



The British
Chamber of Commerce
in Hong Kong
香港英商會

Mr Frank Chan Fan, JP
Secretary for Transport and Housing
20/F - 22/F, East Wing, Central Government Offices,
2 Tim Mei Avenue, Tamar, Hong Kong

3 August, 2017

Dear Mr Chan,

British Chamber of Commerce Position Paper: Hong Kong as an E-Commerce Fulfilment Hub

The Chairman of the British Chamber has already written to congratulate you on your appointment to this vitally important role. But I would like to take this opportunity to add my own congratulations, and to express the thought that we look forward to a strong working relationship with you and your team in the months and years to come. Chamber members include many companies with experience and expertise in sectors relevant to the responsibilities of your Bureau and we would be happy to offer any support we can to your work

I have the pleasure to enclose a position paper prepared by the Chamber's Logistics Committee on the potential for Hong Kong to develop a major strategic role as an E-Commerce Fulfilment Hub. The paper contains a number of proposals regarding policy and legislative actions to support this development, which we see as presenting a major economic and business opportunity for Hong Kong.

We would welcome the opportunity to discuss these proposals further with you and your colleagues. More widely, given the scope and importance of your responsibilities, we would also welcome a broader discussion to learn more about your priorities and to explore some of the policy priorities of the Chamber. A closed-door discussion of this nature with your predecessor was I think highly mutually useful.

Your sincerely,

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Executive Director

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British Chamber of Commerce Position Paper: Hong Kong as an E-Commerce Fulfilment Hub

British Chamber Logistics Committee - Industry Position Paper 2017

Executive Summary

The explosive growth of e-commerce around the world has emerged over the last few years as a major new driver in economic development. Increasingly connected consumers in the developed world - and more importantly, across the developing world - are turning to online shopping for their purchases.

Asia Pacific (APAC) is already the world's biggest and fastest growing Business-to-Consumer (B2C) e-commerce region, representing some 35% of global B2C e-commerce sales and growing at some 29% per annum.

This development presents a major strategic opportunity for Hong Kong. By leveraging our strategic location, free port status and well developed logistics sector, Hong Kong is ideally positioned to capitalise on this growth opportunity. In order to do so, we believe the following initiatives are essential for success and request HKSAR Government's consideration of the following recommendations:

- 1. Ensure timely completion of Airport 3RS expansion**
- 2. Successful completion of the Hong Kong-Zhuhai-Macau Bridge**
- 3. Accelerate deployment of allocated land in Tuen Mun West**
- 4. Expedite the conclusion of the HK-ASEAN Free Trade Agreement**
- 5. Review and refine the Transshipment Ordinance and Trade Declaration Charge**
- 6. Enable and encourage inbound investment for e-commerce companies to establish regional operations in Hong Kong**

With the expertise amongst our members here, and the capabilities of many British businesses who are leaders in the e-commerce arena, the Chamber would like to offer our support to the new administration - and would welcome an opportunity to meet with the Secretary to explore how we can work together to bring about these initiatives.

Detailed Report

1. Introduction

In recent years, Hong Kong's traditional role as the super-connector between Mainland China and the rest of the world has come under threat, as China has opened up and enabled more goods to flow directly in and out of the Mainland, bypassing Hong Kong. The development of the container ports in South China demonstrates this shift, with Shenzhen recently overtaking Hong Kong in terms of container throughput volume.

However, as presented by then Acting Chief Executive, Mrs Carrie Lam at the Asian Logistics and Maritime Conference (ALMC) on 22 November 2016:

"Trading and Logistics together make up the largest sector of the Hong Kong economy. Last year, trading and logistics contributed 23 per cent of our overall Gross Domestic Product and 20 per cent of our employment."

Hong Kong's enduring strengths such as its unique geographical position at the heart of Asia and on the doorstep to China's Guangdong manufacturing region, as well as the highly developed logistics sector that includes the world's largest air cargo hub and fifth largest container port, all combine to provide an excellent opportunity to capitalise on the massive growth in e-commerce - and position Hong Kong as the pre-eminent e-commerce fulfilment hub to serve China, Asia and the world.

Asia's dual role as both a manufacturing powerhouse and home to the world's largest online consumer markets is a unique opportunity for Hong Kong. To take advantage of this, Hong Kong needs to continue to develop its logistics sector and e-commerce infrastructure and actively lure talent and companies to its shores.

2. Global E-Commerce Opportunity

The past two decades have seen major advancements in the commercial use of the internet, which in turn has contributed to the rapid growth of e-commerce. Technological advancements around internet speeds, connectivity and the ubiquitous smartphone have helped to propel online shopping to the forefront of the global consumer economy.

In 2016, worldwide online retail sales reached USD 1.9 trillion - according to eMarketer - and are projected to grow to over USD 4 trillion by 2020.

Consumer electronics, appliances and apparel account for 44% of all online retail sales. In the Fast-Moving Consumer Goods (FMCG) sector, e-commerce is now contributing 35 percent of global growth, according to the June 2017 E-commerce Index from Kantar Worldpanel, which reported that last year, worldwide online sales of FMCG products increased by 26 percent, versus 15% growth in 2015.

In the UK, consumers spend 4.5 times more online on Fast-Moving Consumer Goods than they do in-store, becoming the best-performing country in Europe with 27.5% of UK households purchasing FMCG online, whereas in France the share is 26.2 percent, followed by Spain (24.7 percent) and Portugal (just 6.5 percent). The report also shows that in the UK, online FMCG purchases account for 7.3 percent of total FMCG purchases, whereas in other European countries, this share is much lower: 5.5 percent in France, 1.7 percent in Spain and 1 percent in Portugal.

The UK has the highest share of online retailing in the world, with 76% of the population shopping online. Indeed, more and more British companies are engaging in digital opportunities to accelerate their global export potential. By 2018, the value of UK e-commerce is estimated to be £60 billion, from just £10 billion in 2013.

In the global e-commerce market, Asia Pacific is already the largest region, with China itself projected to reach one trillion USD of online sales this year. According to the China National Bureau of Statistics, in 2016 the Chinese e-commerce market increased by 26.2%, representing 15.5% of total retail sales in China. During the first four months of 2017, online retail sales of goods and services in China reached USD 279 billion, increasing 32% year on year and accounting for 17% of total retail sales.

This massive growth across Asia, thus far primarily powered by China, is a result of quite distinctive Asian consumer behaviour patterns. In the absence of widespread modern retail, sophisticated distribution infrastructure, supply chain networks or offline stores, digital consumers in emerging and developing markets have rapidly taken to online shopping, very often directly from their smart phones; such that the penetration of mobile e-commerce in Asia is much higher than in the developed world. During last November's "Singles' Day" - China's biggest online shopping event – of the USD 17.8 billion of online sales generated in just 24 hours, 82% of all orders were placed from mobile devices.

All predictions are that e-commerce will continue its rapid growth throughout Asia, fuelled by improving logistics networks and transport infrastructure, increasing competition amongst e-commerce players, together with the expanding middle classes, and greater penetration of mobile devices and prevalence of high speed internet access.

3. Cross Border E-Commerce

The rise of digital commerce has enabled online consumers and e-commerce businesses to reach across borders to access new products and markets, leading to a substantial increase in cross-border e-commerce trade – both in terms of transactions and in the flow of goods.

With its huge base of digital consumers, China has been at the forefront of this trend. Cross-border e-commerce sales in China will grow 29% in 2017 to exceed USD 110 billion, according to estimates from eMarketer, with double digit growth rates continuing and sales reaching USD 157 billion by 2020.

4. Regulatory developments in China

As the Chinese e-commerce market has developed, the mainland government has adapted the regulatory framework, seeking to improve standards and control the taxation of goods moving in and out of the country. Across China, multiple pilot zones have been established for the facilitation and standardisation of procedures for cross-border e-commerce transactions, including payments, logistics and customer clearance - as well as tax collection, refund and exchange settlements.

In April 2016 the Cross-Border E-Commerce Retail and Import Taxation Policy was jointly issued by the Ministry of Finance, General Administration of Customs and State Administration of Taxation – to synchronise tax rates for e-commerce transactions and ensure adherence to tax policies.

The Integrated Cross-Border E-Commerce Tax changed the customs declaration framework to replace the existing postal tax, which at the same time was adjusted to three tiers. The new regulations limit product imports to those on a specific list, whilst imposing maximum daily and yearly online orders per consumer, plus a new requirement for a Chinese ID card for cross border e-commerce purchases. The hasty implementation of this new policy resulted in much confusion for the e-commerce platforms and businesses. The authorities were quick to realise the negative impact on the market and subsequently allowed a one year grace period for most commodities.

These attempts by the Chinese authorities to control e-commerce and the related taxes demonstrate ongoing uncertainty about the regulatory framework for e-commerce in the mainland.

Amidst this uncertainty, Hong Kong provides a more stable, free and open market that can readily provide a safe, secure and reliable fulfilment hub for e-commerce throughout Asia.

5. Cross-border e-commerce infrastructure will be a critical growth enabler for Hong Kong to serve the region

Amongst the opportunities, there are also some challenges. Hong Kong's strategic advantage could be somewhat diluted by regional Free Trade Agreements and the Cross-Border E-Commerce Comprehensive Pilot Zones established across mainland China.

However, while land constraints, limited labour supply and talent shortages are a continual challenge for the local logistics industry, Hong Kong's role as a leading financial, technology and international trading hub means the city is ideally positioned to serve the rapidly developing e-commerce consumer markets.

Hong Kong should forge a new role as the leading regional e-commerce fulfilment hub, becoming a financial centre for e-commerce business transactions and providing the ideal environment for companies to set up their e-commerce businesses, for both trading and logistics.

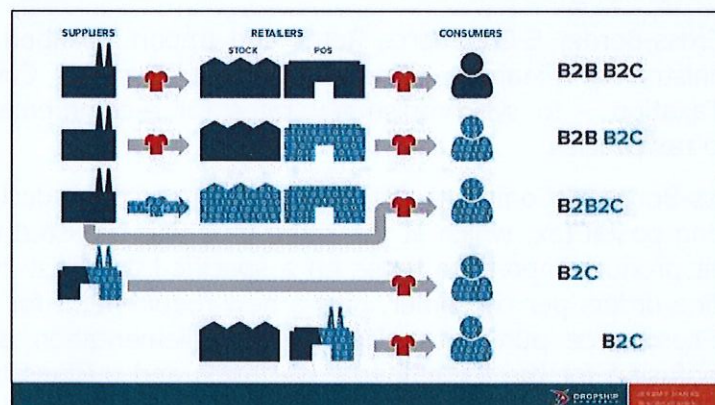
6. E-commerce Distribution Models

New e-commerce distribution models are emerging, as the industry develops and seeks more efficient ways to deliver goods to consumers across Asia.

In the initial model - known as Business to Consumer (B2C) - online retailers and marketplaces sell directly to consumers with delivery via international logistics and bonded warehouses,

More recently, many online businesses are moving to a more sophisticated Business-to-Business-to-Consumer model (B2B2C) which involves international warehousing in a third country, then subsequently shipping directly to the customer, thus shortening lead times.

This B2B2C model suits Hong Kong perfectly! Bulk shipments can easily be imported through Hong Kong's well established air cargo and ocean freight facilities; from where, local logistics service providers can serve as staging hubs, pending the final B2C movement.



Leading Chinese e-commerce platforms JD.com and VIP.com have already established warehouse operations in Hong Kong to handle their cross-border B2B2C and B2C e-

commerce, thereby overcoming policy uncertainties in mainland China, whilst leveraging Hong Kong's reliable business environment.

In the China cross border e-commerce business, online orders placed by mainland consumers are mostly sent from overseas by international air freight into gateways such as Shanghai, Beijing or Shenzhen, from where the orders are transported by domestic trucking for delivery to the consumers in the local cities where they live.

However, challenges with cross-border e-commerce trade include complex regulations and customs procedures, with companies identifying high freight costs and long delivery lead times as some of the specific obstacles.

Strategically located at the doorstep of China and with a highly efficient logistics sector, Hong Kong is well positioned to be the default transportation hub for cross border e-commerce demand from the southern part of China. Moreover, when the Hong Kong-Zhuhai-Macau Bridge is completed, the route through Hong Kong will become even more efficient for consumers residing in the western part of the Pearl River Delta.

Hong Kong also provides an ideal Regional E-Commerce Fulfilment Hub for Chinese e-commerce exporters to better access the South East Asian markets, following the example of Lazada - ASEAN's biggest online marketplace – which is already using Hong Kong as their regional hub.

British online fashion retailer NET-A-PORTER has established itself as one of the world's premier luxury fashion destinations, reaching a monthly audience of over six million via a global multi-channel ecosystem, offering a seamless shopping experience across mobile, tablet and desktop. They chose Hong Kong for their third e-commerce fulfillment hub - supplementing established NET-A-PORTER distribution centres in New York and London. From Hong Kong they service the whole Asia region, including next-day delivery into Australia and Singapore. According to their senior vice president "the primary reason for choosing to open a distribution center in Hong Kong is because it's a free port with strong courier networks, which allows us to improve on our existing shipping service time period by around one day".

Hong Kong seizing the leadership role as the regional fulfilment hub for e-commerce will also generate opportunities for other core service sectors in the local economy. Development of e-commerce businesses requires additional resources and drives market demand for information technology professionals as well as legal, financial and consulting services. Hong Kong's well established and highly respected professional services sector provides an ideal platform for these industries to attract talent to work in the e-commerce space.

Recommendations for Hong Kong to become the leading Regional E-Commerce Fulfilment Hub

In order to capitalise on these opportunities and maximise benefits for Hong Kong to serve as a regional e-commerce fulfilment hub, we recommend the government take an active role in developing and nurturing this sector, including engagement with major China e-commerce companies and logistics providers to secure e-commerce investments in Hong Kong.

This will need continuing strategic investment in hard and soft infrastructure - including precious land and labour resources, which are already in high demand throughout Hong Kong. Shortages of these critical resources are well known across the trade and logistics industry - and other sectors – and require urgent and focused attention from the government.

Specifically, we recommend the following initiatives:

1. Ensure timely completion of Airport 3RS expansion

With the Hong Kong Airport already reaching capacity for take-off and landing slots during parts of the day, the Three-Runway System (3RS) project should proceed smoothly and complete on schedule by 2023.

For Hong Kong to maintain its position as the world's largest and most efficient hub for air cargo and logistics, we urge that all efforts are made to alleviate bottlenecks during the interim years, including active engagement with our Pearl River Delta (PRD) neighbours to seek resolution on airspace co-ordination, which should enable potential for some capacity expansion in the short-term.

We support the ongoing initiatives seeking to add incremental flight capacity within the existing two runway system, including raising the limit to 70 flights per hour between 08.00 and 22.00 and looking for more off-peak slots, including early mornings and late nights, through increased deployment of the much quieter latest-generation aircraft during extended hours of airport operation.

Additionally, we understand improved airspace co-ordination across the Hong Kong, Macau and Guangdong authorities could yield additional flight capacity throughput at HKIA.

We also encourage diligent exploration of practically viable options to utilise spare capacity at neighbouring airports such as Zhuhai - clearly defined as **interim** solutions - for the specific needs of specific sectors such as business aviation and specialised freight services. Whilst the impending completion of the HKZM Bridge will dramatically reduce transit times between Zhuhai and HKIA, careful consideration will be needed on broader multi-jurisdictional aspects such as customs, tax and immigration processes.

2. Successful completion of major new ground transport links including the Hong Kong-Zhuhai-Macau Bridge

Major land infrastructure projects such as the Hong Kong-Zhuhai-Macau Bridge and related road links to the North-West New Territories should be completed as soon as possible. In the e-commerce business, time is of critical importance and more efficient road networks will enable Hong Kong to maintain a seamless connection between the international air and sea ports and the end-consumers across Hong Kong and the Greater PRD.

3. Accelerate deployment of allocated land in Tuen Mun West

A strategic, territory-wide approach for logistics and industrial warehousing should be reviewed and progressed in a timely and regular fashion. As newer developments in Hong Kong move westwards to Tuen Mun and Hung Shui Kiu areas, we request the Government proceed and allocate and release land, licensing businesses to operate within our legal framework on a level playing field basis, including for example the consideration of temporary use of brownfield sites.

In particular, we encourage the long-planned release of land at Area 38 and Area 49 in Tuen Mun West, where some 10 hectares of land has been reserved, and further north at brown-sites and degraded land in the Hung Shui Kiu area. Such initiatives would facilitate the growth of high-end e-commerce and related logistics businesses, with excellent transport links to serve the PRD and eventually the wider region, through the HKIA.

4. Expedite the conclusion of the HK-ASEAN Free Trade Agreement

Hong Kong's Free Port status has long been a major strength of our trade and logistics pillar industry. However, our neighbours continue to forge ahead with bilateral and multilateral Free Trade Agreements which enhance and expand the trade and logistics flows between those countries, in many cases dis-intermediating Hong Kong from the supply chain ecosystem. We urge the government to expedite the conclusion of the HK-ASEAN Free Trade Agreement.

While the Trans-Pacific Partnership (TPP) agreement appears to have stalled, discussions for the Regional Comprehensive Economic Partnership (RCEP) - embracing sixteen countries including China, Japan, South Korea, India and ASEAN - are now at an advanced stage, with agreement expected by the end of 2017. It is imperative and should be a top priority of the

government that Hong Kong also ratifies similar free trade agreements or frameworks with ASEAN and other countries in order to maintain the level playing field for trade.

5. Review and refine the Transshipment Ordinance and Trade Declaration Charge

In becoming the de-facto e-commerce fulfilment hub for Asia, Hong Kong will be managing the logistics flows of products originating from outside of Hong Kong and destined for multiple international locations – throughout mainland China and across the Asia region. Therefore the facilitation of more efficient and effective transshipment capabilities will help to differentiate us from regional rivals and deliver competitive advantage.

The current Import Export Ordinance requires businesses to process both an Import transaction and a separate Export transaction, which is administratively cumbersome and time consuming. Hence, we believe a review of the Transshipment Ordinance to improve the efficiency of flow of import-export goods to better enable regional fulfilment hub operations, which would benefit Hong Kong. More streamlined transshipment processing would ease the administrative burden and offer opportunities for business efficiencies.

We also encourage the further reduction or even elimination of the Trade Declaration Charge – for which a thorough review is long overdue - particularly as the resulting positive multiplier effects for the economy would far outweigh the revenue generated.

6. Enable and encourage inbound investment for e-commerce companies to establish regional operations in Hong Kong

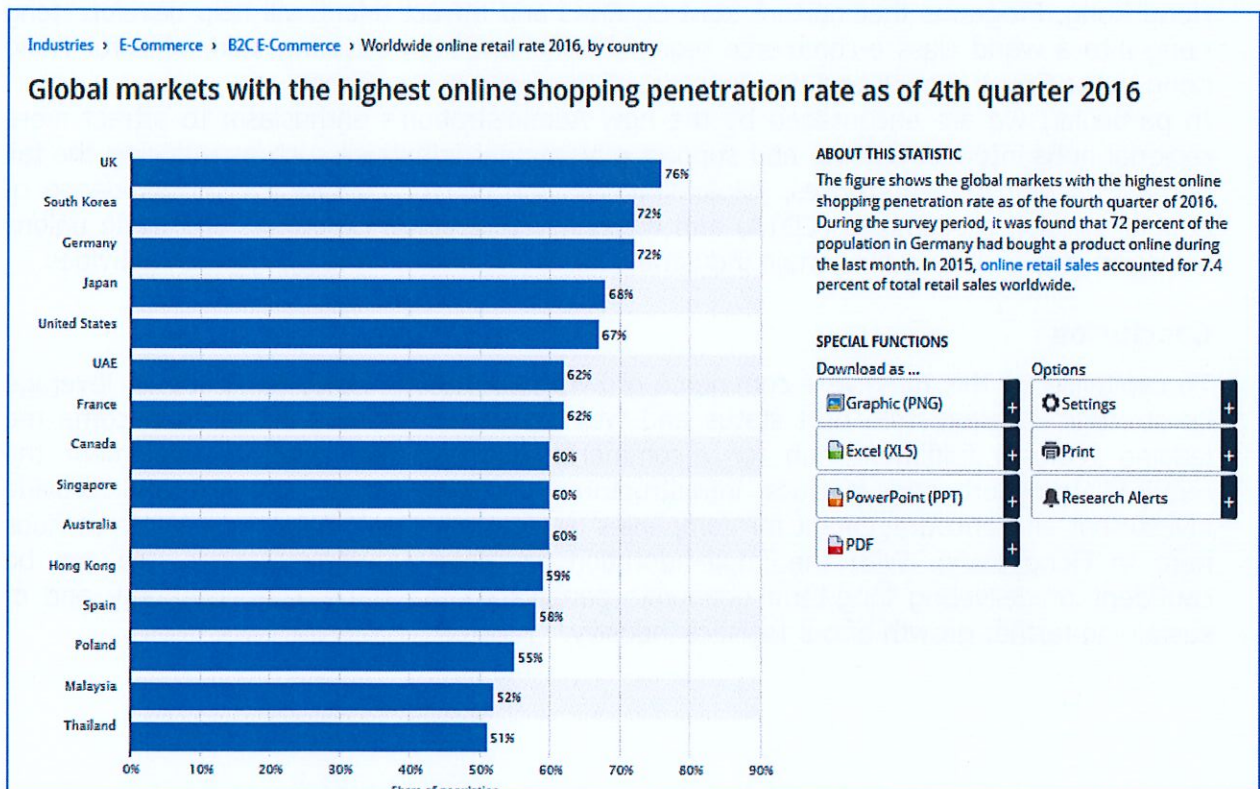
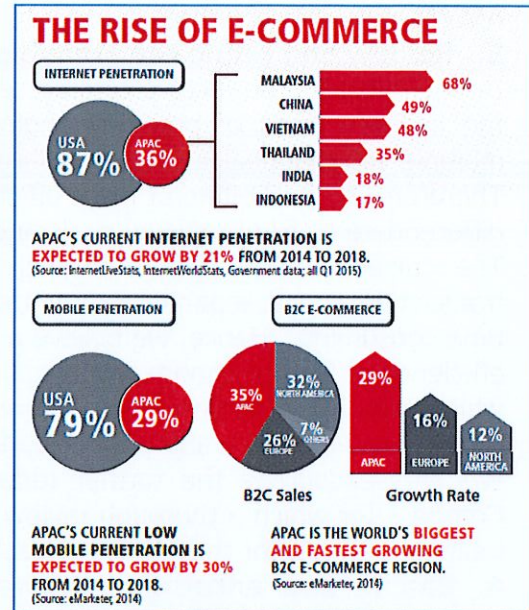
Hong Kong should provide encouragement for inbound investment from e-commerce companies and online platforms to establish financial and information technology hubs in Hong Kong. Programs that nurture start-up firms and attract talent will help develop Hong Kong into a world class e-commerce regional fulfilment hub, ensuring leadership for Hong Kong in the future growth and development of the e-commerce frenzy.

In particular, we are encouraged by the new Administration's enthusiasm to attract more regional hubs into Hong Kong, and support government initiatives such as reducing the tax burden on start-up enterprises, expanding the portfolio of comprehensive avoidance of double taxation agreements (CDTA) and working with employers' groups and trade unions to import foreign labour for certain industries, including logistics and distribution activities.

Conclusion

To capitalise on this massive e-commerce growth opportunity, Hong Kong should leverage its strategic location, free port status and well developed logistics sector to become the leading regional fulfilment hub for e-commerce business. We need to implement the required transport and logistics infrastructure, unshackle trade barriers and provide investment and encouragement for companies to establish their regional e-commerce hubs here in Hong Kong. With the implementation of these recommendations, we can be confident of delivering long-term economic benefits to the Hong Kong economy and of sustaining further growth of our logistics industry.

APPENDIX - EXHIBITS



Source: <https://www.statista.com/statistics>