

China: “One Country, Two Systems”—Myth or Reality? *For Hong Kong: “Twenty Years Down and Thirty to Go”*

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Abstract

This paper is a study of the concept of “One Country, Two Systems” as practiced by the People’s Republic of China and Hong Kong after twenty years of Hong Kong’s reunification with the “motherland.” It addresses the question whether the phrase is an empty slogan or an economic and political reality. The paper delineates key elements of the Sino-British Joint Declaration which permitted Hong Kong to continue its capitalist system for the next fifty years, and points out important characteristics of both China’s and Hong Kong’s capitalist market relating to market capitalization, the stock market, the banking system, finance, and property ownership. It concludes by discussing several issues relating to U.S. China trade relations which may impede progress in the development of both China and Hong Kong in creating “socialism with Chinese characteristics.”

Key Words: “One Country, Two Systems”; Hong Kong Special Administrative Region; State-owned enterprises; Land-use rights; tariffs

1. Introduction: The Context

The term “Two Chinas” often refers to a geopolitical situation in which two political entities each call themselves “China,” differentiating between the People’s Republic of China, more commonly referred to as the PRC or “Mainland China,” established in 1949 as a result of Chairman Mao’s Zedong’s successful revolution (Holmes, 2015), and the Republic of China, known internationally as “Taiwan.” This paper, however, is not an exercise in political science, but one of economic analysis. The paper will deal with the PRC and how it has attempted to change its fundamental economic organizing principle from socialism to some variant of capitalism in the context of “One Country, Two Systems” (Wang, 2018/2019) and its often tumultuous relationship with Hong Kong. Has the reunification of Hong Kong with the PRC continued the movement of China towards “real” capitalism or only the trappings of capitalism? Is the phrase “One Country, Two Systems” an empty slogan or an economic and political reality? There is one more complication: “While most Hong Kongers consider themselves Chinese, they do not consider themselves as part of China” (Boland, 2018).

2. Hong Kong Returns to China

July 1, 2017 marked the 20th anniversary of Hong Kong’s return to the “Chinese Motherland” as a part of the “remarkable journey toward the great renewal of the Chinese nation,” as described by China’s President Xi Jinping (reported in China Daily, 2017). [Excerpts from the speech of President Xi Jinping may be found in Appendix I.] President Jinping spoke about a “New China” and credited his predecessor, Deng Xiaoping, with putting forward the “great vision of One Country, Two Systems,” “eager to adopt capitalist methods and reform in order to stimulate economic growth and restore confidence in the [Communist] party” (Holmes, 2015).

However, as it has become clear, when President Jinping references such concepts as sovereignty, security, and development or “One Country,” he was clearly alluding to the authority of the central government, in which the Hong Kong Special Administrative Region (HKSAR) would be granted a *degree of autonomy* within the new paradigm of “market socialism” adopted to the PRC (Gong & Cortese, 2017).

This position was underscored when, at the United Nations in New York, Chinese State Council Vice-Premier and Foreign Minister Qian Qichen delivered a speech on September 24, 1997 in which he proclaimed the success of Hong Kong: “On 1st July this year, China resumed exercising its sovereignty over Hong Kong, washing away our national humiliation of one and a half centuries and opening up a new chapter of the process of the Motherland's peaceful reunification. Looking back at the last two months and more, Hong Kong has maintained social stability and economic prosperity, and people of Hong Kong, Chinese people, and people around the world have been pleased to see this” (quoted in Edwards, 1998, p. 761).

2.1 The Elements of the Sino-British Agreement

The Sino-British Joint Declaration on the Future of Hong Kong (1984) consisted of eight paragraphs and three Annexes. According to the agreement, “The whole makes up a formal international agreement, legally binding in all its parts. An international agreement of this kind is the highest form of commitment between two sovereign states.” Fung (1997, pp. 289- 290) commented:

“The PRC and the United Kingdom (UK) capped two years of hard negotiations by entering into an international agreement: the Sino-British Joint Declaration on the Future of Hong Kong. The Joint Declaration is a bilateral treaty sounding in international law, registered with the United Nations. The agreement binds: (1) the outgoing sovereign state of Britain, into transferring sovereignty over Hong Kong to China, subject to certain specified conditions and safeguards; and (2) the incoming sovereign state of China, upon resumption of the exercise of sovereignty over Hong Kong in 1997, into giving her people “a high degree autonomy” under Deng Xiaoping's famous twin dicta “One Country, Two Systems” and “Hong Kong People Ruling Hong Kong.””

The HKSAR was promised independent executive, legislative, and judicial power (de Lisle & Lane, 1997; Davis, 2005/2006; Yin, 2014) and that the HKSAR would enjoy a “high degree of autonomy except for foreign and defense affairs” (Tamanaha, 1989). As noted by Chen (2011, p. 294), “Given the low level of the rule of law in the PRC as of 1984, to have faith then in the successful implementation of “One Country, Two Systems” after 1997 was to take a leap in the dark.” The protections afforded to the HKSAR have been referred to as the “Basic Law” (Fung, 1988). Hong Kong would continue to be governed where its common law tradition would be “constitutionally interfaced” with China's civil law socialist legal system (Chan, 1996; Husa, 2017). There were several important sections of the agreement that referred to the unusual status of Hong Kong as what might be described as “quasi-sovereign” or a “quasi-state entity” (Twu, 2017). The Basic Law explains that in addition to Chinese, the English language may also be used before and in organs of government. Although the national flag and national emblem of the PRC would become those of the HKSAR, the HKSAR may use a “regional flag and emblem of its own” in appropriate circumstances. From the standpoint of the economy, the HKSAR was promised that it would be able to maintain its capitalist economic and trade systems previously practiced in Hong Kong and keep its own currency.

The following are the most relevant provisions of the Basic Law outlining the PRC's policies regarding Hong Kong:

- “The [HKSAR] will be directly under the authority of the Central People's Government of the [PRC and] will enjoy a high degree of autonomy, except in foreign and defense affairs.”
- “The [HKSAR] will be vested with executive, legislative and independent judicial power, including that of final adjudication. The laws currently in force in Hong Kong will remain basically unchanged.”
- “The Government of the [HKSAR] will be composed of local inhabitants. The chief executive will be appointed by the Central People's Government on the basis of the results of elections or consultations to be held locally. Principal officials will be nominated by the chief executive of the [HKSAR] for appointment by the Central People's Government. Chinese and foreign nationals previously working in the public and police services in the government departments of Hong Kong may remain in employment. British and other foreign nationals may also be employed to serve as advisers or hold certain public posts in government departments of the [HKSAR].”

- "The current social and economic systems in Hong Kong will remain unchanged, and so will the life-style. Rights and freedoms, including those of the person, of speech, of the press, of assembly, of association, of travel, of movement, of correspondence, of strike, of choice of occupation, of academic research and of religious belief will be ensured by law in the [HKSAR]. Private property, ownership of enterprises, legitimate right of inheritance and foreign investment will be protected by law."
- "The [HKSAR] will retain the status of a free port and a separate customs territory. It can continue the free trade policy, including free movement of goods and capital."
- "The [HKSAR] will retain the status of an international financial centre" with free flow of capital and the Hong Kong dollar remaining freely convertible. The HKSAR may authorize designated banks to issue or continue to issue Hong Kong currency under statutory authority.
- It will have independent finances with its own budgets and final accounts, but reporting it to the Central People's Government. Additionally, "the Central People's Government will not levy taxes on [it]."
- "The HKSAR may establish mutually beneficial economic relations with the United Kingdom and other countries [...]."

On a practical level, the official name for the HKSAR in international relations (for example, in connection with the World Bank or the International Olympic Committee, where Hong Kong would continue to sponsor teams in its own name under Article 151, Chapter 7 of The Basic Law) would be "Hong Kong, China." In such a context, the HKSAR would continue to maintain and further develop economic and cultural relations and enter into agreements with states, regions, and relevant international organizations and to maintain its membership in these organizations as well (Tang, 2007). The HKSAR may continue to issue travel documents for Hong Kong, which Ching (2018) notes are primarily seen in Hong Kong as "documents that offer safety and security." Boland (2018) notes that "The only legal currency in Hong Kong is the homegrown Hong Kong Dollar, which is pegged to the US dollar. The Chinese Yuan is the official currency of China." Interestingly, any international agreements to which the PRC is not a party, but where Hong Kong is such a party, will remain in force and may continue to be implemented in the HKSAR.

In terms of the ordinary exercise of police powers, the government of the HKSAR is charged with responsibility for the maintenance of public order. In recognizing the preeminence of the PRC in matters of defense, any military forces of the PRC which may be stationed in HKSAR shall be complementary to those of the SAR and shall not interfere in the internal affairs in the HKSAR.

The specifics of the PRC's policies regarding Hong Kong were found in the *Annex* which details the way the HKSAR will be administered after the official take over which took place on July 1, 1997. The Annex consisted of following sections: (I) Constitutional arrangements and government structure; (II) the laws; (III) the judicial system; (IV) the public service; (V) the financial system; (VI) the economic system and external economic relations; (VII) the monetary system, (VIII) shipping, (IX) civil aviation; (X) education; (XI) foreign affairs; (XII) defense, security and public order; (XIII) basic rights and freedoms; (XIV) right of abode, travel and immigration. These policies were stipulated in a "Basic Law of the Hong Kong Special Administrative Region."

President Jinping asserted that China would continue to practice socialism (Lippit, 2005) or its variant of "socialism with Chinese characteristics" (Quan, 2018) and will be officially recognized by the National People's Congress and will remain unchanged for a period of 50 years. President Jinping touted this arrangement as advantageous for both entities, but "has not clarified what happens after that" (Reuters, 2017). Many, however, remained skeptical that the PRC would not interfere with Hong Kong's economic and political choices in favor of more authoritarian or "central" solutions (Deutsche Welle, 2018).

In order to maintain at least the fiction of autonomy for Hong Kong, an actual border between the special administrative region and the PRC has continued. "Travelers still need to clear passport controls when moving between Hong Kong and the mainland, just as they would at any other international border" (Twu, 2017). Perhaps, as Twu (2017) commented, this structural arrangement was created in order to shore up global confidence in Hong Kong as an independent or at least "quasi" independent entity and as an example of how Taiwan could one day rejoin the Mainland and effect the eventual complete reunification of China (Edwards, 1998). In making the case that Taiwan would one day be united with the PRC, Lin (1988/1989) noted that "Both Taiwan and Hong Kong share many of the same characteristics that enable a fair comparison and useful deduction of how Taiwan could unify with China.... It is the home of thousands of small entrepreneurial firms and several large, indigenous private sector multinational firms.

The Taiwanese combination of private entrepreneurship and management... is closer to that found in Hong Kong than anywhere in Asia. Because of their strategic location and trade-inclined economies, Hong Kong and Taiwan would serve China as excellent economic intermediaries to the rest of the world.” The real question may lie in assessing whether democracy-minded residents of Hong Kong would accept the notion of “one country” as a means of preserving two separate economic and political systems and the hope of maintaining the limited autonomy of Hong Kong (see Cheung, 2018); or whether Twu (2017) is correct when he asserted: “To the leaders of the Chinese Communist Party, tolerating two systems is a means to achieving one country.” Are these two views reconcilable?

3. Real or Cosmetic Change?

At least in the economic sphere, many of the trappings of “Hong Kong capitalism” (Bradsher, 2007) have rubbed off on the PRC. For example, the benefits attributable to the open trading system in Hong Kong have inured to China’s benefit. Although the PRC was founded as a hard-line socialist country, adopting the Soviet model of state central planning (Balcerowicz, 1995; Hunter & Ryan, 1998), it has slowly embraced the tenets of capitalism, especially since economic reforms were enacted in 1978 under Deng. Rattner (2017) stated that “Skeptics notwithstanding, China’s model, which has brought more people out of poverty faster than any other system in history....” As Holmes (2015) noted, “due to the reforms Deng [Xiaoping] put in place, China has gone from being a country that opposed capitalism to one that embraces property rights, profits and free market competition.” Holmes (2015) may be too effusive in his analysis, but certainly there have been significant strides towards at least embracing capitalist principles within the context of broad state control.

An indication of the PRC’s embrace of capitalism may be seen in the market capitalization of the various worldwide stock exchanges. The Shanghai Stock Exchange ranks number four in the world, with total capitalization of approximately \$4.5 trillion; Hong Kong, at \$4.2 trillion, is number seven; and the Shenzhen Stock Exchange, at approximately \$3 trillion, sits at number eight (see Desjardins, 2018). By way of comparison, the Moscow Stock Exchange has a market capitalization of approximately \$636 billion, not even ranking in the top twenty.

Yet, while China has certainly not completed its metamorphosis to capitalism, even taking into account the practical influences of the HKSAR, it certainly has made great strides in this direction. Touryalai & Stoller (2018) note that the “16th annual *Forbes Global 2000* list includes the publicly-traded companies from 60 countries. Collectively, the companies on this list account for \$39.1 trillion in sales, \$3.2 trillion in profit, \$189 trillion in assets and \$56.8 trillion in market value.... For the first time since 2015, China and the U.S. split the top 10 evenly this year. China is home to 291 Global 2000 companies while the U.S. is on top with 560.” Cendrowski (2015) writes that ninety-eight companies on the *Fortune Global 500 List* are based in China, including those headquartered in Hong Kong (Forbes, 2018). [The United States has 128 companies on the list.] While the Forbes list of the largest world-wide public companies shows four of the top ten as Chinese (ICBC -#1, China Construction Bank-#2, Agricultural Bank-#5, and Bank of China-#9), according to Fortune, the top twelve Chinese companies are essentially still state-owned or state-controlled by the State-Owned Assets Supervision and Administration Commission of the ruling State Council (SASAC) (Cendrowski, 2015).

The SASAC has the authority to appoint the individual CEOs of Chinese companies and to make decisions on large investments. Company finances continue to be supported by the Chinese “monobank” system or by banks closely associated with the government of China, and it appears the Chinese government still maintains ownership of the real property assets of these enterprises. According to Cendrowski (2015), the largest shareholders of ICBC include China Huarong, an asset management company controlled by government of China. Cendrowski (2015) also points out that of the companies with the largest losses in 2014, sixteen were from China— the most of any country.

Based on data provided by Andrea Murphy, Touryalai and Stoller (2018) report that the Chinese banking and finance system may be seen as a positive in times of economic distress. For example, China Petroleum & Chemical (#27 on the Forbes list) or another state-owned or state-controlled Chinese company might have an easier time borrowing from Chinese banks regardless of the economic climate at that moment because of their preferred status.

4. Is China Really One Nation with Two Systems?

The question persists: Is the system in China, although heavily influenced by practices emanating from Hong Kong, really capitalism? Has China been able to transform the theory of “One Nation, Two Systems” into reality? (Wang & Leung, 1998; Yeung & Huang, 2015). Rajah (2017) reaffirmed the original idea of Premier Deng and stated that President Xi Jinping’s version of capitalism, referred to as “socialism with Chinese characteristics for a new era,” will now be officially incorporated into the preamble of China’s Constitution (Buckley, 2018). Steven Rattner (2018), Wall Street executive and a counselor in the Treasury Department under President Obama, stated that “despite its [China’s] Communist heritage, [President Jinping] understands the benefits of incorporating a robust free-enterprise element.”

In the past two decades, the export-based growth model (Los, Timmer, & de Vries, 2015) has lifted many Chinese citizens, especially those living in rural areas, out of poverty (Liu, Liu, & Zhou, 2017; Los, Timmer, & de Vries (2015) noted that between 2001-2006, “foreign demand [for Chinese goods] added 70 million jobs, mainly for workers with only primary education. Rattner (2018) also points out that despite all its public indications of FDP growth and reform, over half of China’s population “still live on \$5.50 per day or less.” According to the website of the International Monetary Fund (2017/2018), China’s GDP (PPP) stood at \$16,624 (ranking 79th). By contrast, Hong Kong’s GDP (PPP) stood at \$61,016 (ranking 9th).

Providing income for increased domestic consumption seems to be the key to the next step in China’s growth. However, increasing domestic consumption is far easier said than done. The 13th Five-year Plan 2016-2020 focused in some measure on social reform in China (KPMG, 2016) and, according to Maiza and Bustillo (2016), includes measures “to lift 55 million people out of poverty, create over 50 million jobs in urban zones, raise education levels, and expand coverage for pensions, health insurance, and unemployment insurance.”

However, a part of this plan includes increasing wages which has forced many cheap labor-intensive companies to shift production to lower-wage countries, such as Pakistan, Indonesia, and Vietnam. Meanwhile, an aging population (Tao, Liu, La, Liang, & Gao, 2017; Chen, Zhang, & Gong, 2018), a lack of confidence in the viability of pension and healthcare systems (Liang, Chen, & Gu, 2004; Liu, Liu, & Zhou, 2017), as well as the continued income disparity between the rural and urban populations (Liu, Liu, & Zhou, 2004), has inflated the Chinese saving rate to a disproportionate percentage in relation to wages (Maiza & Bustillo, 2016). Chen, Chen, & He (2018, p. 2) report that household savings in China increased “significantly” over the past decades. They note that “Between 1978 and 2008, the rural household savings rate rose from 15% to 32%, and the urban savings rate from 15% to 28%.” At best, the widespread poverty still evident in rural areas of China will impede further economic expansion that could be gained from an increase in domestic spending. This will cause added pressures on China’s expected 6%+ growth rate, making it that much more difficult for private industry to survive without continued government intervention and assistance.

5. Concluding Comments

On the political front, there have been several incidents which have called into question the “One Country, Two Systems” relationship between Hong Kong and China (Yuen, 2015; Deutsche Welle, 2018). Bradsher (2007) reminded us that as early as 2004, “the Chinese government sent a small flotilla of warships in a slow cruise past the skyscrapers of downtown Hong Kong, in an unsubtle reminder of who is in charge here. The authorities in Beijing had just blocked further progress in Hong Kong’s steps toward democracy.... Less than a year before, China had pushed for stringent internal security legislation, backing down only when 500,000 people took to the streets in protest. The SARS epidemic in 2003 seemed to underscore Hong Kong’s vulnerability to developments on the mainland. The real estate market was moribund.” For a while, the volatile situation seemed to cool down. Bradsher (2007) continued: “On the eve of the 10th anniversary of Hong Kong’s return to Chinese sovereignty (2007), the city appears transformed. Real estate prices have rebounded. Apartment rents are among the world’s highest. Hong Kong’s stock market led the world last year in initial public stock offerings, thanks to China’s biggest banks and other mainland enterprises raising billions of dollars.” Perhaps this was the momentary triumph of economics over politics.

However, just seven years later, another crisis ensued. The *Umbrella Movement* was a political protest that emerged during the Hong Kong democracy protests which began on September 26, 2014. The name came from the use of umbrellas as a visible tool for passive resistance to the Hong Kong police during the seventy-nine day occupation of Hong Kong by demonstrators who were demanding free elections.

The demonstrations were sparked by the decision of the Standing Committee of the National People's Congress (NPCSC) of August 31, 2014 that provided for a selective “pre-screening” of candidates for the 2017 election of Hong Kong's chief executive (Ortmann, 2015; Yuen, 2015). Many democratic-minded Hong Kongers considered this a serious breach of the Basic Law.

Other more recent examples are present as well. In October of 2017, The National Peoples Congress passed a law that punishes people who “disrespect” the Chinese national anthem (Cone, 2017). The legislation seems to be a response to the “booing and jeering [of] the Chinese national anthem” during soccer matches since 2015 (Yu, 2018). While the issue may seem to be trivial to some, Yu (2018, p. 1) notes that it has “aroused substantial public attention to and long-lasting debate over issues such as freedom of speech, the practicality of law enforcement, retroactive criminalization, and the potential threats to the city’s rule of law.” Had political issues once again returned to prominence? The evidence seems mixed.

On the economic front, there are numerous signs of capitalism “with a twist” taking hold in China’s economic policy-making, although, as Rajah (2017) notes, there is an “uncertain future for China’s state capitalism.” Rattner (2017) states that “China is driving hard toward its ‘Made in China 2025’” plan so that “it can manufacture its own high-value components like semiconductors.” It seems that “China, despite its Communist heritage, understands the benefits of incorporating a robust free-enterprise element” (Rattner, 2017). Rajah (2017) adds that “China’s history of rapid growth has been based on gradually ceding more, not less, control to the market.”

Although under the Constitution of the PRC which was adopted in 1982, “all urban land was declared state-owned” and rural land is “formally owned not by the state, but by sometimes ill-defined collectives,” recognition of land-use rights (LURs) and other long-term property rights which could “last for up to 70 years for residential use; for commercial use, 40 years; and for all other uses, 50 years” has “set in motion a fundamental transformation of the relationship between Chinese property holders and the state” (Clarke, 2017). Farmers now have “use” rights on their land for a period up to 30 years. Perhaps in recognition of these changes, the Heritage Foundation (2018) has continued to rank Hong Kong, now clearly an important part of the Chinese economic mix, at 90.2 (“free”) and #1 in its region for the entire time period of over 20 years. China, by way of contrast, continues to lag behind at #110, as “mostly unfree.”

While China is certainly a more open country, especially in such areas as foreign trade and in efforts to attracting foreign direct investment in its manufacturing sector (Zhang & Song, 2001), the belief that the HKSAR has true autonomy and has significantly influenced the policies of the PRC seems problematic or perhaps a bit naïve. Openness to the prospect of capitalist profits should not be equated with progress on other more subtle fronts; for example, in combating the wide-spread theft of U.S. intellectual property (Kilday, 2013; Clark & Hagan, 2018).

Former U.S. Secretary of Commerce in the Obama Administration, Penny Pritzker, has noted that China is no longer a developing country and needs to play by the rules or have its oft-stated goal of a “new model of great power relations – competitive cooperation,” shift to an inevitable and potentially disruptive relationship based on “confrontation” with the United States (Pritzker, 2018), as China and the U.S. fight a war of words (and tweets). Even more dangerous is what appears to be the start of an actual trade war with China. Will there be a “spill-over” effect with Hong Kong?

On June 20, 2018, the U.S. Trade Representative gave the required notice of an initial action in the Section 301 investigation of the “acts, policies, and practices of the Government of China related to technology transfer, intellectual property, and innovation” (Office of the United States Trade Representative, 2018). As a result, the United States imposed an additional 25 percent *ad valorem* duty on products of China with an annual trade value of approximately \$34 billion. The duty took effect July 6, 2018. The June 20 notice also sought “public comment” on the possibility of further actions in the form of an additional 25 percent *ad valorem* duty on products of China with an annual trade value of approximately \$16 billion. To no one's surprise, China was not pleased. On July 6, 2018, China responded by imposing additional duties on goods from the United States. China’s new tariffs will be levied at rates of 5% or 10%, depending on the product. Mullen (2018) further reports that “more than 5,000 US goods will be affected, including meat, nuts, alcohol, alcoholic drinks, chemicals, clothes, machinery, furniture, and auto parts.”

In light of China's decision to respond to the investigation by imposing duties on U.S. goods, the U.S. Trade Representative proposed a modification of the action taken in the initial investigation to maintain the original \$34 billion action and the proposed \$16 billion action, and to impose an additional 10 percent *ad valorem* duty on products of China with an annual trade value of approximately \$200 billion.

In keeping with the theme of this people, the following question seems most relevant: what effect will these developments have on Hong Kong? As early as 1996, Chan (1996, p. 203) stated: "Despite significant justification for pessimism, there remains hope to be guardedly optimistic. The claims of Hong Kong's economic benefit to China probably cannot be underestimated." The Economist (2017) commented about the current economic conditions in Hong Kong and noted that Hong Kong hosts the world's fourth-biggest stock exchange and currency market. "It is a hub for cross-border loans. About half of China's outward direct investment flows through it.... Hundreds of private mainland firms also use Hong Kong to list and as a springboard for foreign expansion." Hong Kong has become "a pan-Asian life-insurance hub in the past decade, hosting the two large regional competitors, AIA and Prudential as well as FWD, an upstart worth several billion dollars" (Economist, 2017). As noted earlier, "The only legal currency in Hong Kong is the homegrown Hong Kong Dollar, which is pegged to the US dollar. The Chinese Yuan is the official currency of China" (Boland, 2018).

On the negative side, Hong Kong's true weakness is technology. The Economist (2017) raises an ominous point: "Perhaps China will ignore its own economic interests and rip up Hong Kong's rule of law. Or perhaps the city's decline will be more insidious, with its regulators and courts decaying. Still, one of Hong Kong's biggest problems is its own lack of confidence. For a rock that was made rich by refugees, that is unbecoming."

The fear is that U.S. relations with the PRC will lead to globally weak economic conditions, major market corrections, and potentially, a worldwide Depression which could have dire consequences for both the PRC and the HKSAR.

APPENDIX I

Excerpts from President Xi Jinping's Speech marking Hong Kong's 20th Anniversary of its Return to the Motherland – July 1, 2017

... Since its return to the motherland, Hong Kong has joined the remarkable journey toward the great renewal of the Chinese nation. As a special administrative region directly under the Central Government, Hong Kong has been re-integrated into China's national governance system since the very day of its return. The Central Government exercises jurisdiction over Hong Kong in accordance with China's Constitution and the Basic Law of the HKSAR, and corresponding systems and institutions have been set up for the special administrative region. Hong Kong's ties with the mainland have grown increasingly close, so have its interactions and cooperation with the mainland. The people of Hong Kong have played an active part in China's reform, opening-up and modernization drive and made their unique and important contribution to this endeavor. They have ever stronger confidence in China's development and national renewal, and share with the people on the mainland the dignity and honor of our great motherland.

... Since its return to the motherland, Hong Kong has maintained prosperity and stability. Hong Kong has kept its distinct features and strengths. Its allure of being a vibrant metropolis where the East meets the West has remained as strong as ever. Under the practice of "One Country, Two Systems", Hong Kong has retained its previous capitalist system and way of life, and its laws have remained basically unchanged. The people of Hong Kong, now masters of their own house, run their local affairs within the purview of autonomy of the HKSAR. The people of Hong Kong enjoy more extensive democratic rights and freedoms than at any other time in its history. Having withstood the impact of the Asian financial crisis, the SARS epidemic and the global financial crisis, Hong Kong has emerged stronger as an international financial, shipping and trading center; and it has been consistently rated by many international institutions as one of the freest economies and most competitive regions in the world. Hong Kong has made substantial advances in various programs, increased external interactions and raised its international profile.

What has happened in Hong Kong fully demonstrates that the concept of "One Country, Two Systems" provides the best solution to the historical question of Hong Kong and the best institutional arrangement to ensure Hong Kong's long-term prosperity and stability after its return. "One Country, Two Systems" has proved to be a workable solution welcomed by the people.

Fellow Compatriots, Dear Friends,

"One Country, Two Systems" is a great initiative pursued by China. It offers a new way of thinking and a new formula to the international community in addressing similar issues. It is another contribution made by the Chinese nation to promoting global peace and development. And it embodies the Chinese vision which values openness and inclusiveness. To uphold and implement the principle of "One Country, Two Systems" meets the interests of the Hong Kong people, responds to the needs of maintaining Hong Kong's prosperity and stability, serves the fundamental interests of the nation, and meets the shared aspiration of all Chinese. That is why I have made it clear that the Central Government will unswervingly implement the policy of "One Country, Two Systems" and make sure that it is fully applied in Hong Kong without being bent or distorted. This will enable us to keep advancing in the right direction.

"One Country, Two Systems" is a pioneering initiative that has no precedent to follow. Its application entails an evolving process. Currently, some new developments have occurred and new issues emerged regarding its application in Hong Kong. Hong Kong needs to improve its systems to uphold national sovereignty, security and development interests. It needs to enhance education and raise public awareness of the history and culture of the Chinese nation. It is yet to build public consensus on some major political and legal issues. The Hong Kong economy also faces quite a few challenges. Hong Kong's traditional strengths start to lose the edge while new drivers of growth are yet to emerge. Housing and other issues that affect the daily life of the people have become more serious. To address these challenges, meet the expectation of Hong Kong people for a better life and advance Hong Kong's development in all sectors, we must stay on the right and steady course, gain a full understanding of the policy of "One Country, Two Systems" and faithfully implement it. Hence, I wish to take the opportunity to talk to you about how to better implement the policy of "One Country, Two Systems" in Hong Kong.

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