

Greater Bay Area Insight

Tracking regional integration

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Economics - China

- ◆ The GBA is moving beyond connecting up the region physically towards freer movement of capital, talent and data
- ◆ New impetus has been injected into tech collaboration with the opening of a Hong Kong science park in Shenzhen
- ◆ Financial ties are also expanding in response to the increasingly diversified needs of wealthy GBA households

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Connecting up the region...

As mainland China transitions to a new growth model, the GBA is serving as a model for industrial upgrading and the creation of new growth engines. The first step is to physically connect the region better. Several major infrastructure projects are helping to cope with rising traffic levels and business needs. More linkages are to follow. Local governments in the region are exploring freer cross-boundary movements of capital, talent and data.

...with more regional tech collaboration...

Hong Kong Science Park recently opened its first branch in the Hetao sci-tech zone of Shenzhen, shortly after the State Council unveiled its development plan for the area. The 30-measure package laid out guidance and timelines for technology collaboration between Hong Kong and Shenzhen. We think the top-down design will help facilitate freer flows of technology, capital and talent and ensure the so-called 'cooperation zone' will serve as a bridgehead for innovation and technology development between the two cities. Having said that, the ambitious strategy involves not just R&D, but also urban development. It will take time to yield results.

...with financial integration now taking off

Given the GBA is increasingly co-ordinated, hosts frequent business exchanges and is home to a relatively wealthy population base, there has been rising demand for cross-boundary financial services. Of all the linkages, the development of Wealth Management Connect (WMC) is particular noteworthy this year, with a notable ramp-up in Southbound flows since it was first launched in September 2021. We expect GBA's financial integration to continue and believe schemes, such as WMC, have further room to grow, aligning with the latest round of mainland China's financial opening measures.

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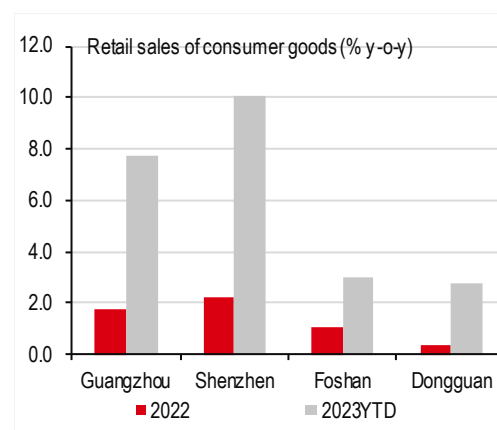
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Hong Kong residents have been hopping over the border to Shenzhen at the weekend to eat and shop. This helps to explain the acceleration in retail sales in Guangdong, particularly Shenzhen (Chart 1), and also vice versa (as mainland Chinese shoppers travel the other way), with retail sales in Hong Kong jumping by over 20% YTD. This shows how it is becoming much easier to travel within the region. Thanks to better cross-boundary transport, there has been a steady recovery in cross-boundary travel across the GBA since the reopening of mainland China. Average passenger departure numbers from Hong Kong through the existing nine cross-boundary transportation networks that link Hong Kong with Shenzhen have reached an average of over 290,000 passenger trips on a daily basis by the end of August (Chart 2).

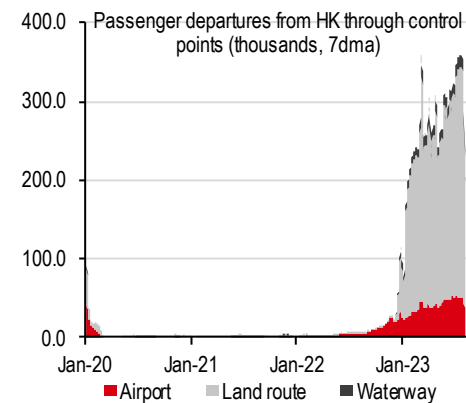
Cross-boundary traffic is just one example that shows the GBA is creating a closer 'living circle', but there are more. In this report, we track the key integration trends in infrastructure, technology and financial sectors. Alongside these regional developments and policy announcements, opportunities are emerging.

Chart 1: Retail sales in key cities in Guangdong have ramped up quickly



Source: Wind, HSBC

Chart 2: Daily departures from HK through nine land routes connected to Shenzhen reached c290,000 in late August



Source: Wind, HSBC

Infrastructure integration – more connected than ever

Recently, several key regional infrastructure projects have reached key milestones. They will play a key role in coping with the increasing cross-boundary passenger traffic and business linkages in the coming years:

- ◆ In June, the new **Guangzhou Baiyun Station**, which is expected by the Guangzhou government to become one of Asia's largest transit-oriented development (TOD) hubs, has entered the decoration phase and is due to be completed by the end of 2023. After completion, it will serve as a hub for various transport connections, including the Beijing-Guangzhou Railway, Beijing-Guangzhou High-Speed Railway, and Guangzhou-Zhanjiang High-Speed Railway, and six metro lines. The district government estimates that more than 50 million passengers will depart from the station annually by 2035, when all planned railways come into operation.
- ◆ **Guangzhou Baiyun International Airport Phase III** also made some major progress by completing the steel structure on its east side and 70% of its underground structure in August. Once completed in 2025, annual passenger and freight handling capacity will increase to 120 million passengers and 3.8 million tons, respectively, according to the Guangdong Airport Authority. Note that in 2022, Baiyun Airport already ranked number one among mainland airports, with passenger throughput of 26 million in 2022.

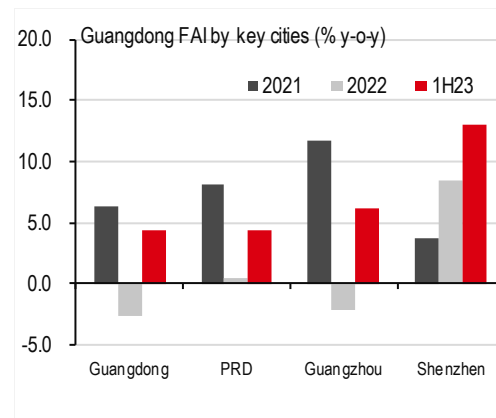
- ◆ In August, another five main towers of the Huangmao Sea Channel Bridge and Gaolan Port Bridge were erected. The whole project, **Huangmao Sea Channel**, is due to be completed in 2024. Upon operation, the channel will team up with other transportation projects, such as the Shenzhen-Zhongshan Link (also to commence in 2024) and Hong Kong-Zhuhai-Macao Bridge (HKMB), and create a cluster of passages on the west bank of Pearl River Estuary.
- ◆ On 11 June, the Shenzhen-Zhongshan Undersea Immersed Tunnel completed docking. This is the world's longest and widest steel-shell concrete immersed tunnel, and is a part of the **Shenzhen-Zhongshan Channel**. Travel time between Zhongshan and Shenzhen, Guangdong, Hong Kong and Macao will be shortened after the completion of the whole project in 2024, and it will become an important linkage between the eastern and western cities of the PRD.

During the two provincial meetings held in January, the Guangdong government said it planned to invest RMB149.1bn in the intercity railway network, known as the 'GBA on Rail,' this year. It has arranged 35 railway projects, eight transportation hub projects and 28 urban rail transit projects. In order to accelerate infrastructure interconnections, the annual planned investment is RMB490bn, including transportation, water conservation, energy and other infrastructure projects. This means more than RMB600bn will flow into infrastructure construction in the GBA during 2023.

In 2021, the investment, construction, operation and management of intercity railways was handed over to two metro companies under the Guangzhou and Shenzhen governments from the Guangdong Provincial Railway Investment Group. Therefore, the number of intercity lines and interconnection facilities in the region are likely to increase from the original plan under which Guangzhou was positioned as the key transportation hub. We think this also explains the elevated fixed asset investment (FAI) growth in Shenzhen after 2021 (Chart 3). Amid ongoing construction of transportation networks, infrastructure-related credit support has increased notably so far this year: by the end of June, Guangdong's outstanding bank loans to the infrastructure sector amounted to RMB3.2trn, up 15.8% y-o-y, 4.7ppts higher than the same period last year.

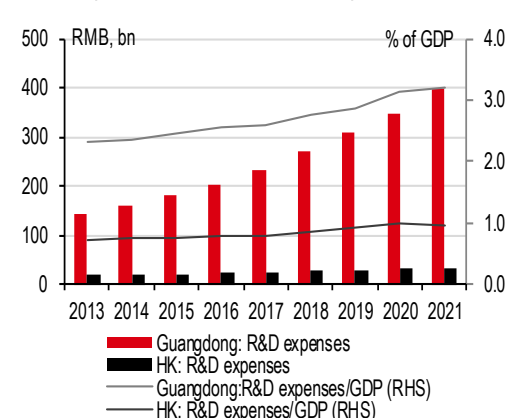
In addition to physical infrastructure construction, more soft infrastructure connections have been established since the reopening of mainland China following the COVID-19 pandemic. For instance, the schemes allowing Northbound travel of Macao vehicles (effective 1 January) and Hong Kong vehicles into Guangdong (effective 1 July) have added new momentum to the flow of people across the region: owners of more than 550,000 single-plate vehicles from Hong Kong and Macao have benefited from the scheme, as previously only dual-plate vehicles were allowed to make cross-boundary journeys (Chinadaily, 9 August).

Chart 3: FAI picked up at a much faster pace in Shenzhen after 2021



Source: Wind, HSBC

Chart 4: Guangdong's R&D expenses steadily ramped up in recent years



Source: CEIC, HSBC

Technology integration backed by Beijing

On 30 August, the State Council released a plan to boost the high-quality development of the Shenzhen part of the Hetao Sci-Tech Innovation Cooperation Zone (Hetao Cooperation Zone) jointly developed by Shenzhen and Hong Kong governments. The central government outlined 30 measures, covering areas such as development targets, overall layout including infrastructure layout of the Shenzhen part, as well as the city's collaboration with Hong Kong to promote international investment and technology development. The plan also set some key targets for the development of the Hetao Cooperation Zone, including:

- ◆ By 2025, a mechanism should be established to support the scientific and technological innovation co-operation between the two regions, while the reconstruction of the Huanggang Checkpoint will be completed and customs clearance procedures realised.
- ◆ By 2035, the Shenzhen section is expected to become a world-class research hub that enables cross-border innovation, supporting the development of the Guangzhou-Shenzhen-Hong Kong-Macao sci-tech innovation corridor.

In 2017, the Shenzhen and the Hong Kong governments signed a memorandum of understanding to jointly develop the Hetao Cooperation Zone, aiming to set up a key base for scientific research, as well as higher education and other complementary facilities. In 2019, the State Council issued the outline development plan for the GBA, in which the central government supported the development of the co-operation zone. The latest State Council plan laid out a more concrete development plan for the Hetao Cooperation Zone. Most importantly, the plan gave detailed guidance about providing access to scientific researchers, as well as how to handle the cross-border movement of items such as merchandise, funds and data. In our view, these are crucial elements to facilitate technology collaboration between the two cities. The clear timeline, in the most recent development plan, to establish a collaboration mechanism will provide a meaningful impetus to technology collaboration between Shenzhen and Hong Kong.

According to Shenzhen government's statistics, there have been more than 150 high-end science and innovation projects implemented within the Hetao Cooperation Zone. So far, over 300 individuals from 24 entrepreneurial teams from Hong Kong and Macao have been stationed there, leading to the granting of 203 patents (Shenzhen Daily, 30 August). After the State Council's policy announcement, Shenzhen authorities said they would launch 40 other projects based in the new co-operation zone, while Hong Kong Science Park announced the launch of its new branch in Shenzhen. So far, five Hong Kong universities have set up 10 innovation centres in the Hong Kong-Shenzhen Innovation and Technology Park on the north side of the corporation zone.

We have argued previously that in order to support technology and innovation, accelerate technology transfer, and promote commercialisation of innovative ideas, it is essential for governments within the GBA region to create an ecosystem in which ideas, policies, capital and the market can come together. Over the past several years, Guangdong province has seen a notable increase in R&D expenses, with its proportion of GDP ramping up nearly 1ppts since 2013 (Chart 4), and in the context of technology co-operation, Hong Kong's link with Shenzhen is probably the most crucial connection because of the areas' complementary strengths and existing collaborations. Having said that, the ambitious strategy on regional integration will take years to yield results as it involves R&D and large-scale urban developments (e.g. Hong Kong's Northern Metropolis Development Plan).

Financial- and capital-market integration

Among the regional market connection schemes, Shenzhen-Hong Kong Stock Connect is probably the most well-known to the investors. Over the past six years, the operation has been smooth, expanding its scope with more active cross-border investment (Table 1). In addition to the stock and bond connections, other financial linkages include Wealth Management Connect (WMC), Qualified Foreign Limited Partnership (QFLP), Private Equity/Venture Capital linkage, ETF Connect and Swap Connect have also been piloted within the GBA context.

Table 1: Major cross-boundary financial connection schemes within GBA

Name		Quota
SZ-HK Stock Connect	Northbound Trading	RMB52bn per day
	Southbound Trading	RMB42bn per day
Bond Connect	Northbound Trading	None
	Southbound Trading	RMB500bn per year, RMB20bn per day
Cross-boundary Wealth Management Connect	Northbound Trading	Total quota: RMB150bn (each side)
	Southbound Trading	Single investor: RMB1mn (each side)
Swap Connect	Northbound swap connect	RMB 20bn per day
	Southbound swap connect	Not started yet

Source: HKMA, HKEX, Wind, HSBC

Among all GBA financial linkage channels, the development of WMC¹ since the beginning of this year is particularly worth noting. There has been rising demand within the GBA for more financial services, including cross-boundary financial products. This may also provide a fresh perspective when we think about mainland China's rising wealth and households' diversified investment needs. In particular, with mainland China reaching a peak in property investment, households may start to broaden out their investments to other financial assets.

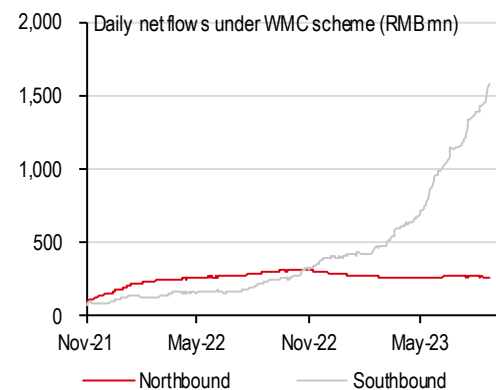
Some key trends from WMC that we have observed so far this year:

- ◆ As of 5 September, daily net fund flows through the Northbound and Southbound schemes under WMC reached RMB266m and RMB1.58bn, respectively, a decline of 8% and an increase of nearly 300% since end-2022 (Chart 5). However, compared with the RMB150bn quota assigned for each side, there is still plenty of space to be utilised.
- ◆ The cumulative value of investment products purchased by individual investors through WMC reached RMB1.46bn by the end of July (+279% y-o-y or five times the level of December 2021). As of July 2023, Northbound accounted for only 15% of total investment while Southbound expanded notably to 85%; the proportion was more evenly distributed 12 months ago (55% and 45%, respectively).
- ◆ Within the Northbound investments, about 70% of the funds were used to invest in wealth management products (WMP), while 98% of the Southbound investments went into deposits. Northbound investors (or Hong Kong and Macao investors) still accounted for the majority (or nearly 75%) of the 57,200 registered individual investors under WMC (Chart 6). This may be a reflection of Northbound individual investors being more aware of financial linkage products and generally more interested in onshore investment opportunities.

¹ In September 2021, the People's Bank of China (PBoC), Hong Kong Monetary Authority (HKMA), and Monetary Authority of Macao (AMCM) jointly launched the Cross-boundary Wealth Management Connect Scheme in GBA (WMC). It is one of the key initiatives tailor-made for the 11 cities of GBA residents, allowing them to invest in approved wealth management products in mainland China, Hong Kong and Macao.

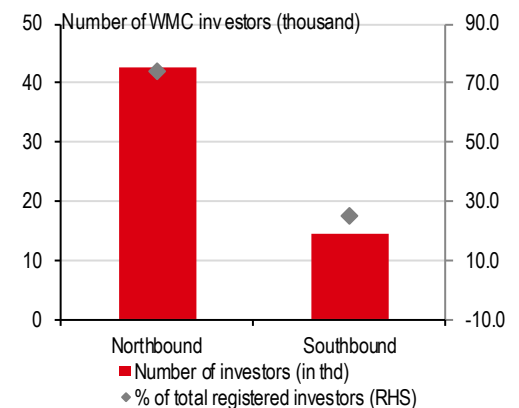
Several factors may have contributed to this divergent trend between Northbound and Southbound investments: 1) a widening yield gap between mainland China and key developed markets over the past year; 2) the strengthening of the USD against major currencies, and hence relatively large depreciation pressure on the RMB; and 3) GBA individual investors are seeking asset diversification.

Chart 5: Southbound flows picked up more rapidly than Northbound flows in 2023



Source: Wind, HSBC

Chart 6: Albeit Northbound investors still accounted the majority of the program



Source: Wind, HSBC

What to expect from regional economic co-operation...

Guangdong is committed to building a better and stronger manufacturing industry (newsgd, 2 June). The government will do this by cultivating 10 strategic industrial clusters, such as new generation IT, NEVs, intelligent connected vehicles, intelligent equipment, high-end equipment and bio-medicine. This policy plan aims to keep the proportion of manufacturing value-added at 35% of GDP in 2027 (total manufacturing value added at RMB4.4trn or 34% of GDP in 2022).

The GBA is expected to serve as a model for the country as it looks to upgrade manufacturing and cultivate new growth engines. From the latest developments, we can see that the Guangdong government has been working to explore the free cross-border flow of scientific research equipment and materials, simplify the import and export procedures of R&D equipment and samples, and most importantly, facilitate cross-border movement of professionals from Hong Kong and Macao. Meanwhile, Hong Kong has also stepped up efforts in promoting its role as an international innovation and technology centre. Therefore, there is likely to be a step-up in the cross-boundary flow of scientific research factors, including high-tech personnel who can bring benefits to the regional technology and innovation co-operation.

For the region, more integrated economic development means that the factors of production – capital, labour and technology – could be redistributed in a more open and connected landscape.

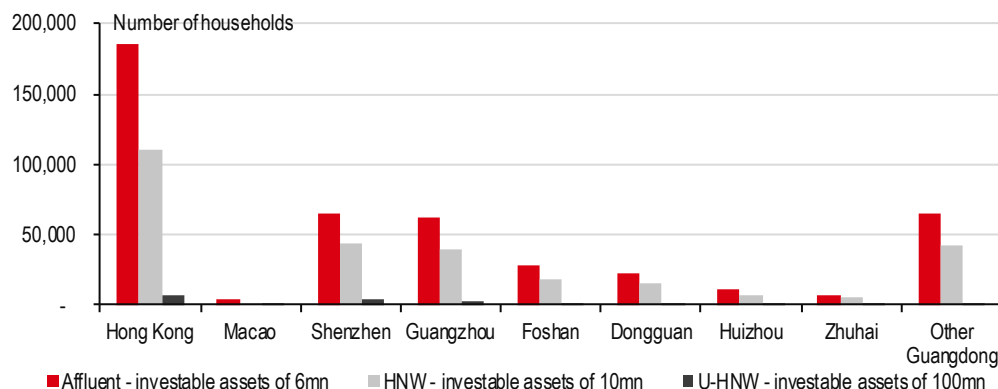
...and financial interconnections

As mentioned earlier, the behaviour of mainland China's wealthy and middle income households may gradually shift amid the changing international and domestic environment. In particular, as mainland China's old growth model, driven by property and infrastructure investment, comes to an end, demand from mainland China's wealthy may gradually shift from real estate to financial assets and from deposits to more diversified financial products (see *China Insights: Households' 'safety first' strategy and how to end it*, 4 September). Currently, wealthier individuals are more inclined focus on the safety and liquidity of assets, or to the diversification of asset allocation.

GBA's financial integration is set to continue, as suggested by the latest round of financial opening measures. Residents within GBA are demanding more financial products, such as insurance. For instance, the recent implementation of the 'Northbound Travel for Hong Kong Vehicles' scheme is expected by Hong Kong's Transport and Logistics Bureau to benefit 450,000 eligible locally registered private cars. According to an estimate by the Chinese General Chamber of Commerce (CGCC), the scheme could generate at least HKD90m of insurance revenue. Similarly, regulators have been promoting the convergence of rules and the development of cross-border medical and critical illness insurance exclusive to this region (Southcn, 1 August), as it was reported that more than 500,000 Hong Kong permanent residents live across the boundary in the GBA (SCMP, April 2023).

GBA is one of the world's richest regions. According to the Hurun China Wealth Report 2022, cities with the largest concentration of high net worth (HNW) households in mainland China present a '3+2+2' pattern, with the top three being Beijing, Shanghai and Hong Kong, followed by Shenzhen and Guangzhou, and then Hangzhou and Ningbo. This means Guangdong has mainland China's largest number of HNW families (with total assets valued at more than RMB10m; USD1.4m) with 307,000 households, followed by Beijing (306,000), and Shanghai (271,000). Even Hong Kong (215,000) has fewer people in this category. Within this category, Guangdong also has 173,000 HNW families with investable assets of more than RMB10m. If we assume each of these families has one member investing through WMC, Southbound investors could grow by another 90%, while Northbound investors could increase by 60%. Therefore, the full benefit from Guangdong's wealthy individuals is yet to be realised when thinking about the future development of WMCs.

Chart 7: Distribution of affluent HNW and Ultra HNW households in the major GBA cities



Source: Hurun report, HSBC

Conclusion

So far this year, GBA's economic growth has been put under pressure by weak external demand and a struggling property market. This backdrop may mean some cities in mainland China face challenges reaching their growth targets set at the beginning of the year. However, despite a rather cautious near-term outlook, some developments may have been overlooked. There has been steady regional integration, which we think is crucial for unleashing the full potential of the GBA over the medium and longer term. Following the reopening of mainland China, the resumption of traffic flows and cross-boundary trips has continued to benefit regional businesses, especially contact-based services. Mega-regional plans and benefits will take years to materialise, but we think in the GBA's case, the national policy is clearly behind it, as the region strives to achieve a more sustainable growth model.

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