> (HK\$ billion)	<u>Offshore trade</u> (HK\$ billion)
2002	1,430	1,458
2003	1,621	1,667

Box 2.1 (cont'd)

Analysed by destination for goods sold under merchanting arrangement, the Mainland was the largest destination, accounting for 37% of the total value of goods sold under such arrangements in 2003, as against 44% for re-exports. The United States came next, with a share of 18% (as against 18% for re-exports). This was followed by Japan, at 8% (6%), Taiwan, at 4% (2%), and the Republic of Korea, at 4% (2%). Regarding the source of Hong Kong's offshore trade, the Mainland took up the major share, at 51% of the total sale value in 2003. This was similar to that for re-exports, with the Mainland taking up 60% of the value of re-exports in 2003.

It can thus be seen that offshore trade resembles closely that of re-export trade in terms of both destinations and sources. Hence it will be useful to look at the gross margin of re-exports and offshore trade taken together. While the growth in gross margin from offshore trade in value terms, at 12.6% per annum, outpaced the growth in gross margin from re-exports in value terms, at 6.8% per annum over the past ten years in tandem with the structural shift towards offshore trade, the combined gross margin of re-exports and offshore trade still recorded very significant growth of 8.2% per annum in value terms over the past ten years.

However, it should be noted that owing to the different level of involvement of the Hong Kong companies in offshore trade and in re-exports, the trade margin of merchanting (8.5% in 2003) was only about half of the rate of re-export margin (17.9% in 2003). The commission rate of merchandising for offshore transactions was even smaller (3.4% in 2003). It implies that Hong Kong would have to channel larger volumes of offshore trade in order to maintain the same value added to the economy as in re-export trade.