Grayson Hunter-Williams

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Examining Atlantic Council's Hong Kong Report

The goal of this paper is to assess whether business conditions in Hong Kong, for most firms, will remain unchanged despite differing legal and political environments the 2020 National Security Law established. The paper focuses on potential risks in the commercial operating environment, including currency risks, compliance challenges, threats to judicial independence, access to accurate information, and data security. Among these risks, currency risks, compliance challenges, and data security are identified as the most pressing concerns.

As systems rivaling Hong Kong's local government policies have been created, there has been a shift towards aligning more closely with Beijing's views rather than those of the local government. These changes may lead to financial markets analyzing Beijing's preferences instead of relying on the word of the Hong Kong Monetary Authority (HKMA). There are concerns about potential currency risks, such as the possibility of altering Hong Kong's peg to the dollar. If extreme capital flight occurs, China may perceive Hong Kong's free capital flows as a vulnerability, potentially leading to a switch to pegging the currency to the renminbi. This would require stricter capital controls between Beijing and Hong Kong or Hong Kong and the rest of the world to prevent capital flight. Although there have been no indications of such a switch being considered, market uncertainty will now factor in Beijing's intentions rather than relying solely on Hong Kong authorities and systems.

Growing Beijing influence in Hong Kong policies has raised concerns regarding compliance with two different legal systems. The United States has imposed sanctions through laws or executive orders on various individuals or institutions within Hong Kong since 2020. In response, China passed the Anti-Foreign Sanctions Law in 2021, which imposes punishments and allows for the seizure of entities that comply with foreign sanctions. Currently, this law has not been implemented in Hong Kong. Hong Kong itself, along with most foreign financial institutions, largely follows U.S. blocking sanctions (although the Hong Kong government has stated that it will only enforce sanctions imposed by the United Nations Security Council). Financial entities may face significantly increased compliance costs if tensions between the two legal and financial systems continue to escalate.

The Implementation Rules of the National Security Law have heightened concerns about data safety in Hong Kong. Previously, entities located in Hong Kong already had to assess the risk of their data (or client's data) being secretly accessed. The law now provides a legal framework for the seizure, searches, and surveillance of data in cases of national security. Concerns have emerged regarding the law being used against international firms to benefit mainland competitors. Some entities, such as the New York Times, have already started shifting data storage out of Hong Kong. While no actions have been taken against financial entities thus far, data security concerns have influenced businesses' decisions regarding operating in Hong Kong.

This paper does not argue that any financial changes have been made to the Hong Kong system due to the National Security Law. However, the implementation of the National Security Law in Hong Kong allows for a greater possibility of China's interference in Hong Kong's political scene, which may increase risks and costs for financial entities. Hong Kong remains highly profitable for China in its open market state, and there are no indications that China currently wishes to alter Hong Kong's economic framework. Therefore, it is reasonable for financial entities to expect minimal risks when operating in Hong Kong. Nevertheless, considering the rising tensions, monitoring pro-Beijing media within Hong Kong, and observing broader U.S. political trends, as suggested in the article, would be an advantageous strategy.