

# Andrzej Buszko

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## **THE CHANGES OF THE CONSTRUCTION MARKET IN HONG KONG DURING THE YEARS 1990-2002**

***Andrzej Buszko***

Chair Macroeconomics  
University of Warmia and Mazury in Olsztyn

Key words: market, competition, development, changes.

### **A b s t r a c t**

The main task of this study is to show the changes in construction market in Hong Kong. The study is connected with the time of 1990-2002. The construction companies were divided into three groups: foreign, local and Chinese ones. The major role in the 90 played the foreign organizations. In the middle of 90 the Chinese firms took the advantage. The background of this process was examined and presented.

### **ZMIANY NA RYNKU USŁUG BUDOWLANYCH W HONGKONGU W LATACH 1990-2002**

***Andrzej Buszko***

Katedra Makroekonomii  
Uniwersytet Warmińsko-Mazurski w Olsztynie

Słowa kluczowe: rynek, konkurencja, rozwój, zmiany.

### **A b s t r a k t**

Celem artykułu jest przedstawienie zmian na rynku budowlanym Hongkongu. Zbadano lata 1990-2002. Zwrócono uwagę na trzy kategorie przedsiębiorstw: zagraniczne, lokalne oraz chińskie. Stwierdzono, iż udziały w rynku uległy zasadniczym zmianom. W połowie lat 90 przewagę utraciły firmy zagraniczne na rzecz podmiotów lokalnych oraz chińskich. Ukazano podstawowe źródła powyższych zmian.

## **Introduction**

The aim of the paper is to present the changes of construction market in Hong Kong nad the attempt estimation of the influences of the foreign companies on domestic ones. The sudy was covered during the years 1990-2002

when there was the economic revival of the construction market. The following hypothesis was named: The activity of foreign construction companies helped the development of local and Chinese firms operating in Hong Kong.

During the 1990-2002 the overall construction output performed by yearly dynamic more than 10% providing the turnover nearly 10 HK\$b (*Singapore Annual Report 2003*). The basic information on Hong Kong construction market is presented at table 1.

**Table 1**

The selected economic data of Hong Kong's construction market during the years 1990-2002

Data	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
The value of construction market HK\$b	8.9	9.5	10.6	11.9	13.6	16.9	17.9	18.2	19.5	20.1	21.8
The GNP yearly dynamic (%)	5.5	4.8	5.9	5.1	5.9	7.1	6.1	4.8	6.1	3.2	3.1
The share of construction in GNP (%)	6.1	7.1	7.3	7.8	8.2	6.2	8.8	9.0	8.9	9.1	9.1
The number of construction workers '000	122	121	119	117	122	121	117	117	119	111	133

Source: own calculation based on Singapore Annual Report 1. Singapore Chamber of Commerce. Singapore 2003

Since the construction market in Hong Kong always reached high dynamic and turnover it was a an attractive place of penetration for foreign construction companies. Additionally there was a boom in the market (LAI 1984). During the years 1978-1984 the value of construction output reached the level of 7-9 HK\$b on yearly basis. That time nearly all contracts were taken over by foreign companies (HO 1987). After seasonal boom in mid 80 foreign construction companies left Hong Kong, and such a step did not make any changes in the market (ALEXANDER 1995).

The law in Hong Kong is based on English solutions. Additionally the system of commerce law is based on international standards. Due to above factors foreign construction companies could gain all needed information for their business activity.

The market of construction materials has not developed. The basic materials are imported from three main sources (the basic stream of deliveries come from the region and Australia – 85% of total import, the rest come from USA and EU). The finishing products come mainly from USA, UE, China and Taiwan (60% of deliveries). There are the close ties between production of construction products and contractors. The construction companies rely on successful deliveries of materials. Secondly the high value of construction materials import attract the contractors. This is not only because of capital connection among the producers of construction materials and contractors but

because of the practical skills of usage such products. That why construction companies follow the import of construction materials (LEONG 1987). Such a scenario was noted in 1978 in Hong Kong. The import of construction products increased on yearly basis by 7% made foreign companies to reopen their activity in this market (HO 1987). Based on literature the benefits of foreign companies operating in local markets are like follows:

- there is the shortage of local construction companies. Demand for the works is higher than supply. Foreign firms can increase the supply and reduce the demand significantly.

- the foreign construction companies offer is better according quality and price terms (MURRA 1995).

The second statement is very important. In free market economy the price is the key factor and influences the terms of the tenders. This is confirmed by the situation in Hong Kong in mid 80, when the contracts were taken over by foreign firms (FLANNGAN 1999). The financial results study confirms the relation among the level of taxes and turnover and profits. The relation is presented in table 2.

**Table 2**

The yearly turnover dynamic, the profit brutto and the tax level paid by foreign companies and local ones during the years 1978-1984

	Foreign companies							Local companies						
	78	79	80	81	82	83	84	78	79	80	81	82	83	84
The yearly turnover dynamic (%)	16	22	34	51	43	51	46	7	8	11	9	14	11	14
The share in the market (%)	27	35	41	46	52	56	71	73	65	59	54	48	46	29
The profit brutto HK\$b	21	16	11	9	11	6	4	17	14	11	16	9	7	8
The tax value HK\$b	14	11	9	8	5	4	2	11	8	7	9	7	4	5

Source: Hong Kong Trade Development Council. Report 1. Hong Kong 1985.

During the economic revival the foreign construction companies increased their turnover. The dynamic of increase was several higher than among local entities. For example in 1983 foreign companies increased their turnover by 51% but local ones by 11% only. The share of the market was changed as well. The unquestionable share was taken by foreign companies. Their share in the market (taking into consideration the value of production) in 1978 was 27%, but in 1984 reached the level of 71%. The share of local firms decreased from 73% to 29% accordingly. In spite of the fact that foreign companies increased their turnover the level of taxes and profit brutto decreased. In 1978 the value

of profit brutto was 21HK\$b decreased to the level of 4 HK\$b. This was more than five times. The same trend was related with the taxes. During the same period of time the foreign companies reduced their taxes obligations by seven times, from 14HK\$b till 2 HK\$b in 1984.

Local companies performed differently. Their value of profit brutto decreased, but the decline was not so sharp like in foreign entities. The same process was connected with the taxes value. Such a decline was caused by the low dynamic of turnover and the loss of the market share.

During analysed time the changes of big value contracts( over 500 mio HK\$) were noticed. In the years 1978-1984, 97% of such contracts were taken over by foreign companies. Moreover local companies did not take any part in 61% of big value contracts (CHOW 1995). This result gives clear information, that foreign companies relied on their labor force only and the local companies could not perform as the effective competitors.

The situation in the market (where the key role play foreign companies) is regarded as positive in following cases:

- local companies increase their technological ability, and they can provide competitive offer systematically,
- there is a close cooperation between foreign and local companies. The domestic companies take part in technology advanced projects and they increase their share in the market (CARILLO 1996).

Within the years 1990-2002 the local companies gained the better position. This process was different from the situation that happened in the mid 80. The companies from mainland China could strengthen their position as well. This was especially seen after 1997, when Hong Kong was returned back to China. Those changes were presented in table 3.

The analysed period should be divided into two separate times. first covers the years 1990-1997 the second one covers the years 1998-2002. During the first period of time the 10<sup>th</sup> largest foreign construction companies increased their turnover from 2.1HK\$b till 6.6HK\$b in 1997. Starting from 1997 their turnover decreased till 4 HK\$b in 2002. The different trend was noticed among local and Chinese companies. The first group of companies gained higher level of turnover from 0.1HK\$b in 1990 till 5.8HK\$b in 2002. There was the break point in 1999. when local companies surpassed foreign companies. That time local companies reached the level of 4.8HK\$b. but foreign companies 4.1HK\$b accordingly. The group of 10<sup>th</sup> local largest construction companies become the key market player in Hong Kong. At the same time Chinese companies systematically increased their turnover. In the beginning 90 their turnover was relatively small. less than 10 mio HK\$. This turnover level was far below local and foreign;s turnovers. Till 1996 the Chinese construction companies played marginal role in the market. Starting from 1997 the turnover increases. The

**Table 3**

The turnover value of 10<sup>th</sup> largest foreign, local and Chinese construction companies operating in Kong Kong during the years 1990-2002 (HK\$b)

Year	Foreign companies	Local Firms	Chinese Firms
1990	2.1	0.1	*
1991	3.4	0.13	*
1992	3.1	0.14	0.01
1993	3.6	0.12	0.01
1994	4.2	0.3	0.02
1995	5.1	1	0.3
1996	6.6	1.3	1
1997	5.9	2	1.1
1998	4.3	3.2	1.7
1999	4.1	4.8	2.2
2000	4	5.3	1.9
2001	4.2	5.8	3.2
2002	4	5.8	3.5

Source: Hong Kong Chinese Chamber of Commerce Annual Report. Hong Kong 2003

\* less than 10 mio HK\$.

**Tabela 4**

The share of foreign, local and Chinese construction firms in A and B project execution in Hong Kong during the years 1990-2002 (%)

Years	A Category Projects			B Category Projects		
	Foreign companies	Local companies	Chinese companies	Foreign companies	Local companies	Chinese companies
1990	95	5	*	91	9	*
1991	97	3	*	82	18	*
1992	91	9	*	63	37	*
1993	87	13	*	47	45	8
1994	88	12	*	37	48	15
1995	76	14	10	37	46	17
1996	65	22	13	32	48	20
1997	58	25	17	22	53	25
1998	55	23	22	19	51	30
1999	48	33	19	18	51	31
2000	43	25	32	19	48	33
2001	42	24	34	21	44	34
2002	41	31	28	17	58	25

Source: Building and Contractor Authority. Hong Kong 2003.

dynamic was quite high and was quite close to the turnover's of 10<sup>th</sup> largest foreign companies. The value of Chinese construction companies turnover reached the level of 3.5 HK\$b.

The increase of the turnover was not the only change in the construction market. The next change was related to complicated investment which required technical knowledge, experience, works of coordination skills. Such complicated investment were divided into two categories A and B. The first one included high value investment more than 1 HK\$b, and focused on project management like like Hong Kong airport contract. The value of this contract exceeded 100 HK\$b and 650 construction firms were included. The group B focused on special project like tunnel works, land improvement. The approximate value of those project was about 500 mio HK\$.

In the beginning of 90 the foreign companies took over majority of A and B contracts. In 1990 those firms were involved in 95% A contracts and 91% B contracts. This dominant share was decreased systematically. In 2002 foreign construction companies executed 41% A contracts and B contracts only. The local companies gained bigger share of the market. In 1990 they could take over 5% of A contracts, but in 2002 they took over 31% this category of projects. Within 6 years Chinese firms could get any contracts of A category. They won the first such projects in 1996. Their share of the market was 10% of A category projects. In following years Chinese companies increased their share of the market. In 2001 they gained even bigger share in the market than local companies. The share of Chinese entities was 34% in A category projects. In 2002 the share decreased slightly till 28%.

The constructions companies were involved in B category contracts differently. In the beginning of 90 dominant share of above mentioned projects gained foreign firms. Their share of the market was on the level of 91%. Such a high share can be explained by the skills of foreign constructions companies, which allowed them to carry on any kind of special projects. There was a shortage of such skills among Chinese and local firms. Year by year foreign companies lose their share in B category projects. In 2002 this share was on the level 17%. Majority of those contracts won local companies. At the end of analyzed period their share of the market constituted 58%. Just for comparison in 1990 such share was 9% only.

A substantial progress was noticed among Chinese companies. They started expansion in 1993, when their share of the market was just 8%. In 2002 Chinese firms could reach the level of 25% and replaced the foreign entities.

The close cooperation and setting up joint-venture is regarded as the key factor of local and Chinese firm;s success. The Chinese companies were searching for close contacts with domestic and foreign companies. This trend is presented in table 5.

**Table 5**

The number of joint-venture firms (JV) in Hong Kong during the years 1990-2002

Year	J.V. Foreign firm and local one	J.V. Foreign firm and Chinese one	J.V. Local firm and Chinese one
1990	226	*	8
1991	137	*	11
1992	112	11	22
1993	76	34	28
1994	65	46	33
1995	57	51	37
1996	54	48	56
1997	44	71	51
1998	47	86	50
1999	51	119	75
2000	43	210	78
2001	28	221	89
2002	5	326	116

Source: own estimation based on Business Register of Companies of HongKong. Hong Kong, 2003.

The data from table 5 provide the information on the number of joint-venture companies among foreign, local and Chinese firms. The significance number drop of joint – venture between local and foreign companies was noted. In 1990 there were 226 such an organizations. but in 2002 there were only 5 joint ventures between local and foreign entities. From the other hand the number of joint venture between foreign and Chinese firms grew up systematically. They started the activity in 1992 with relatively small number 11. In 1993 there was such joint-venture three times more. and in 2002 the number of joint venture bewteen foreign and Chineses firms reached the peak of 326 organizations. The dynamic trend was notice among local and Chinese companies. In 1990 there was 8 such organisations only. but in 2002 – 116.

The increasing number of joint-venture could reduce the technological gap among companies originated from different markets. The participation of Chinese companies in joint venture allowed them not only to adopt new technology but strenghten their position in the market. In 2002 the local and Chinese companies become the important executors of A and b category projects.

Apart from that Chinese and local companies become the general contractors in many important projects. In the beginning of 90 Chinese companies were mainly named as the subcontractors. Starting from 1995 Chinese firms started to act as the general contarctors and setting up the tasks for the other members of the market. This process is presented at the table 6.



**Table 6**

The number of projects (exceeded 5 mioHK\$) executed as the contractor or subcontractor by foreign, local and Chinese companies in Hong Kong during the years 1991-2002

Year	Foreign Company		Local Company		Chinese Company	
	Contractor	Subcontractor	Contractor	Subcontractor	Contractor	Subcontractor
1991	76	9	122	229	*	*
1992	69	11	127	238	*	*
1993	77	13	128	183	*	*
1994	43	15	119	201	*	*
1995	38	18	89	106	28	7
1996	38	17	138	73	43	11
1997	39	28	122	88	48	17
1998	41	45	98	133	51	46
1999	40	50	99	144	55	277
2000	36	51	101	154	58	356
2001	33	54	95	166	62	422
2002	30	76	95	188	77	411

Source: Hong Kong Chinese Chamber of Commerce Report. Hong Kong, 2003.

Within the years 1991-2002 the role as the contractor and subcontractor of foreign companies changed. These firms lost their share as the contractor of 5 mio HK\$ projects. In 1991 foreign companies acted as the general contractor in 76 projects, but in 2002 they took part in 30 such projects. Foreign companies focused on subcontractors works. In 1991 they were involved as the subcontractor in 9 projects, but in 2002 in 76 projects.

The local companies slightly reduced their commitment as the subcontractor and contractor. In 1991 local companies were involved as the contractor in 122 big value projects, and in 2002 in 95 such contracts. The similar trend was noticed according the role as the subcontractor. In 1991 local companies were involved as the subcontractor in 229 more than 5 mioHK\$ projects and in 2002 188 such projects.

The Chinese companies implemented different strategy. They started to act as the contractor in 1995. That time they took over 28 big value contracts and acted as the subcontractor in 7 such contracts. The Chinese firms systematically increased their activity and in 2002 they become contractor in 77 projects and as the subcontractor in 411 projects.

## Conclusion

The carried out analyze confirmed the right of taken hypothesis. The foreign companies operating in Hong Kong helped to develop domestic market and construction firms.

During 1990-2002 the market was changed fundamentally. In the first years of 90 the dominant role of the market played the foreign construction companies. They took over the majority of A and B category of contracts. The foreign companies acted as the contractor mainly. The local and Chinese firms played the role as the subcontractor. In this way they could adopt effective management skills, works technology. In the beginning the local and Chinese companies were involved in B category projects. Thanks to close cooperation, especially based on joint-venture formula local and Chinese firms gained the needed experience and later on could compete in the market. The increase of engagement in A ranked projects and the role as the contractor were confirmation of above mentioned trend.

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