

INNOVATION STRATEGY AND INDUSTRIAL DYNAMICS: THE CASE OF HONG KONG-OWNED MANUFACTURING IN GUANGDONG PROVINCE, CHINA

by

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Abstract

Since mid-2007, Hong Kong-owned manufacturing firms have increasingly been forced to shut down or move their production plants out of Guangdong Province (hereinafter ‘Guangdong’) in the People’s Republic of China (hereinafter ‘China’). Such a cessation or migration of industrial activity has been caused by the combined effects of unfavorable central government policies, a stronger Yuan, escalating raw materials prices, stringent pollution control requirements, cancellation and reduction of tax refunds for low-end processed exports (tax rebate cuts), and the introduction of welfare benefits for employees (such as annual leave and medical coverage). These policies have squeezed thousands of typically labor-intensive, highly polluting industries, such as leather tanning, shoe making, and textile and garment production, out of business. Most of these businesses have been and continue to be run by Hong Kong-based entrepreneurs. Unless these entrepreneurs, who control a sizeable portion of low-end manufacturing in Guangdong, can innovate—or move up the value chain—they face a serious risk of extinction, dramatically undermining Hong Kong’s manufacturing-related service-based economy.

In this paper, we study the dynamics of Hong Kong-owned manufacturing enterprises in Guangdong by conducting an innovation survey, administered from March to August 2008, to 496 Hong Kong enterprises with manufacturing operations in Guangdong. The survey instrument was adapted from the Fourth European Community Innovation Survey (CIS4), which itself conforms to the OECD’s Oslo Manual and provides the analytical framework of our study. In addition to exploring the usual innovation-related issues (as per the CIS4), we also explore the motivation that Hong Kong-owned manufacturing enterprises might have to undertake R&D activities or cooperate with China in pursuing innovation, as well as whether or why Hong Kong-owned manufacturing firms anticipate moving or closing down operations in Guangdong.

Hong Kong-owned manufacturers in Guangdong exhibit many complementary features and unique characteristics. By analyzing the results of the CIS4-based data generated from our survey, this paper applies the statistical techniques of multiple analyses to identify three distinct modes of innovation: product innovation, process innovation, and organizational innovation. Apart from providing a statistical representation of these three modes of innovation, we also consider five structural

characteristics of innovation systems: (i) turnover from new or improved products, (ii) types of innovation activities, (iii) R & D expenditures and other innovation expenditures, (iv) sources of information that facilitate innovation, and (v) innovation activity in manufacturing industries in Guangdong.

Our results confirm that, to keep Hong Kong's service-based, manufacturing-related economy thriving and its economic future strong, it is essential that businesses engage in product or process innovation in order to maintain their competitiveness and move up the value chain.