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WITHDRAWAL SHEET

Ronald Reagan Library

Collection Name LAUX, DAVID: FILES

Withdrawer

CAS 6/9/2010

File Folder CHINA-FOREIGN RELATIONS-HONG KONG (7/1/82-8/24/82)

FOIA

M09-299/1

Box Number 13

COLLINGS

5

ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions
92246	CABLE	HONG KONG 10511 R 6/21/2012 M299/1	2	7/2/1982	B1
92247	CABLE	092345Z JUL 82 D 12/20/2017 M299/1	1	7/9/1982	B1 B3
92248	CABLE	HONG KONG 11153 R 6/21/2012 M299/1	1	7/15/1982	B1
92249	CABLE	HONG KONG 11553 R 6/21/2012 M299/1	1	7/22/1982	B1
92250	CABLE	HONG KONG 11554 R 6/21/2012 M299/1	1	7/22/1982	B1
92251	PAPER	RE HONG KONG D 12/20/2017 M299/1	2	7/28/1982	B1 B3
92252	CABLE	HONG KONG 12051 R 6/21/2012 M299/1	2	7/29/1982	B1
92253	CABLE	HONG KONG 12051 DUPE OF 92252 R 6/21/2012 M299/1	2	7/29/1982	B1
92254	PAPER	RE CHINA AND HONG KONG (P. 3 ONLY) R 12/20/2017 M299/1	1	8/10/1982	B1

Freedom of Information Act - [5 U.S.C. 552(b)]

B-1 National security classified information [(b)(1) of the FOIA]

B-2 Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]

B-3 Release would violate a Federal statute [(b)(3) of the FOIA]

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B-8 Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]

B-9 Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

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ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions
92255	CABLE	101937Z AUG 82 <i>D 12/20/2017 M299/1</i>	1	8/10/1982	B1 B3
92256	CABLE	HONG KONG 13029 <i>R 6/21/2012 M299/1</i>	2	8/13/1982	B1
92257	CABLE	HONG KONG 13030 <i>R 6/21/2012 M299/1</i>	3	8/13/1982	B1
92258	CABLE	HONG KONG 13165 <i>R 6/21/2012 M299/1</i>	2	8/16/1982	B1
92259	CABLE	HONG KONG 13165 (COMPLETE COPY OF 92258) <i>R 6/21/2012 M299/1</i>	2	8/16/1982	B1
92260	CABLE	LONDON 19042 <i>R 6/21/2012 M299/1</i>	1	8/31/1982	B1
92261	CABLE	HONG KONG 13401 <i>R 6/21/2012 M299/1</i>	1	8/19/1982	B1
92262	CABLE	HONG KONG 13401 (DUPE OF 92261) <i>R 6/21/2012 M299/1</i>	1	8/19/1982	B1
92263	CABLE	232121Z AUG 82 (ANNOTATED) <i>D 12/20/2017 M299/1</i>	1	8/23/1982	B1 B3

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ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions	
92264	CABLE	232121Z AUG 82 (UNANNOTATED COPY OF 92263) D 12/20/2017 M299/1	1	8/23/1982	B1	B3
92265	CABLE	232121Z AUG 82 (ANNOTATED COPY OF 92263) D 12/20/2017 M299/1	1	8/23/1982	B1	B3

Freedom of Information Act - [5 U.S.C. 552(b)]

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PAGE 01
ACTION EA-12

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INFO	OCT-00	COPY-01	ADS-00	AID-07	INR-10	SS-10	CIAE-00
	EB-08	H-01	EXIM-04	NSC-01	NSAE-00	COME-00	LAB-04
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	ICAE-00	SP-02	/085 W				

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R 010549Z JUL 82
FM AMCONSUL HONG KONG
TO SECSTATE WASHDC 1712
INFO AMEMBASSY LONDON
AMEMBASSY BEIJING
AMCONSUL GUANGZHOU
AMCONSUL SHANGHAI

UNCLAS HONG KONG 10371

E.O. 120657 N/A

TAGS: EFIN, EINV, PEPR, CH, UK, HK

SUBJ: HONG KONG GOVERNMENT GUARANTEES HOME LOANS
BEYOND 1997

1. WITH THE LEASE ON THE NEW TERRITORIES DUE TO EXPIRE JUNE 30, 1997 - FIFTEEN YEARS FROM TODAY, THE HONG KONG GOVERNMENT (HKG) PLEDGED TO GUARANTEE FIFTEEN YEAR HOME OWNERSHIP SCHEME MORTGAGES BEYOND THIS DATE. THE GOVERNMENT GUARANTEE SHOULD HELP CALM ANY ANXIETY AMONG PARTICIPATING BANKS AS THE COUNTDOWN TO THE LEASE EXPIRATION DATE DRAWS NEARER.

2. UNDER THE PROGRAM, THE HKG HAS AGREED TO GUARANTEE THE OUTSTANDING PRINCIPAL AND INTEREST ON MORTGAGES UNDER THE HOME OWNERSHIP SCHEME. MORTGAGES UNDER THE SCHEME ARE FOR FIFTEEN YEARS. THIS PROGRAM IS TO HELP MEET THE HOME OWNERSHIP ASPIRATIONS OF HONG KONG'S LOWER MIDDLE INCOME FAMILIES. BY YEAR END 1982, THE GOVERNMENT WILL HAVE SOLD SOME 24,000 FLATS SINCE THE SCHEME'S INCEPTION IN 1978. THE HKG AIMS TO BRING AN AVERAGE OF 5,000 FLATS ON TO THE MARKET EVERY YEAR WITH ANOTHER 5,000 A YEAR IN THE PRIVATE SECTOR PARTICIPATION SCHEME STARTING IN 1984. AT PRESENT SOME 50 BANKS AND DEPOSIT TAKING COMPANIES - THE MAJOR FIRMS IN THE LOCAL BANKING COMMUNITY - HAVE LENT MONEY TO HOME OWNERSHIP SCHEME BUYERS.

3. FIFTEEN YEAR MORTGAGES - WHERE BANKERS WOULD BE PLACED IN THE POSITION OF ADVANCING LOANS FOR MORTGAGES NOT BACKED FOR THE FULL FIFTEEN YEARS BY THE SECURITY OF PROPERTY - ARE NOT A PRESSING PROBLEM IN THE PRIVATE SECTOR. HERE MOST MORTGAGES RUN FOR A TWELVE YEAR MAXIMUM. IN PRACTICE, THE REPAYMENT PERIOD IS OFTEN LESS AS MANY HOME PURCHASERS PREFER TO REPAY LOANS AS SOON AS THEY CAN AFFORD TO DO SO.

4. COMMENT: THE HKG HOME LOAN GUARANTEE IS MORE IMPORTANT PSYCHOLOGICALLY TO REASSURE BANKERS AND INVESTORS THAN IT IS IN FINANCIAL TERMS. THE AMOUNT OF MONEY INVOLVED IS RELATIVELY SMALL. IN THE PAST, HOWEVER, THE BRITISH GOVERNMENT HAS GUARANTEED SUBSTANTIAL LOANS FOR THE CASTLE PEAK POWER PLANT EXTENDING TO THE YEAR 2002. THE REAL TEST OF THE GOVERNMENT'S WILLINGNESS TO GUARANTEE LOANS BEYOND THE LEASE EXPIRATION DATE WILL COME WHEN FINANCING MUST BE ARRANGED FOR MAJOR UPCOMING PROJECTS SUCH AS THE NEW AIRPORT. LEVIN

HK - Econ

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NLRR m299 #92246

BY KML NARA DATE 6/21/12

DUNCAN WILLIAM T
82 HONG KONG 10511

07/19/82 111306 PRINTER: EQ

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PAGE 01 HONG K 10511 01 OF 02 021217Z
ACTION EA-12
INFO OCT-00 COPY-01 ADS-00 INR 10 FUR 12 SS-10 CIAE-00
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PM-09 AIT-02 PA-01 ICAE-00 SP-02 SPRS-02 /078 W
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FM AMCONSUL HONG KONG
TO SECSTATE WASHDC 1781
CHINA POSTS COLLECTIVE
CINCPAC HONOLULU HI

~~CONFIDENTIAL~~ SECTION 01 OF 02 HONG KONG 10511
CINCPAC FOR POLAD

E.O. 12065: RDS-4 7/1 2002 (LEVIN, BURTON) OR-M

TAGS: PEPR, EINV, CH HK, UK

SUBJECT: REPORT OF BEIJING GUIDELINES FOR RESOLVING
HONG KONG 1997 PROBLEM

REF: A) HONG KONG 9400; B) HONG KONG 10000

1. (C) SUMMARY. A HONG KONG MAGAZINE SAYS THAT BEIJING POLICY-MAKERS HAVE SET GENERAL GUIDELINES FOR "RECOVERING SOVEREIGNTY" OVER HONG KONG AND MACAO IN THE NOT-TOO-DISTANT FUTURE UNDER A "ONE COUNTRY, TWO SYSTEMS" FORMULA THAT WOULD ALLOW CAPITALISM TO CONTINUE TO DEVELOP IN THESE AREAS. WITH REGARD TO SPECIFIC ARRANGEMENTS, BEIJING HAS ANNOUNCED THAT IT WILL CONTINUE TO CONSULT WITH LOCAL RESIDENTS ON WHAT CONDITIONS THEY NEED FOR FUTURE PROSPERITY. PARTICIPANTS IN THE WELL PUBLICIZED JUNE 15 MEETING BETWEEN DENG XIAOPING AND HONG KONG-MACAO CHINESE LEADERS HAVE INDICATED TO CONGREGANTS THAT THE TALKS WERE NOT VERY PRODUCTIVE ON THE 1997 ISSUE. END SUMMARY.

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PAGE 02 HONG K 10511 01 OF 02 021217Z

2. (U) A CORRESPONDENT OF HONG KONG'S INDEPENDENT LEFTIST MAGAZINE ZHENG MING WRITES IN THE CURRENT ISSUE THAT ACCORDING TO UNDISCLOSED SOURCES IN BEIJING PRC POLICY-MAKERS HAVE DECIDED ON FIVE GUIDING PRINCIPLES FOR RESOLVING THE PROBLEM OF THE FUTURE OF HONG KONG. THEY ARE: (1) HONG KONG AND MACAO ARE CHINESE TERRITORY, AND CHINA SHOULD HAVE COMPLETE SOVEREIGNTY OVER THEM. CHINA CANNOT RECOGNIZE THE LEGALITY OF THE UNEQUAL TREATIES SIGNED IN THE PAST WITH INVADERS. (2) RECOVERING (SHOUHUI) SOVEREIGNTY OVER HONG KONG AND MACAO WILL NOT BE A MATTER OF THE DISTANT FUTURE. (3) THE HONG KONG-MACAO SOVEREIGNTY PROBLEM WILL BE RESOLVED USING THE FORMULA, "ONE

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82 HONG KONG 10511

07/19/82 111307 PRINTER: FQ

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COUNTRY, TWO SYSTEMS. (4) HONG KONG'S "PREVAILING SYSTEM" WILL NOT BE CHANGED. HONG KONG AND MACAO WILL BE ALLOWED TO KEEP THE CAPITALIST SOCIAL SYSTEM, AND THE CONTINUED DEVELOPMENT OF CAPITALISM WILL BE PERMITTED. (5) HONG KONG WILL REMAIN A FREE PORT.

3. (C) COMMENT. WE CANNOT CONFIRM THE OVERALL ACCURACY OF THE ZHENG MING STORY, BUT SOME PARTS OF IT JIBE WITH WHAT WE HAVE BEEN TOLD ABOUT COMMENTS OF PRC LEADERS TO LEADING FIGURES IN THE HONG KONG CHINESE COMMUNITY WHO HAVE BEEN SUMMONED TO BEIJING TO CONFER ON THE 1997 ISSUE IN RECENT MONTHS. VARIOUS OF THESE DIGNITARIES HAVE CONFIRMED TO US THAT CHINESE SOVEREIGNTY OVER ALL OF HONG KONG MUST BE A PART OF ANY SETTLEMENT OF THE COLONY'S FUTURE (REPELS). LU KENG, PUBLISHER OF THE INDEPENDENT MAGAZINE BAI XING, TOLD A CONGENOFF LAST WEEK THAT THE NEW PHASE "RECOVER SOVEREIGNTY" WAS USED IN THE JUNE 15 MEETING BETWEEN DENG AND TWELVE HONG KONG AND MACAO CHINESE LEADERS.

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PAGE 03 HONG K 10511 01 OF 02 021217Z
A POINT HE FOUND SIGNIFICANT. HOW THIS IS TO BE FORMALLY ACCOMPLISHED WHILE AT THE SAME TIME IN PRACTICAL TERMS THE CONTINUATION OF THE "PREVAILING SYSTEM" MENTIONED BY ZHENG MING IS ASSURED WOULD BE THE KEY ISSUE INVOLVED IN THE SETTLEMENT OF THE PROBLEM.

4. (U) THE FORMULA "ONE COUNTRY, TWO SYSTEMS" ALSO SEEMS NEW. HOW IT WOULD BE IMPLEMENTED REMAINS TO BE WORKED OUT, BUT THE PRINCIPLE WOULD SEEM TO REINFORCE PRC LEADERS' OFT-REPEATED ASSURANCES THAT CHINA HAS NO PLAN TO IMPOSE ITS SOCIALIST SYSTEM ON HONG KONG.

5. (C) BEYOND ENUNCIATING SOME VERY GENERAL PRINCIPLES, IT IS NOT CLEAR THAT BEIJING HAS MADE MUCH PROGRESS YET TOWARD FORMULATING DEFINITE PROPOSALS, OR EVEN TOWARD ASCERTAINING WHAT WILL BE NEEDED TO MAINTAIN CAPITALIST PROSPERITY IN HONG KONG AND MACAO. FOREIGN MINISTER HUANG HUA ANNOUNCED IN PORTUGAL, JUNE 14, THAT CHINA WOULD CONTINUE TO EXPLORE THIS PROBLEM WITH ACO'S INHABITANTS. HOWEVER, THE BIG MEETING JUNE 15 BETWEEN DENG AND TWELVE PRO-PRC LEADERS FROM HONG KONG AND MACAO DOES NOT SEEM TO HAVE BEEN TOO PRODUCTIVE. ONE PARTICIPANT, HONG KONG CHINESE CHAMBER OF COMMERCE PRESIDENT K.C. WONG, TOLD A CONGENOFF JUNE 16 THAT HE AND HIS COLLEAGUES HAD NOT PUT FORTH ANY OPINIONS OR PROPOSAL ON THE FUTURE OF THE COLONIES BECAUSE THEY HAD NOT HAD ENOUGH TIME TO PREPARE. (WONG IS NOW CONSULTING OTHER HONG KONG BUSINESSMEN ON THE SUBJECT.) HIS STATEMENT TENDS TO CONFIRM AND FLESH OUT AN EARLIER REMARK

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OUTGOING
TELEGRAM

PAGE 01 STATE 185943
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INFO OCT-00 COPY-01 ADS-00 INR-10 CIAE-00 EB-08 EA-12
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APPROVED BY EB/IFD/OIA:PTLINCOLN, JR.
TREASURY:GLEE
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EA/PRCM:L TAKAHASHI

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TO AMCONSUL HONG KONG

UNCLAS STATE 185943

EO. 12065N/A
TAGS:EINV, HK
SUBJECT: HONG KONG INVESTMENT IN THE UNITED STATES

REF.: (A) HONG KONG 08364; (B) USDOC 10672

1. REFTEL (A) REQUESTED DATA ON BOTH PORTFOLIO AND DIRECT FOREIGN INVESTMENT IN THE U.S. BY HONG KONG. WHILE HONG KONG'S DIRECT INVESTMENT IN THE U.S. IS RATHER SMALL (REFTEL B), HONG KONG DOES HAVE SUBSTANTIAL PORTFOLIO INVESTMENT IN THE U.S. THIS CABLE GIVES DATA ON PORTFOLIO INVESTMENT, AS WELL AS U.S. INVESTMENT IN HONG KONG.

2. FOREIGN INVESTMENT IN THE UNITED STATES IS DEFINED AS DIRECT INVESTMENT IF IT INVOLVES OWNERSHIP OF 10 PERCENT OR MORE OF THE VOTING EQUITY OR ITS EQUIVALENT OF A U.S. ENTITY. ALL OTHER FOREIGN INVESTMENT IN THE UNITED STATES IS CONSIDERED PORTFOLIO INVESTMENT.

3. THE TREASURY CONDUCTED A BENCHMARK SURVEY (E.G., CENSUS) OF FOREIGN PORTFOLIO INVESTMENT IN THE UNITED STATES FOR YEAR-END 1978. THAT CENSUS REVEALED THAT HONG KONG'S PORTFOLIO INVESTMENT IN THE UNITED STATES AS OF DECEMBER 31, 1978, WAS 1,919 MILLION DOLLARS, DIVIDED AS FOLLOWS:

-- (MILLION DOLLARS)

MARKETABLE U.S. LONG TERM SECURITIES - 594
U.S. BANKS' OWN AND CUSTODY LIABILITIES - 1260
OTHER U.S. FINANCIAL AND COMMERCIAL
LIABILITIES - 65

TOTAL: 1,919.

4. SINCE 1978, HONG KONG'S PORTFOLIO INVESTMENT IN THE U.S. HAS INCREASED SUBSTANTIALY.

HONG KONG'S PORTFOLIO INVESTMENT IN THE U.S.:
(MILLION DOLLARS; AS OF END OF)

	1979	1980	1981	1982
BANK'S LIABILITIES:	1,677	2,633	4,030	4,278
OTHER LIABILITIES:	104	60	143 P	N.A.
NET PURCHASES OF U.S.				
LONG-TERM SECURITIES:	128	422	362	123 P

P: PRELIMINARY.
N.A.: NOT YET AVAILABLE.

NOTE: THE DATA FOR BANK LIABILITIES AND OTHER LIABILITIES REPRESENT STOCK POSITIONS. THE DATA FOR NET PURCHASES OF U.S. LONG-TERM SECURITIES REPRESENT FLOWS AND NOT

THE TOTAL HOLDINGS OF SUCH SECURITIES.

5. REF A INDICATED THAT THE DATA WAS TO BE USED TO COMPARE TO THE U.S. TRADE DEFICIT WITH HONG KONG. WE ARE SKEPTICAL ABOUT THE VALUE OF SUCH A COMPARISON FOR A NUMBER OF REASONS: BILATERAL TRADE BALANCES BEAR VERY LITTLE RELATION TO BILATERAL INVESTMENT BALANCES; BILATERAL INVESTMENT DATA INCLUDE NOMINEE ACTIVITY (WHICH IS VERY IMPORTANT IN HONG KONG); THE DATA DOES NOT INCLUDE CLAIMS AND LIABILITIES OF U.S. BANKS' OVERSEAS AFFILIATES AND BRANCHES VIS-A-VIS HONG KONG; AND SINCE FUNDS ARE FUNGIBLE, I.E., SOME U.S. BANKS' CLAIMS ON THE U.K. MAY REFLECT U.K. BANKS' CLAIMS ON HONG KONG, BILATERAL DATA DO NOT INDICATE ULTIMATE SOURCES OR USERS OF FUNDS.

6. U.S. DIRECT INVESTMENT IN HONG KONG GREATLY EXCEEDS HONG KONG'S DIRECT INVESTMENT IN THE UNITED STATES, WHILE U.S. BANK AND OTHER CLAIMS ON HONG KONG ARE OF THE SAME ORDER OF MAGNITUDE AS U.S. LIABILITIES TO HONG KONG.

U.S. INVESTMENT IN HONG KONG:
(MILLION DOLLARS; AS OF END OF)

	1979	1980	1981
U.S. BANKS' CLAIMS:	1,859	2,365	4,217 P
OTHER CLAIMS:	183	176	196 P
DIRECT INVESTMENT POSITION:	1,770	1,969	N.A.
U.S. NET PURCHASES OF FOREIGN SECURITIES (1)	73	-87	17

P: PRELIMINARY.

N.A.: NOT YET AVAILABLE.

(1): REPRESENTS U.S. PURCHASES OF FOREIGN SECURITIES FROM FOREIGNERS DOMICILED IN HONG KONG.

NOTE: THE DATA ON U.S. BANK CLAIMS, OTHER CLAIMS AND DIRECT INVESTMENT POSITION REPRESENT STOCK POSITIONS. THE DATA ON U.S. NET PURCHASES OF FOREIGN SECURITIES REPRESENT FLOWS, AND NOT THE TOTAL U.S. HOLDINGS OF SUCH SECURITIES.

7. A SUBSTANTIAL PORTION OF U.S.-HONG KONG INVESTMENT INVOLVES BANKS' DEALINGS WITH THEIR OWN FOREIGN OFFICES. MARCH 31, 1982, U.S. LIABILITIES TO HONG KONG INCLUDE 1,548 MILLION DOLLARS TO BANKS' OWN FOREIGN OFFICES, WHILE 1981 U.S. CLAIMS ON HONG KONG INCLUDE 2,538 MILLION DOLLARS ON BANKS' OWN FOREIGN OFFICES. VIRTUALLY ALL OF THIS REPRESENTS INTRA-BANK LENDING, CLEARING, AND MONEY TRADING ACTIVITIES. STOESSER

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CAS 6/9/2010

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CHINA-FOREIGN RELATIONS-HONG KONG (7/1/82-8/24/82)

FOIA

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COLLINGS

Box Number

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<i>ID</i>	<i>Document Type</i> <i>Document Description</i>	<i>No of</i> <i>pages</i>	<i>Doc Date</i>	<i>Restric-</i> <i>tions</i>
92247	CABLE	1	7/9/1982	B1
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INCOMING
TELEGRAM
92248

PAGE 01
ACTION EA-12

HONG K 11153 151203Z

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~~CONFIDENTIAL~~ HONG KONG 11153

E.O. 12065: GDS 7/15/88 (PLAISTED, JOAN M.) OR-E
TAGS: ECON, PEPR, EINV, HK, CH, UK, MPOL
SUBJECT: U.K. VIEWS ON THE FUTURE OF HONG KONG

REF: A) HONG KONG 10056, B) HONG KONG 9400,
- C) LONDON 874

1. HONG KONG'S ASSISTANT POLITICAL ADVISOR SAID IT IS IRONIC THAT CHINA IS NOW ACTIVELY CONSIDERING THE 1997 LEASE ISSUE, (AS REPORTED IN REFTELS A AND B) WHILE THE BRITISH GOVERNMENT AT THE TOP LEVEL HAS YET TO FOCUS ON THE PROBLEM. HAVING JUST RETURNED FROM LONDON, HE FOUND THE UK GOVERNMENT STILL PREOCCUPIED WITH THE FALKLAND CRISIS. THE FOREIGN OFFICE IS IN DISFAVOR. WITH THE FALKLAND AFTERMATH, FOREIGN SECRETARY FRANCIS PYM IS HESITANT TO APPROACH PRIME MINISTER THATCHER TO SUGGEST NEGOTIATIONS WITH CHINA ON THE SOVEREIGNTY OF HONG KONG. THE ASSISTANT POLITICAL ADVISOR BELIEVES THE ISSUE MUST BE BROUGHT TO THE PRIME MINISTER'S ATTENTION BEFORE HER AUGUST VACATION. HE SPECULATED THAT SIR EDWARD YOUDE, GOVERNOR OF HONG KONG, WOULD GO TO LONDON SHORTLY TO DISCUSS HONG KONG'S FUTURE.
2. THE PRIME MINISTER AND CHINA'S AMBASSADOR TO THE UK DINED TOGETHER RECENTLY. THE ASSISTANT POLITICAL ADVISOR HAS NOT HAD A REPORT ON THEIR DISCUSSION, BUT EXPRESSED DOUBT THE CHINESE AMBASSADOR WOULD HAVE RAISED ANY CONTROVERSIAL POINTS CONCERNING HONG KONG'S FUTURE.
3. WE WOULD APPRECIATE ANY INFORMATION AMEMBASSY LONDON MAY OBTAIN CLOSER TO THE DATE OF MRS. THATCHER'S SEPTEMBER DEPARTURE FOR CHINA, HONG KONG AND TOKYO.
LEVIN

Hong Kong - Pol - 1

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BY KML NARA DATE 6/21/12

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INCOMING
TELEGRAM

PRC-Hong Kong

PAGE 01 HONG K 11553 222151Z
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FM AMCONSUL HONG KONG
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INFO CHINA POSTS COLLECTIVE
CINCPAC HONOLULU HI
USICA WASHDC 1355

~~CONFIDENTIAL~~ HONG KONG 11553

CORRECTED COPY (TAGS LINE)

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USICA FOR PGM/RC, VOA/NEWS/CA

E.O. 12065: GDS 7/21/88 (LEVIN, BURTON) OR-M
TAGS: PEPR, CH, HK
SUBJECT: HONG KONG TO BE A "SPECIAL ADMINISTRATIVE ZONE?"
NOT NECESSARILY.

REF: BEIJING 9491

1. SUMMARY (C)

REFUTING PRESS SPECULATION, A KNOWLEDGEABLE PRC SOURCE
IN HONG KONG HAS DENIED THAT CHINA HAS PLANS TO MAKE
HONG KONG A "SPECIAL ADMINISTRATIVE REGION." ALL
INDICATIONS ARE THAT BEIJING HAS NOT YET REACHED A
DECISION ON THE FORM OF ADMINISTRATION IT WANTS IN
HONG KONG IN THE FUTURE.

END SUMMARY

2. (LOU) A RECENT FLURRY IN THE HONG KONG PRESS WAS
TOUCHED OFF BY A JULY 16 WESTERN NEWS SERVICE STORY
ON A STATEMENT BY PENG ZHEN, VICE CHAIRMAN OF THE
NATIONAL PEOPLE'S CONGRESS STANDING COMMITTEE AND OF
THE CONSTITUTIONAL REVISION COMMITTEE, WHO CALLED FOR
STUDY AND COMMENTS ON CHINA'S NEW DRAFT CONSTITUTION
BY "COMPATRIOTS IN TAIWAN, HONG KONG AND MACAO AND
OVERSEAS CHINESE." THE REPORT, CARRIED ON THE FRONT
PAGE OF HONG KONG'S MAIN ENGLISH-LANGUAGE PAPERS JULY 17,
POINTED OUT THAT ARTICLE 30 OF THE NEW CONSTITUTION,
WHICH PROVIDES FOR THE ESTABLISHMENT OF "SPECIAL
ADMINISTRATIVE REGIONS" WITH THEIR OWN LAWS, HAS BEEN
SEEN ALL ALONG AS PROVIDING A CONSTITUTIONAL FRAMEWORK
FOR JOINING TAIWAN TO THE PRC WHILE PRESERVING ITS OWN
SOCIAL SYSTEM. "IT WAS CLEAR TO ANALYSTS THAT THE TWO
TERRITORIES (HONG KONG AND MACAO) HAD BEEN PURPOSELY
LINKED WITH TAIWAN" IN PENG ZHEN'S STATEMENT, THE STORY
SAID, TO SIGNAL THE POSSIBILITY THAT BEIJING WILL MAKE
THESE AREAS "SPECIAL ADMINISTRATIVE ZONES" ALSO. THE
REPORT SUGGESTED THAT PENG ZHEN MIGHT HAVE MADE THIS
HINT TO TEST PUBLIC REACTION TO THE IDEA BEFORE PRIME
MINISTER THATCHER'S VISIT TO BEIJING IN SEPTEMBER.

3. (LOU) IN THE FOLLOWING DAYS LOCAL PUNDITS
GENERALLY DEBUNKED THE STORY AND ITS UNNAMED ANALYSTS'
VIEWS AS FAR-FETCHED. TWO MING PAO EDITORIALS AND A
SOUTH CHINA MORNING POST ANALYSIS ARGUED THAT PENG'S
STATEMENT HAD BEEN GROSSLY OVER-INTERPRETED.

4. (C) ON JULY 20 A CONGENOFF RAISED THE SUBJECT OF THE
REPORT WITH JI SHAOXIANG, A NCNA SECRETARY WHO SERVES AS
A LIAISON OFFICER WITH THE HONG KONG GOVERNMENT POLITICAL
ADVISOR'S OFFICE ON PRC-HONG KONG RELATIONS. JI SAID
HE HAD NOT RECEIVED ANY "INSIDE INFORMATION" ABOUT THE
MATTER. HE DESCRIBED THE WIRE SERVICE STORY AS "PURE
SPECULATION," THOUGH HE SAID THE EVENTUAL APPLICATION
OF ARTICLE 30 TO HONG KONG "OF COURSE REMAINS A
POSSIBILITY."

5. (LOU) COMMENT

WE TOO BELIEVE THAT PENG ZHEN'S REMARKS HAVE BEEN
OVER-INTERPRETED. PENG'S PROBABLE PURPOSE WAS SIMPLY
TO PROMOTE UNITED FRONT SENTIMENT BY POINTING OUT THE
BENEFITS OFFERED BY THE NEW CONSTITUTION TO THE VARIOUS
GROUPS OF CHINESE LIVING OUTSIDE THE PRC. PENG NOTED
THAT ARTICLE 30 "CONFIRMS IN LAW" THE SUBSTANCE OF YE
JIANYING'S NINE-POINT PROPOSAL FOR PEACEFUL REUNIFICATION
WITH TAIWAN, BUT HE MADE NO MENTION OF LONG KONG OR
MACAO IN THIS CONTEXT. WE HAVE SEEN NO RELIABLE EVIDENCE
THAT BEIJING HAS YET REACHED ANY DECISIONS ON THE
ADMINISTRATIVE AND LEGAL ARRANGEMENTS THAT IT WOULD SEEK
IN RENEGOTIATION OF HONG KONG'S STATUS. LEVIN

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E. O. 12065: GDS 7 19/88 (LEVIN, BURTON) OR-M
TAGS: ECON, CH
SUBJECT: HONG KONG 1997: UNDER THE PRC FLAG?

REFS: A) HONG KONG 9400, B) HONG KONG 10056, C) HONG KONG
- 10511

(C) SUMMARY: A LEADING HONG KONG BUSINESSMAN WHO RECENTLY VISITED BEIJING SAID PRC LEADERS STRESS THE IMPORTANCE OF REGAINING SOVEREIGNTY OVER HONG KONG, AND WOULD INCLUDE IN ANY SETTLEMENT OF THE 1997 ISSUE THE CONDITION OF FLYING THE PRC FLAG OVER HONG KONG. THIS IS THE MOST EXPLICIT STATEMENT WHICH WE HAVE HEARD OF HOW CHINA WOULD LIKE TO ASSERT ITS SOVEREIGNTY. END SUMMARY.

1. (C) FUNG KING HEY (PROTECT), RECENTLY VISITED BEIJING AND MET WITH PREMIER ZHAO ZIYANG (REF A). HE HAS TOLD THE CONSUL GENERAL THAT PRC LEADERS STRESSED THE IMPORTANCE OF REGAINING SOVEREIGNTY OVER HONG KONG BY 1997, AND THAT THEY TOLD HIM THIS WOULD HAVE TO INCLUDE FLYING THE PRC FLAG OVER THE AREA. AT THE SAME TIME THEY INDICATED THAT THE ADMINISTRATION OF THE AREA NEED NOT CHANGE, AND THAT "EVERYTHING ELSE" COULD REMAIN THE SAME.

2. (C) FUNG AND HIS OFFICIALS HAVE TOLD US THAT ALL OF THE REASSURANCES WHICH CHINA HAS GIVEN TO HONG KONG BUSINESSMEN SO FAR ARE INFORMAL. FUNG'S OFFICIALS CONSIDER THEM TO BE INSUFFICIENT TO MAINTAIN INVESTOR CONFIDENCE IN THE ECONOMIC VIABILITY OF HONG KONG.

3. (C) COMMENT. THERE HAS BEEN CONSIDERABLE SPECULATION IN THE HONG KONG PRESS RECENTLY ABOUT THE STATE OF CHINA'S POLICY TOWARDS THE FUTURE OF HONG KONG. IT IS GENERALLY ACKNOWLEDGED THAT CHINA WISHES TO ESTABLISH ITS CLAIM TO SOVEREIGNTY OVER THE TERRITORY. THE PRC HAS LONG MAINTAINED THAT THE "UNEQUAL TREATIES" WHICH GAVE BRITAIN ITS JURISDICTION OVER BOTH HONG KONG AND THE NEW TERRITORIES ARE NOT VALID. FUNG'S STATEMENT IS THE FIRST EXPLICIT ASSERTION WE HAVE SEEN THAT BEIJING NOW CONTEMPLATES FLYING ITS FLAG OVER HONG KONG AS PART OF ANY SETTLEMENT. WE DOUBT THAT THE BRITISH WOULD BUY SUCH AN ARRANGEMENT. SINCE SERIOUS NEGOTIATIONS HAVEN'T EVEN STARTED ON THE ISSUE, IT WOULD BE PREMATURE TO CONCLUDE THAT THE CHINESE POSITION ON THE FLAG OR OTHER ELEMENTS OF THE SETTLEMENT IS FIXED. THE CHINESE MAY BE STAKING OUT A HARD POSITION TO TEST THE WATERS. THEY ARE PROBABLY ALREADY AWARE THAT THE FLAG. PROPOSAL WON'T BE AN EASY ONE TO SELL HERE.
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China Hints of Hong Kong Takeover

But Wants U.K. Colony To Remain Free Port

By FRANK CHING

Staff Reporter of THE WALL STREET JOURNAL

HONG KONG — China has decided against extending Britain's lease over most of Hong Kong when it expires in 1997 and will "recover" its sovereignty over the entire colony, according to usually well-informed sources here and in Peking.

It is unclear exactly how China hopes to exercise its sovereignty. Chinese leaders have told British officials and visiting Hong Kong businessmen that they intend to preserve the territory's prosperity, keeping it as a free port and a financial and commercial center.

China's paramount leader, Vice Chairman Deng Xiaoping, has repeatedly said that Hong Kong investors should "set their hearts at ease." But investors and other residents of Hong Kong are waiting for a more explicit explanation from the Chinese government as to just how Hong Kong's prosperity can be maintained and what role the British will play.

Time is rapidly running out. Already, the Hong Kong government has had to pledge to guarantee all of the colony's Home Ownership Scheme mortgages extending beyond the expiration of the lease on July 1, 1997—less than 15 years from now. So far, private banks have gone along with this, because they perceive the risk as minimal. But the risk is likely to increase as time goes on without a resolution of the problem of Hong Kong's future.

"The name of the game in Hong Kong is confidence," said Jimmy McGregor, director of the Hong Kong General Chamber of Commerce. "Businessmen worry all the time and big investment decisions need security. If confidence is to be maintained, there is a degree of urgency (to resolution of the Hong Kong question)."

According to Mr. McGregor, the sense of urgency is dictated by the fact that "we've moved into the 15-year critical pe-



Prime Minister Margaret Thatcher is scheduled to visit Peking and Hong Kong in September and, at that time, the matter of Hong Kong's future will be an important item on the agenda. No one expects an agreement to be reached at that time, but if the two sides can agree, say, to set up a joint committee to study the matter, it would be widely regarded as a positive step.

In London, Foreign Office spokesmen say they don't consider reports of China's intentions to regain sovereignty as anything particularly new. Newspapers there, however, ran reports suggesting China was making an early attempt to stake out its Hong Kong negotiating position prior to Mrs. Thatcher's visit.

The Foreign Office declined to comment on the future of the lease, but British officials said the Chinese have assured them that whatever is decided, the nature of Hong Kong will be preserved.

One source close to the Chinese government explained that China's leaders cannot

agree to an extension of the lease because "they don't want to go down in history as traitors, just like Ching Dynasty officials." Another said, "Even African and Asian countries will look down on us if we do that."

On the other hand, the Chinese government doesn't really want to incorporate Hong Kong into the People's Republic because it derives tremendous benefits from the British-administered territory. Hong Kong accounts for between 30% and 40% of China's annual foreign exchange earnings. China also benefits substantially from Hong Kong's financial services, its international contacts and its skills in designing, styling, promoting and marketing of Chinese goods.

Every so often, the suggestion is made that Hong Kong can be run as a special economic zone of China, with British "experts" hired to help run it. But this appears to be totally unacceptable to London.

"Modifications may be possible but there cannot be a mercenary British administration," one British official source said. "Britain won't be politically humiliated," asserted Mr. McGregor, a former Hong Kong government official. "They would sooner pull out."

"The problem, therefore, is to devise a formula that will save the political face of both China and Britain. Richard Lee, a prominent businessman with close ties to the mainland, has suggested that Hong Kong could become an "independent special zone" under the Chinese flag and that the Hong Kong government could be replaced by a "governing committee," with a rotating chairman. He suggests that a Chinese can serve as chairman for, say, three years and be succeeded by a British chairman for the next three years.

Actually, a draft of the new Chinese constitution, which is expected to be adopted later this year, provides for the setting up of "special administrative regions," which can have their own socioeconomic and legal systems. The provision was meant to apply to Taiwan but there is

Doubt on Colony's Future Delays Airport Decision

Special to THE WALL STREET JOURNAL

HONG KONG—Government officials are delaying a decision whether to build a new airport, currently estimated to cost \$6.8 billion, even though the British colony's current facility is badly congested.

Officials said they were being cautious because of the great cost. But some bankers and businessmen believe the government also wants to delay the decision until Hong Kong's future status with China is more clear. Britain's lease on much of the colony's territory expires in less than 15 years.

Some financial observers believe the government, as well as commercial banks, would be reluctant to invest so much money in a project that wouldn't begin to pay for itself before the status of Hong Kong changes.

some speculation that the provision may apply to Hong Kong as well.

Though there are likely to be changes in the way Hong Kong is run after 1997, a British source said, they cannot be so drastic as to undercut Hong Kong's usefulness to China. A key question is the currency that will circulate in Hong Kong after 1997.

"A hard currency is necessary for Hong Kong and China," he said. "It is important that it not be perceived as another form of renminbi (the Chinese currency), because then it will no longer be hard."

Maintaining the economic status quo is the wish not only of China but also of the vast majority of Hong Kong residents. "It is not that Hong Kong people support colonialism or like the British, they don't," said Mr. McGregor of the Hong Kong Chamber of Commerce. "But they are pragmatists, so they prefer the continuation of the status quo, economically speaking."

"It is a nettle that has to be grasped," said Mr. McGregor, "and actually it's not a very prickly one. Deng Xiaoping has shown himself capable of tackling a lot of prickly issues. He is a statesman rather than a politician."

Mr. McGregor and others agree that "the confidence level is very high right now." But, he warned, this can change rapidly and can become "like a run on the bank."

The Chinese government has made it clear that it doesn't want to change the status quo in Hong Kong. It has been preoccupied with internal problems. But the 1997 deadline and attendant legal problems are forcing the Chinese to focus on the issue. Recently, a special group to study the issue is believed to have been set up.

The Chinese privately have told important British visitors that China's sovereignty over all of Hong Kong cannot be challenged. Officially, the British position is that Hong Kong Island, also called Victoria, and part of the Kowloon Peninsula on the Chinese mainland were ceded in perpetuity to Britain by China. The New Territories, which make up the bulk of Hong Kong, will revert to China under the terms of a 99-year lease signed in 1898.

There have been recent indications from United Kingdom sources that London may be willing to acknowledge Chinese sovereignty over all of Hong Kong. In fact, one possibility is for Britain to openly repudiate its 19th century treaties with China by accepting the Chinese position that those were unequal treaties foisted upon a weakened Ching Dynasty by Imperial Britain.

In return, according to this scenario, the Chinese will agree that British administration of the territory can continue. Such an agreement would remove the 1997 deadline, which is hanging over Hong Kong like the sword of Damocles.

Britain's recent war with Argentina over the Falklands inevitably raises speculation that London might also resort to arms to retain control of Hong Kong. But the two situations aren't parallel. For one thing, the population of the Falklands is entirely of British stock, while Hong Kong is 99% Chinese.

Another factor is that 90% of the colony's territory is scheduled to revert to China under the terms of Britain's lease, which would leave a rump colony with no airport, no agricultural land and virtually no industries. Moreover, Hong Kong is dependent on China for food and water.

A formula under which Britain conceded China's sovereignty over Hong Kong and Kowloon could enable the British to continue their administration of the whole territory.

Undoubtedly, both the British and the Chinese have considered various formulas that might be used to enable China to claim that it has regained sovereignty over Hong Kong and for the British to continue running it. But neither country appears to have formulated its bottom-line position.

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E.O. 12065: RDS 7/28/02 (LEVIN, BURTON) OR-M
TAGS: PEPR, CH, HK, UK
SUBJECT: BRITISH, CHINESE STUDY HONG KONG'S
FUTURE

REF: (A) HONG KONG 11153, (B) HONG KONG 10056, (C) HONG KONG 9400

1. (C/WF - ENTIRE TEXT)

2. SUMMARY

A HONG KONG OFFICIAL CLOSELY INVOLVED IN RELATIONS WITH THE PRC SAYS HIS GOVERNMENT CONTINUES TO BE SLOW IN GETTING ITS ACT TOGETHER FOR PRIME MINISTER THATCHER'S SEPTEMBER VISIT TO CHINA AND PROSPECTIVE NEGOTIATIONS ON HONG KONG'S FUTURE STATUS. HE BLAMES THE FALKLAND CRISIS FOR DISTRACTING TOP-LEVEL ATTENTION AND ALSO FOR RAISING BRITISH SENSITIVITIES TO SOVEREIGNTY CLAIMS. HE DOUBTS THAT TOP LEADERS EITHER IN LONDON OR IN BEIJING HAVE BEEN ACCURATELY INFORMED ON THE REALITIES OF HONG KONG'S SITUATION AND THE CONCESSIONS THAT WILL BE NEEDED FROM BOTH SIDES TO ASSURE HONG KONG'S CONTINUED STABILITY AND PROSPERITY. UNDER THESE CIRCUMSTANCES THE MOST HE EXPECTS TO COME OUT OF MRS. THATCHER'S VISIT IS AN AGREEMENT TO HOLD FURTHER CONSULTATIONS ON HONG KONG'S FUTURE. END SUMMARY.

3. ON JULY 26, ASSISTANT POLITICAL ADVISOR RICHARD MARGOLIS (PROTECT) DISCUSSED WITH CONGENOFFS THE STATE OF PLAY AS THE UK AND PRC STUDY OPTIONS AND PREPARE NEGOTIATING POSITIONS ON THE STATUS OF HONG KONG WHEN THE LEASE ON THE NEW TERRITORIES EXPIRES IN 1997. ELABORATING ON EARLIER REMARKS (REF A), MARGOLIS LAMENTED THAT THE UK HAS "LOST VALUABLE TIME" IN RECENT MONTHS AS TOP LEADERS, PREOCCUPIED WITH THE FALKLAND CRISIS, GAVE NO ATTENTION TO THE HONG KONG ISSUE AND WHAT SHOULD BE SAID ABOUT IT DURING THE PRIME MINISTER'S VISIT TO CHINA. IT WAS IRONIC THAT THE BRITISH SIDE, HAVING AT LAST CONVINCED BEIJING THAT ACTION WAS NEEDED SOON ON THE 1997 ISSUE IN ORDER TO REASSURE INVESTORS, WAS NOW ITSELF LAGGING. HE EXPECTED, HOWEVER, THAT GOVERNOR YOUDE WOULD RAISE THE MATTER WITH MRS. THATCHER DURING HIS CURRENT VISIT TO BRITAIN. (THE LOCAL PRESS TODAY REPORTED THAT YOUDE HAD MET WITH THATCHER IN LONDON.)

4. BY CONTRAST, MARGOLIS NOTED, BEIJING HAS BEEN MOVING AHEAD WITH CONSULTATIONS WITH HONG KONG CHINESE ABOUT THE TERRITORY'S FUTURE. NOT ONLY HAVE BUSINESS AND OTHER LEADERS BEEN INVITED TO BEIJING TO TALK WITH TOP LEADERS (REF B), BUT HE UNDERSTANDS THAT NCNA AND OTHER PRC

REPRESENTATIVES SUCH AS CHINA RESOURCES HAVE BEEN QUERYING LESS PROMINENT INDIVIDUALS IN HONG KONG FOR THEIR VIEWS ON THE 1997 QUESTION. DESPITE THIS ACTIVITY, HOWEVER, MARGOLIS IS NOT SURE BEIJING IS GETTING AN ACCURATE PICTURE THROUGH ITS INFORMATION CHANNELS. FOR EXAMPLE, HE SAID THAT CHINESE LEADERS SEEM TO THINK BRITAIN DERIVES LARGE CASH INFLOWS FROM ITS ADMINISTRATION OF HONG KONG. HE SAID THIS WAS NOT SO, AND HE BELIEVES WANG KUANG, THE NCNA CHIEF HERE, REALIZES IT. HOWEVER, HE DOUBTS WANG WILL STICK HIS NECK OUT TO DISABUSE HIS SUPERIORS OF THEIR ILLUSIONS. (COMMENT. A SOURCE CLOSE TO HONG KONG FINANCIER FUNG KING HEY, WHO MET WITH ZHAO ZIYANG IN APRIL, TOLD US ZHAO IS CONVINCED THAT THE BRITISH MUST BE MAKING A LOT OF MONEY FROM HONG KONG, OR THEY WOULD NOT STAY HERE (REF C). HOWEVER, CONSTRUCTION MAGNATE GORDON WU, WHO MET WITH ZHAO ABOUT THE SAME TIME, TOLD CONGENOFFS THAT ZHAO HAS NO SUCH ILLUSIONS. END COMMENT.)

5. BRITISH LEADERS MAY CHERISH ILLUSIONS TOO, MARGOLIS THINKS. FOR EXAMPLE, HE BELIEVES THAT SOME CONCESSION IN PRINCIPAL ON SOVEREIGNTY OVER HONG KONG WILL ULTIMATELY BE NECESSARY TO REACH A NEW AGREEMENT WITH BEIJING, BUT HE DOES NOT THINK MRS. THATCHER HAS YET

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BEEN EXPOSED TO SUCH THINKING. RATHER, HE FEARS THAT GOVERNMENTAL AND PUBLIC OPINIONS IN BRITAIN HAVE HARDENED AGAINST CONCESSIONS ON SOVEREIGNTY OVER ANY OVERSEAS TERRITORY LEST BRITAIN'S POSITION IN THE FALKLANDS AND GIBRALTAR BE AFFECTED. IN THE WAKE OF THE FALKLANDS AFFAIR, THE FOREIGN OFFICE IS SEEN BY MANY AS OVERLY WILLING TO MAKE CONCESSIONS ON BRITAIN'S SOVEREIGNTY, HE SAID, AND WHITEHALL'S FIRST TASK IN PRESENTING ITS VIEWS ON HONG KONG WILL BE TO DO "A BIT OF A SELLING JOB" ON ITS OWN CREDIBILITY.

6. IN A RECENT DISCUSSION WITH THE CONSUL GENERAL, C.H. TUNG, THE INHERITOR OF HIS LATE FATHER'S (C.Y. TUNG) SHIPPING EMPIRE, OFFERED SUPPORTING EVIDENCE FOR MARGOLIS' FEARS THAT BRITISH LEADERS MAY BE ADOPTING AN UNREALISTIC HARD LINE ON THE SOVEREIGNTY ISSUE. TUNG REVEALED THAT ABOUT TEN DAYS AGO MRS. THATCHER HAD PRIVATELY TOLD HIM THAT AS FAR AS SHE WAS CONCERNED, THE ONLY THING SUBJECT TO NEGOTIATION WITH THE PRC WAS THE EXPIRATION OF THE LEASE ON THE NEW TERRITORIES. AN INTERNATIONAL TREATY HAD AWARDED THE UK PERPETUAL SOVEREIGNTY OVER HONG KONG AND THE ADJACENT AREAS OF KOWLOON. THE PRC'S UNHAPPINESS OVER THE STATE OF AFFAIRS WOULD NOT MOVE THE U.K. TO ABANDON ITS SOVEREIGN RIGHTS. AFTER ALL SHE WAS NOT HAPPY WITH SOME OF THE TREATIES ENTERED INTO BY HER PREDECESSORS, BUT HER GOVERNMENT WOULD CONTINUE TO OBSERVE THEM IN KEEPING WITH INTERNATIONAL LAW. THE PRC WOULD HAVE TO DO THE SAME. TUNG EXPRESSED THE OPINION THAT IF THE PM PERSISTED IN WHAT HE CLEARLY THOUGHT TO BE AN UNREALISTIC POSITION, THEN THE PRC AND U.K. WERE IN FOR SOME ROCKY TIMES ON THE QUESTION OF HONG KONG'S FUTURE. IN COMMON WITH MOST FINANCIAL HEAVYWEIGHTS HERE--BOTH BRITISH AND CHINESE--TUNG BELIEVES THAT IF A DEAL IS TO BE STRUCK WITH THE CHINESE, IT WILL HAVE TO FEATURE A U.K. COMPROMISE ON THE SOVEREIGNTY ISSUE IN RETURN FOR PRC ACQUIESCENCE IN CONTINUED BRITISH ADMINISTRATION OF THE ENTIRE TERRITORY.

7. MARGOLIS SAID THAT BRITISH PLANNING FOR NEGOTIATIONS OVER HONG KONG IS DONE LARGELY BY THE HONG KONG AND GENERAL DEPARTMENT IN THE FOREIGN OFFICE, IN CLOSE COLLABORATION WITH THE POLITICAL ADVISOR'S OFFICE HERE. DRAFTS PREPARED IN LONDON ARE NORMALLY SENT HERE FOR COMMENT, HE SAID. ON THE CHINESE SIDE, HE BELIEVES THE KEY MAN IS LIAO CHENGZHI, HEAD OF THE OVERSEAS CHINESE AFFAIRS OFFICE OF THE STATE COUNCIL. LIAO, HE SAID, OVERSAW THE PREPARATION OF SOME EARLY STUDIES OF THE HONG KONG PROBLEM BY THE CHINESE ACADEMY OF SOCIAL SCIENCES (SOME OF WHICH INVOLVED "VERY UNREALISTIC SCENARIOS"). NOW STATE COUNCILLOR JI PENGFEI HEADS A SPECIAL COMMITTEE RECENTLY SET UP TO STUDY THE ISSUE,

BUT MARGOLIS BELIEVES THE CHAIRMANSHIP WAS GIVEN TO JI, A FORMER FOREIGN MINISTER, IN ORDER TO ROPE THE FOREIGN MINISTRY IN ON PROPOSALS THAT WILL STILL BE LARGELY ENGINEERED BY LIAO. (COMMENT. SEVERAL INDEPENDENT HONG KONG PUBLICATIONS HAVE REPORTED THAT A SPECIAL COMMITTEE TO STUDY THE HONG KONG ISSUE WAS SET UP UNDER THE STATE COUNCIL IN MARCH, WITH JI PENGFEI AS ITS CHAIRMAN AND LIAO CHENGZHI AND LUO QINGCHANG AS DEPUTIES. WE HAVE NOT SEEN ANY PRC CONFIRMATION OF THIS REPORT. END COMMENT.)

8. GIVEN THE STATE OF PREPARATIONS, MARGOLIS EXPECTS NO SERIOUS PROGRESS TOWARD RESOLVING THE 1997 QUESTION DURING THE PRIME MINISTER'S VISIT TO BEIJING IN SEPTEMBER. HE THINKS SHE AND THE CHINESE WILL AGREE TO FURTHER CONSULTATIONS BETWEEN THEIR GOVERNMENTS ON THE PROBLEM, AND LITTLE MORE. SUCH CONSULTATIONS WILL TAKE PLACE FORMALLY BETWEEN THE UK EMBASSY AND THE CHINESE FOREIGN MINISTRY, HE SAID, BUT HE PERSONALLY BELIEVES SOME "DIRECT, INFORMAL LINK" WILL ALSO NEED TO BE CREATED TO VET IDEAS BEFORE THEY ARE FORMALLY PROPOSED, AND HE CONFESSES TO "SOME SLIGHTLY MEGALOMANIAC IDEAS ABOUT WHERE THAT LINK MIGHT BE."

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1. (C/NF - ENTIRE TEXT)

2. SUMMARY

A HONG KONG OFFICIAL CLOSELY INVOLVED IN RELATIONS WITH THE PRC SAYS HIS GOVERNMENT CONTINUES TO BE SLOW IN GETTING ITS ACT TOGETHER FOR PRIME MINISTER THATCHER'S SEPTEMBER VISIT TO CHINA AND PROSPECTIVE NEGOTIATIONS ON HONG KONG'S FUTURE STATUS. HE BLAMES THE FALKLAND CRISIS FOR DISTRACTING TOP-LEVEL ATTENTION AND ALSO FOR RAISING BRITISH SENSITIVITIES TO SOVEREIGNTY CLAIMS. HE DOUBTS THAT TOP LEADERS EITHER IN LONDON OR IN BEIJING HAVE BEEN ACCURATELY INFORMED ON THE REALITIES OF HONG KONG'S SITUATION AND 790E791NCESSIONS THAT WILL BE NEEDED FROM BOTH SIDES TO ASSURE HONG KONG'S CONTINUED STABILITY AND PROSPERITY. UNDER THESE CIRCUMSTANCES THE MOST HE EXPECTS TO COME OUT OF MRS. THATCHER'S VISIT IS AN AGREEMENT TO HOLD FURTHER CONSULTATIONS ON HONG KONG'S FUTURE. END SUMMARY.

3. ON JULY 26, ASSISTANT POLITICAL ADVISOR RICHARD MARGOLIS (PROTECT) DISCUSSED WITH CONGENOFFS THE STATE OF PLAY AS THE UK AND PRC STUDY OPTIONS AND PREPARE NEGOTIATING POSITIONS ON THE STATUS OF HONG KONG WHEN THE LEASE ON THE NEW TERRITORIES EXPIRES IN 1997. ELABORATING ON EARLIER REMARKS (REF A), MARGOLIS LAMENTED THAT THE UK HAS "LOST VALUABLE TIME" IN RECENT MONTHS AS TOP LEADERS, PREOCCUPIED WITH THE FALKLAND CRISIS, GAVE NO ATTENTION TO THE HONG KONG ISSUE AND WHAT SHOULD BE SAID ABOUT IT DURING THE PRIME MINISTER'S VISIT TO CHINA. IT WAS IRONIC THAT THE BRITISH SIDE, HAVING AT LAST CONVINCED BEIJING THAT ACTION WAS NEEDED SOON ON THE 1997 ISSUE IN ORDER TO REASSURE INVESTORS, WAS NOW ITSELF LAGGING. HE EXPECTED, HOWEVER, THAT GOVERNOR YOUNG WOULD RAISE THE MATTER WITH MRS. THATCHER DURING HIS CURRENT VISIT TO BRITAIN. (THE LOCAL PRESS TODAY REPORTED THAT YOUNG HAD MET WITH THATCHER IN LONDON.)

4. BY CONTRAST, MARGOLIS NOTED, BEIJING HAS BEEN MOVING AHEAD WITH CONSULTATIONS WITH HONG KONG CHINESE ABOUT THE TERRITORY'S FUTURE. NOT ONLY HAVE BUSINESS AND OTHER LEADERS BEEN INVITED TO BEIJING TO TALK WITH TOP LEADERS (REF B), BUT HE UNDERSTANDS THAT NCNA AND OTHER PRC

REPRESENTATIVES SUCH AS CHINA RESOURCES HAVE BEEN QUERYING LESS PROMINENT INDIVIDUALS IN HONG KONG FOR THEIR VIEWS ON THE 1997 QUESTION. DESPITE THIS ACTIVITY, HOWEVER, MARGOLIS IS NOT SURE BEIJING IS GETTING AN ACCURATE PICTURE THROUGH ITS INFORMATION CHANNELS. FOR EXAMPLE, HE SAID THAT CHINESE LEADERS SEEM TO THINK BRITAIN DERIVES LARGE CASH INFLOWS FROM ITS ADMINISTRATION OF HONG KONG. HE SAID THIS WAS NOT SO, AND HE BELIEVES WANG KUANG, THE NCNA CHIEF HERE, REALIZES IT. HOWEVER, HE DOUBTS WANG WILL STICK HIS NECK OUT TO DISABUSE HIS SUPERIORS OF THEIR ILLUSIONS. (COMMENT. A SOURCE CLOSE TO HONG KONG FINANCIER FUNG KING HEY, WHO MET WITH ZHAO ZIYANG IN APRIL, TOLD US ZHAO IS CONVINCED THAT THE BRITISH MUST BE MAKING A LOT OF MONEY FROM HONG KONG, OR THEY WOULD NOT STAY HERE (REF C). HOWEVER, CONSTRUCTION MAGNATE GORDON WU, WHO MET WITH ZHAO ABOUT THE SAME TIME, TOLD CONGENOFFS THAT ZHAO HAS NO SUCH ILLUSIONS. END COMMENT.)

5. BRITISH LEADERS MAY CHERISH ILLUSIONS TOO, MARGOLIS THINKS. FOR EXAMPLE, HE BELIEVES THAT SOME CONCESSION IN PRINCIPAL ON SOVEREIGNTY OVER HONG KONG WILL ULTIMATELY BE NECESSARY TO REACH A NEW AGREEMENT WITH BEIJING, BUT HE DOES NOT THINK MRS. THATCHER HAS YET

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BY KML NARA DATE 6/21/12

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BEEN EXPOSED TO SUCH THINKING. RATHER, HE FEARS THAT GOVERNMENTAL AND PUBLIC OPINIONS IN BRITAIN HAVE HARDENED AGAINST CONCESSIONS ON SOVEREIGNTY OVER ANY OVERSEAS TERRITORY LEST BRITAIN'S POSITION IN THE FALKLANDS AND GIBRALTAR BE AFFECTED. IN THE WAKE OF THE FALKLANDS AFFAIR, THE FOREIGN OFFICE IS SEEN BY MANY AS OVERLY WILLING TO MAKE CONCESSIONS ON BRITAIN'S SOVEREIGNTY, HE SAID, AND WHITEHALL'S FIRST TASK IN PRESENTING ITS VIEWS ON HONG KONG WILL BE TO DO "A BIT OF A SELLING JOB" ON ITS OWN CREDIBILITY.

6. IN A RECENT DISCUSSION WITH THE CONSUL GENERAL, C.H. TUNG, THE INHERITOR OF HIS LATE FATHER'S (C.Y. TUNG) SHIPPING EMPIRE, OFFERED SUPPORTING EVIDENCE FOR MARGOLIS' FEARS THAT BRITISH LEADERS MAY BE ADOPTING AN UNREALISTIC HARD LINE ON THE SOVEREIGNTY ISSUE. TUNG REVEALED THAT ABOUT TEN DAYS AGO MRS. THATCHER HAD PRIVATELY TOLD HIM THAT AS FAR AS SHE WAS CONCERNED, THE ONLY THING SUBJECT TO NEGOTIATION WITH THE PRC WAS THE EXPIRATION OF THE LEASE ON THE NEW TERRITORIES. AN INTERNATIONAL TREATY HAD AWARDED THE UK PERPETUAL SOVEREIGNTY OVER HONG KONG AND THE ADJACENT AREAS OF KOWLOON. THE PRC'S UNHAPPINESS OVER THE STATE OF AFFAIRS WOULD NOT MOVE THE U.K. TO ABANDON ITS SOVEREIGN RIGHTS. AFTER ALL SHE WAS NOT HAPPY WITH SOME OF THE TREATIES ENTERED INTO BY HER PREDECESSORS, BUT HER GOVERNMENT WOULD CONTINUE TO OBSERVE THEM IN KEEPING WITH INTERNATIONAL LAW. THE PRC WOULD HAVE TO DO THE SAME. TUNG EXPRESSED THE OPINION THAT IF THE PM PERSISTED IN WHAT HE CLEARLY THOUGHT TO BE AN UNREALISTIC POSITION, THEN THE PRC AND U.K. WERE IN FOR SOME ROCKY TIMES ON THE QUESTION OF HONG KONG'S FUTURE. IN COMMON WITH MOST FINANCIAL HEAVYWEIGHTS HERE--BOTH BRITISH AND CHINESE--TUNG BELIEVES THAT IF A DEAL IS TO BE STRUCK WITH THE CHINESE, IT WILL HAVE TO FEATURE A U.K. COMPROMISE ON THE SOVEREIGNTY ISSUE IN RETURN FOR PRC ACQUIESCENCE IN CONTINUED BRITISH ADMINISTRATION OF THE ENTIRE TERRITORY.

7. MARGOLIS SAID THAT BRITISH PLANNING FOR NEGOTIATIONS OVER HONG KONG IS DONE LARGELY BY THE HONG KONG AND GENERAL DEPARTMENT IN THE FOREIGN OFFICE, IN CLOSE COLLABORATION WITH THE POLITICAL ADVISOR'S OFFICE HERE. DRAFTS PREPARED IN LONDON ARE NORMALLY SENT HERE FOR COMMENT, HE SAID. ON THE CHINESE SIDE, HE BELIEVES THE KEY MAN IS LIAO CHENGZHI, HEAD OF THE OVERSEAS CHINESE AFFAIRS OFFICE OF THE STATE COUNCIL. LIAO, HE SAID, OVERSAW THE PREPARATION OF SOME EARLY STUDIES OF THE HONG KONG PROBLEM BY THE CHINESE ACADEMY OF SOCIAL SCIENCES (SOME OF WHICH INVOLVED "VERY UNREALISTIC SCENARIOS"). NOW STATE COUNCILLOR JI PENGFEI HEADS A SPECIAL COMMITTEE RECENTLY SET UP TO STUDY THE ISSUE,

BUT MARGOLIS BELIEVES THE CHAIRMANSHIP WAS GIVEN TO JI, A FORMER FOREIGN MINISTER, IN ORDER TO ROPE THE FOREIGN MINISTRY IN ON PROPOSALS THAT WILL STILL BE LARGELY ENGINEERED BY LIAO. (COMMENT. SEVERAL INDEPENDENT HONG KONG PUBLICATIONS HAVE REPORTED THAT A SPECIAL COMMITTEE TO STUDY THE HONG KONG ISSUE WAS SET UP UNDER THE STATE COUNCIL IN MARCH, WITH JI PENGFEI AS ITS CHAIRMAN AND LIAO CHENGZHI AND LUO QINGCHANG AS DEPUTIES. WE HAVE NOT SEEN ANY PRC CONFIRMATION OF THIS REPORT. END COMMENT.)

8. GIVEN THE STATE OF PREPARATIONS, MARGOLIS EXPECTS NO SERIOUS PROGRESS TOWARD RESOLVING THE 1997 QUESTION DURING THE PRIME MINISTER'S VISIT TO BEIJING IN SEPTEMBER. HE THINKS SHE AND THE CHINESE WILL AGREE TO FURTHER CONSULTATIONS BETWEEN THEIR GOVERNMENTS ON THE PROBLEM, AND LITTLE MORE. SUCH CONSULTATIONS WILL TAKE PLACE FORMALLY BETWEEN THE UK EMBASSY AND THE CHINESE FOREIGN MINISTRY, HE SAID, BUT HE PERSONALLY BELIEVES SOME "DIRECT, INFORMAL LINK" WILL ALSO NEED TO BE CREATED TO VET IDEAS BEFORE THEY ARE FORMALLY PROPOSED, AND HE CONFESSES TO "SOME SLIGHTLY MEGALOMANIAC IDEAS ABOUT WHERE THAT LINK MIGHT BE."

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3. CHINA: OVERTURES ON HONG KONG

Beijing's recent overtures on Hong Kong are designed to reassert China's sovereignty over the British colony in 1997 and to reassure investors and residents that the island's special status will continue in the post-reversion period. The Chinese want to show Taiwan and the US that they can achieve an agreement that accommodates the interests of all parties. Without a continued British presence and the retention of existing managerial expertise, however, Hong Kong's prosperity will be jeopardized.

* * *

Government and private leaders in Hong Kong argue for an early decision on the island's future that will maintain the status quo and thus avoid the exodus of the island's businessmen. The substantial departure of the commercial community would pose a serious problem for China, which acquires up to 45 percent of its foreign exchange and part of its advanced technology through Hong Kong. China reportedly has set up a special committee, including prominent members of the island's Chinese community, to study the potentially adverse effects of reversion.

At a minimum, China insists that its flag fly over Hong Kong. But Thatcher, who is scheduled to visit China and Hong Kong in September, has stated that there can be "no Hong Kong" without the British flag. Thatcher's extreme position could be a bargaining strategy. The 1898 treaty awarding the New Territories to Britain expires in 1997. Upon expiration, 90 percent of the colony would be returned to China, thereby making retention of Hong Kong island and the adjacent areas of Kowloon (given in perpetuity in 1842) virtually untenable.

China's view that two different systems can coexist in one country is implicit in its nine-point reunification proposal; it was explicitly endorsed and amplified by Party Chairman Hu Yaobang last February. More recently, a Chinese official noted that the new draft constitution provides for "special administrative zones" operating with laws designed to meet each area's "specific concerns."

Beijing probably believes that special zones can provide a framework whereby Hong Kong, and eventually Taiwan can be joined to China and simultaneously preserve their non-socialist economic and political structures. But it is unlikely that things can remain as they are if China reasserts its sovereignty over Hong Kong and tries to use officials of a communist system, however unobtrusively, to oversee a capitalist program.

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CHINA-FOREIGN RELATIONS-HONG KONG (7/1/82-8/24/82)

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SECRET/NOFORN

E.O. 12356: DECL: 8/13/12
TAGS: PEPR, EINV, HK, CH, UK
SUBJECT: THE 1997 BLUES: HONG KONG STARTS REALLY
- WORRYING

REF: HONG KONG 11553

1. (C) SUMMARY

HONG KONGERS' LATENT FEARS ABOUT THE COLONY'S POLITICAL FUTURE HAVE SURGED TO THE SURFACE IN RECENT WEEKS, STRONGLY ABETTED BY AND IN TURN FEEDING A DECLINING BUSINESS CLIMATE. THERE HAS BEEN VIRTUALLY NO CHANGE IN THE LONG-HELD PUBLIC POSITIONS OF THE BRITISH AND CHINESE GOVERNMENTS ON THE ISSUE, AND THERE IS NO RELIABLE EVIDENCE AS TO WHAT DECISIONS--IF ANY--LONDON OR BEIJING HAVE MADE IN PREPARATION FOR PRIME MINISTER THATCHER'S SEPTEMBER VISIT TO CHINA. HOWEVER, THE JITTERY MOOD IN THE COLONY HAS PRODUCED A SPATE OF PRESS STORIES OF "INITIATIVES" AND "PLANS," MOST OF WHICH HAVE BEEN ONLY PUFFED-UP SPECULATION. HOWEVER, IN AT LEAST ONE CASE IT APPEARS THAT AN NCHA SOURCE, FOR MOTIVES THAT ARE UNCLEAR, PLANTED A STORY SAYING THAT CHINA INTENDS TO FLY ITS FLAG AND APPOINT HONG KONG'S GOVERNOR AFTER 1997. END SUMMARY.

2. (LOU) THE LEVEL OF ANXIETY ABOUT HONG KONG'S FUTURE HAS MOUNTED RAPIDLY IN RECENT WEEKS AS PRIME MINISTER THATCHER'S VISIT TO CHINA LOOMED CLOSER, AS THE MAGIC DATE OF JULY 30, 1997, PASSED (THE LAST DAY WHEN A STANDARD 15-YEAR LEASE COULD BE SIGNED IN THE NEW TERRITORIES), AND AS THE EFFECTS OF THE WORLD-WIDE RECESSION BELATEDLY IMPACTED ON HONG KONG. RUMORS AND NEWS STORIES CIRCULATED OF A "HARDENING IN CHINA'S POSITION" ON HONG KONG'S STATUS PREDICTABLY ALARMING A PUBLIC WHICH, ACCORDING TO A PUBLIC OPINION POLL RELEASED AUGUST 12 BY AN INDEPENDENT REFORM GROUP, FAVORED BY 95 PERCENT THE RETENTION OF THE STATUS QUO. THE SAME DAY INVESTORS SEEMED TO PUT THEIR MONEY WHERE THEIR MOUTHS WERE AS THE ALREADY BATTERED HANG SENG STOCK INDEX PLUNGED MORE THAN 100 POINTS TO REACH A TWO-YEAR LOW. THOUGH OTHER SIGNIFICANT FACTORS WERE INVOLVED IN THE STOCK DECLINE (SEPT), FEW DOUBTED THAT POLITICAL UNCERTAINTY HAD BECOME IMPORTANT.

3. (LOU) TO SOME EXTENT HONG KONG AND THE PRESS HAVE BEEN SCARING THEMSELVES OVER THE PAST FEW WEEKS AS STORIES OF CHINESE "INITIATIVES" AND "PLANS" HAVE FED ON ONE ANOTHER. FOR EXAMPLE, A JULY 16 STATEMENT BY NPC VICE CHAIRMAN PENG ZHEN WAS RATHER FAR-FETCHEDLY INTERPRETED BY A WIRE SERVICE AS A HINT THAT CHINA

PLANNED TO INCORPORATE HONG KONG INTO CHINA AS A "SPECIAL ADMINISTRATIVE REGION." THE STORY WAS GENERALLY POOH-POOHED IN THE HONG KONG PAPERS (REFTEL), BUT MENTIONS OF THE "TRIAL BALLOON" CONTINUED TO BOUNCE AROUND IN THE INTERNATIONAL MEDIA. NOW THIRD AND FOURTH-HAND REFERENCES TO THIS "CHINESE INITIATIVE" HAVE FOUND MORE CREDENCE IN HONG KONG THAN THE ORIGINAL STORY DID, AND THE "SPECIAL ADMINISTRATIVE REGION" SCENARIO HAS TAKEN ON THE EXAGGERATED STATUS OF A SERIOUS PRC TRIAL BALLOON FLOATING THROUGH THE OVER-HEATED ATMOSPHERE.

4. (C) MORE SERIOUS STORIES, PUBLISHED IN ENGLISH-LANGUAGE PAPERS AUGUST 10 AND 11, SAY THAT CHINA HAS DECIDED TO REPLACE THE UNION JACK WITH THE PRC FLAG AND TO APPOINT--OR PERHAPS HAVE THE POPULACE ELECT--THE GOVERNOR, BUT TO MAKE NO OTHER INITIAL CHANGES IN THE GOVERNMENT. A CONOFF TALKED WITH THE AUTHOR OF ONE OF THE ARTICLES, AN AMERICAN ACADEMIC RESIDENT IN HONG KONG, WHO CLAIMED THAT THE "CHINESE PLAN" HAD BEEN DISCLOSED TO HIM JULY 28 BY AN NCHA CONTACT. HIS SOURCE SAID CHINA HAD DECIDED TO REASSERT ITS SOVEREIGNTY OVER ALL OF HONG KONG IN 1997 BY SUBSTITUTING ITS FLAG FOR THE UNION JACK, APPOINTING A CHINESE GOVERNOR--POSSIBLY A HONG KONG CHINESE--AND LEAVING THE REST OF THE ADMINISTRATION AS IT IS. THE EXPATRIATES IN THE HKG WOULD BE RETAINED, ALTHOUGH NO NEW ONES WOULD BE HIRED AND THE SYSTEM WOULD GRADUALLY BECOME CHINESE THROUGH ATTRITION. HIS SOURCE URGED HIM TO DISCUSS THE PLAN WITH LOCAL AMERICAN BUSINESSMEN AND THEN PUBLISH IT. HE CLAIMS THIS STORY WAS ALSO LEAKED

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TO AT LEAST ONE OTHER FOREIGN CORRESPONDENT, AND PROBABLY TO OTHER LOCAL JOURNALISTS. (AN ALMOST IDENTICAL "PLAN" WAS DESCRIBED IN THE AUGUST 11 HONG KONG STANDARD, ATTRIBUTED TO "MIDDLE-RANKING OFFICIALS OF CHINA-AFFILIATED ORGANIZATIONS HERE.")

5. (C) THE AMERICAN IS PUZZLED BY THE MOTIVATION BEHIND THE LEAK. HE THINKS THAT PERHAPS SOME OLD HONG KONG HANDS IN NCNA BELIEVE BEIJING'S "PLAN" WILL PROVE UNACCEPTABLE TO PEOPLE IN HONG KONG, AND HAVE LEAKED IT TO THE PRESS IN ORDER TO LET BEIJING SEE THE NEGATIVE PUBLIC REACTION. HE SAID HIS SOURCE HAS DESCRIBED BEIJING'S LATEST PLAN AS AN ABRUPT AND VERY RECENT CHANGE FROM AN EARLIER INTENTION NOT TO PUSH HARD ON THE SOVEREIGNTY ISSUE.

6. (LOU) ON THE RECORD, THE PRC AND ITS LOCAL SPOKESMEN HAVE TRIED TO COOL SPECULATION AND ANXIETY, REFUSING TO CONFIRM SUCH STORIES BUT OFFERING NOTHING SPECIFIC TO COUNTER THEM. THEY HAVE BASICALLY REITERATED CHINA'S STAND, ENUNCIATED BY HUANG HUA AT THE U.N. IN 1972, THAT HONG KONG IS CHINESE TERRITORY AND THAT THE PROBLEM OF BRITISH RULE WILL BE RESOLVED "WHEN THE TIME IS RIPE." THEY HAVE THEN REPEATED GENERAL ASSURANCES TO INVESTORS THAT HONG KONG'S PROSPERITY WILL BE MAINTAINED WHILE REFUSING TO BE PINNED DOWN ON WHAT ADMINISTRATIVE ARRANGEMENTS ARE EXPECTED TO MAKE THAT POSSIBLE.

7. (S/NF) DEPUTY POLITICAL ADVISOR RICHARD MARGOLIS, IN CONVERSATION AUGUST 11 AND 12 WITH CONOFFS, EXPRESSED THE CONVICTION THAT PEKING HAS NOT YET SETTLED ON ANY DEFINITE PLAN FOR HONG KONG. HE SAID HIS GOVERNMENT HAS RECENTLY ACQUIRED CLANDESTINE INFORMATION FROM WHAT IT CONSIDERS AN EXTREMELY RELIABLE SOURCE SHOWING THAT GUIDANCE FROM THE HIGHEST LEVEL OF THE PRC IN MID-JUNE ONLY LAID OUT THE "THINKING OF TOP LEADERS WITHOUT CHOOSING SPECIFIC OPTIONS. HE IS CONFIDENT THAT BEIJING HAS NOT PROGRESSED BEYOND THIS STAGE. HIS CONFIDENCE IS SUPPORTED BY AUGUST 13 REMARKS TO A CONOFF BY JI SHAOXIANG AND LI RUOHE, NCNA WORKING LEVEL CONTACTS WHO REGULARLY DEAL WITH THE BRITISH HERE ON POLITICAL ISSUES. THEY AFFIRMED THAT CHINA HAS NOT YET FORMED A DEFINITE PLAN, BUT IS ONLY DISCUSSING "VARIOUS IDEAS." MARGOLIS BELIEVES THAT SOME HONG KONG CADRES, BRIEFED WITH THE MID-JUNE DOCUMENT, HAVE BEEN RETAILING AND SELECTIVELY DISTORTING PARTS OF IT AROUND TOWN AND THAT THIS MAY BE THE SOURCE OF THE RECENT PRESS STORIES. SOME OF THE STORIES ARE UNDOUBTEDLY REPLAYS, IN SOME INSTANCES GARBLED, OF

ACCOUNTS BROUGHT BACK BY HONG KONG PERSONAGES FROM RECENT MEETINGS WITH PRC LEADERS.

8. (C) COMMENT. WE SEE NO RELIABLE EVIDENCE THAT EITHER LONDON OR BEIJING HAS YET DECIDED ON ITS EXACT TALKING POINTS, MUCH LESS BEGUN TO MAKE THEM PUBLIC. THIS WEEK'S INCIPIENT PANIC IN ITSELF MIGHT WELL INFLUENCE THE POSITIONS OF BOTH PARTIES. ONE POSSIBILITY IS THAT BEIJING'S AWARENESS OF THE EVIDENT FRAGILITY HERE MIGHT PROMPT IT TO A SOFTER POSITION ON HONG KONG. THE BRITISH NOW PROBABLY FEEL MORE URGENCY IN GETTING SOMETHING POSITIVE ON HONG KONG OUT OF THE THATCHER VISIT. PARADOXICALLY, THE BRITISH MAY SEE THE PRESENT JITTERS IN HONG KONG AS USEFUL TO THEIR LONG-TERM INTERESTS. SOME HERE ARE EVEN SPECULATING THAT THE BRITS ARE MACHIAVELLIAN ENOUGH TO STIR THEM UP. WE KIND OF DOUBT THIS. LEVIN

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E.O. 12356: DECL: 8/12/88
TAGS: ECON, EFIN, CH, HK, UK
SUBJECT: HONG KONG GETS THE JITTERS

REFS: A) HONG KONG 9280, B) HONG KONG 12580

(C) SUMMARY AND INTRODUCTION: HONG KONG HAS A CASE OF THE JITTERS WHICH MAY LAST FOR SOME TIME. THE HONG KONG DOLLAR SLID TO A LOW OF H.K. DOLS 6.183 EQUALS U.S. ONE DOLLAR ON AUGUST 11, BEFORE MAKING A SLIGHT RECOVERY TO H.K. DOLS 6.135 AT THE MARKET'S CLOSE, AFTER REPORTED GOVERNMENT INTERVENTION. THE STOCK MARKET PLUNGED 100 POINTS ON AUGUST 12, BRINGING IT TO A TWO-YEAR LOW. WE WOULD TRACE THE JITTERS INITIALLY TO BASICALLY ECONOMIC FACTORS, NOW ACCENTUATED BY CONCERN OVER HONG KONG'S FUTURE. AS ONE ANALYST SAID, EVERYTHING SEEMS TO BE GOING WRONG AT THE SAME TIME. ON THE ECONOMIC SIDE, THE U.S. DOLLAR IS EXTREMELY STRONG, THE INTEREST RATE DIFFERENTIAL BETWEEN U.S. AND U.K. RATES FAVORS AN OUTFLOW OF H.K. DOLLARS, THE INTERBANK SYSTEM HERE IS AWASH WITH FUNDS FROM A RECENT LAND DEAL, HONG KONG'S TRADE FIGURES SHOW NO REAL GROWTH IN THE FIRST HALF OF 1982, HONG KONG'S ECONOMIC GROWTH RATE HAS SLOWED, THE EEC IS DEMANDING STEEP CUTS IN HONG KONG'S TEXTILE EXPORTS TO THE COMMUNITY AND THE ECONOMIC OUTLOOK IS POOR FOR HONG KONG'S MAJOR TRADING PARTNERS. ON THE POLITICAL SIDE, PRESS ARTICLES REPORT THAT CHINA'S TERMS ON THE 1997 ISSUE APPEAR TO BE HARDENING. RECENT ARTICLES REFER TO A LOCAL CHINESE GOVERNOR AND THE CHINESE FLAG FLYING OVER HONG KONG. CONFIDENCE, HONG KONG'S MOST PRECIOUS BUT INVISIBLE COMMODITY, IS BEING UNDERMINED. THE LOCAL ADVERSE REACTION TO THE RECENT TIN SHUI WAI AND BANK OF CHINA LAND DEALS EXEMPLIFIES THIS NERVOUSNESS. THE DEPUTY POLITICAL ADVISOR BELIEVES THE WEAK HONG KONG DOLLAR AND PLUNGING STOCK MARKET REFLECTED LOCAL AND INTERNATIONAL ECONOMIC FACTORS. NOW PEOPLE ARE ATTRIBUTING THE FALL TO UNCERTAINTY OVER HONG KONG'S FUTURE. HE SEES THIS PUTTING INCREASED PRESSURE ON BRITAIN (AND IMPLICITLY CHINA) TO DO SOMETHING. END SUMMARY.

1. (U) THE HONG KONG DOLLAR HAS RECENTLY DEPRECIATED AGAINST THE U.S. DOLLAR IN PART DUE TO THE U.S. DOLLARS RECENT STRENGTH. IT SLID FROM H.K. DOLS 5.908 EQUALS U.S. ONE DOLLAR ON JULY 26 TO A LOW OF H.K. DOLS 6.183 ON AUGUST 11, BEFORE RECOVERING TO CLOSE AT H.K. DOLS 6.135 REFLECTING REPORTED GOVERNMENT INTERVENTION IN BOTH THE FOREIGN EXCHANGE AND INTERBANK MARKETS. THE EFFECTIVE EXCHANGE RATE INDEX STOOD AT 88.3 (BASE YEAR 1971 EQUALS 100) ON AUGUST 11 DOWN FROM 88.8 ON JULY 26. THE ONE PERCENTAGE POINT INTEREST RATE DIFFERENTIAL BETWEEN THE HONG KONG PRIME RATE OF 14 PERCENT AND THE U.S. 15 PERCENT PRIME HAS SLIGHTLY WEAKENED THE HONG KONG

DOLLAR. THE HONG KONG INTERBANK MARKET MAY BEEN AWASH WITH HONG KONG DOLLARS SINCE JULY 80 WHEN THE DEVELOPER OF THE TIN SHUI WAI PROJECT DEPOSITED THE H.K. DOLS 1.46 BILLION SUM IT RECEIVED FROM THE SALE OF PART OF THE SITE TO THE HONG KONG GOVERNMENT (HKG) IN THE SHORT-TERM INTERBANK MARKET. THE MONEY FLOODED INTO AN ALREADY-LIQUID HONG KONG DOLLAR MARKET TO TEMPORARILY DRIVE DOWN THE OVERNIGHT INTERBANK RATE TO 3 PERCENT. THE OVERNIGHT RATE HAS SINCE REBOUNDED WITH GOVERNMENT INTERVENTION TO 9.25 PERCENT. A FURTHER WEAKNESS OF THE HONG KONG DOLLAR WILL BE REGISTERED IF PEOPLE CONTINUE TO GET OUT OF THE HONG KONG DOLLAR - AND INTO THE U.S. DOLLAR.

2. (C) PEOPLE ARE GETTING OUT OF THE STOCK MARKET. THE WEAKNESS OF THE HONG KONG DOLLAR AND THE ECONOMY IN GENERAL, APPREHENSION OVER HONG KONG'S FUTURE, AND THE CONFUSION AND DISAPPOINTMENT SURROUNDING THE GOVERNMENT'S LATEST "FRIENDSHIP" LAND SALE TO THE BANK OF CHINA (BOC) CAUSED THE LOCAL HANG SENG STOCK MARKET INDEX TO PLUMMET MORE THAN 100 POINTS ON AUGUST 12, TO BELOW 1000, THE LOWEST LEVEL IN MORE THAN TWO YEARS. THE HONG KONG STOCK MARKET WHICH TRADES IN MANY PROPERTY COMPANY STOCKS CLOSELY REFLECTS THE LOCAL PROPERTY MARKET. WITH THE EXCEPTION OF THE CENTRAL FINANCIAL DISTRICT WHERE PRICES HAVE BEEN SUSTAINED, HONG KONG'S PROPERTY PRICES IN GENERAL HAVE PLUNGED ABOUT 30 PERCENT OR MORE FROM 1981 PEAKS. SOME SECURITIES ANALYSTS SAY THE HANG SENG INDEX COULD EASILY FALL ANOTHER 200 POINTS. A PROMINENT LOCAL BUSINESSMAN SAID THE INDEX COULD FALL EVEN LOWER TO 700. THE HONG KONG STOCK MARKET IS NOTORIOUSLY VOLATILE.

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THIS IS NOT THE FIRST TIME THERE HAS BEEN A SEVERE SLUMP IN HONG KONG STOCKS, APPARENTLY TRIGGERED BY EXTERNAL PRESSURES. HOWEVER, THESE SLUMPS DON'T NORMALLY CONTINUE WITHOUT INSTITUTIONAL PRESSURES. FORTUNES HAVE BEEN MADE IN PREVIOUS MANIPULATIONS BY FIGURES SUCH AS FUNG KING HEY AND OTHER STALWARTS OF TODAY'S HONG KONG. THE LOSERS ARE USUALLY THE SMALL INVESTORS WHO PANIC AND SELL TO THE BIG GUYS AT THE BOTTOM OF THE MARKET. WE EXPECT THAT THIS ONE MAY BE NO DIFFERENT.

3. (C) IN TWO RECENT LAND SALES, THE HKG WAS SEEN LOCALLY AS GIVING THE CHINESE OVERLY GENEROUS TERMS- I.E. GOVERNMENT CAPITULATION TO CHINA. THE HKG, ONE NEWSPAPER EDITORIAL SAID, VIOLATED THE FIRST ECONOMIC COMMANDMENT: "THOU SHALL PAY ACCORDING TO THE MARKET RATE." THE DETAILS OF THE TIN SHUI WAI MIGHTY CITY AND BOC SALES HAVE BEEN REPORTED IN HONG KONG 9280 AND HONG KONG 12580, RESPECTIVELY. WHILE THE HKG OFFICIALLY STATES THAT THE BOC SALES WHICH HELPED SET THE STOCK MARKET PLUMMETING REFLECTED THE FULL MARKET VALUE OF THE SITE, HONG KONG'S DEPUTY POLITICAL ADVISOR PRIVATELY ADMITS CHINA GOT A BARGAIN. HE DESCRIBED THE DEAL AS POLITICAL. THE 13 YEAR LOAN TERMS, WHICH WERE HIGHLY CRITICIZED HERE, WERE AT CHINA'S INSISTANCE. THE HKG ALSO CAME UNDER CRITICISM FOR THE POOR TIMING OF THE ANNOUNCEMENT. ACCORDING TO THE DEPUTY POLITICAL ADVISOR, CHINESE AUTHORITIES FIRST RELEASED THE NEWS OF THE SALE WITHOUT CONSULTING WITH THE HKG. THE GOVERNMENT HERE HAD HOPED THE SALE WOULD FOSTER CONFIDENCE BY DEMONSTRATING CHINA'S CONTINUED COMMITMENT TO HONG KONG. INSTEAD THE ALREADY SHAKY MARKET NOSE DIVED. FINANCIAL SECRETARY BREMIDGE PRIVATELY EXPRESSED HIS FRUSTRATION WITH THE MARKET'S REACTION, PROCLAIMING "THEY ARE ALL LUNATICS. THIS NEWS WAS SUPPOSED TO CHEER THEM UP."

4. (C) THE JITTERS NOW PREVALENT IN HONG KONG CAN BE TRACED TO BOTH ECONOMIC AND POLITICAL FACTORS. THE INITIAL NERVOUSNESS, WE BELIEVE, COULD LARGELY BE TRACED TO ECONOMIC FACTORS AFFECTING THE ALREADY WEAKENED HONG KONG ECONOMY. HOWEVER, WITH TIME, THE ECONOMIC ISSUES WERE ACCENTUATED BY POLITICAL UNCERTAINTY OVER THE 1997 LEASE ISSUE. AS A HONG KONG AND CHANGHAI BANK SOURCE COMMENTED TO ECOHOFF, EVERYTHING STARTED GOING WRONG AT ONCE. IT'S AS IF AN ALREADY SICK MAN (HONG KONG'S ECONOMY) WERE EXPOSED TO TORRENTIAL RAINS, STRONG WINDS, AND LANDSLIDES.

5. (C) AMONG THE ECONOMIC FACTORS, WE WOULD LIST:

--THE STRONG U.S. DOLLAR.

--THE INTEREST RATE DIFFERENTIAL BETWEEN THE U.S. AND HONG KONG PRIME RATES.

--THE EXCESS LIQUIDITY IN THE HONG KONG INTERBANK MARKET.

--THE HONG KONG ECONOMY'S POOR TRADE PERFORMANCE IN THE FIRST HALF OF 1982 WITH NO REAL GROWTH IN DOMESTIC EXPORTS.

--THE DOWNWARD REVISION OF THE PROJECTED REAL GROSS DOMESTIC PRODUCT FOR THE HONG KONG ECONOMY IN 1982 FROM 8 TO 6 PERCENT OR LESS.

--THE POOR PERFORMANCE OF THE PROPERTY MARKET.

--THE STYMIED TEXTILE NEGOTIATIONS WITH THE EEC, WITH THE EUROPEANS DEMANDING 12 PERCENT CUTBACKS FOR CERTAIN ITEMS.

--THE POOR ECONOMIC OUTLOOK FOR HONG KONG'S MAJOR TRADING PARTNERS.

6. (C) TO THESE ADVERSE ECONOMIC FACTORS, WE MUST ADD THE POLITICAL OVERLAY OF INCREASED LOCAL NERVOUSNESS OVER THE 1997 LEASE ISSUE. FOR SOME TIME, THE BRITISH GOVERNMENT AND PROMINENT LOCAL HONG KONG CHINESE BUSINESSMEN HAVE URGED THE PRC TO LOOK AT THIS ISSUE. TODAY, SOME MAY QUESTION THE WISDOM OF THEIR URGINGS. ALMOST EVERYDAY THE LOCAL PRESS PRESENTS ONE CONFIDENCE ERODING ARTICLE AFTER ANOTHER ON THE PRC'S SUPPOSED INTENTIONS TOWARDS HONG KONG. LOCAL INVESTORS ARE EXPOSED TO HEADLINES

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MUST GET A MOVE ON 1997. IF, AS ASSUMED, THE PRC BELIEVES IT HAS AN IMPORTANT ECONOMIC STAKE IN HONG KONG'S STABILITY, IT TOO WILL HAVE TO MOVE. FOR EXAMPLE, FURTHER DEPRECIATION OF THE HONG KONG DOLLAR WILL ERODE CHINA'S FOREIGN EXCHANGING EARNINGS--ABOUT 40 PERCENT OF WHICH CAME FROM HONG KONG.
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LIKE "BEIJING PREPARING FOR THE TAKE-OVER: CHINA LEAKING LEASE PLANS." THE CHINESE TERMS SO REPORTED BY THE PRESS ARE MUCH TOUGHER THAN THE LOCAL POPULATION HAD EXPECTED. ASSORTED ARTICLES TALK OF CHINA'S RECOVERING OR PRESERVING ITS SOVEREIGNTY OVER HONG KONG IN 1997 OR BEFORE, A LOCAL CHINESE GOVERNOR APPOINTED BY BEIJING, A CHINESE FLAG FLYING OVER HONG KONG, AND HONG KONG'S INCORPORATION AS A SPECIAL AUTONOMOUS REGION OF CHINA UNDER ARTICLE 30 OF THE NEW CHINESE CONSTITUTION. IN ADDITION, GOVERNOR YOUDE'S ANNOUNCEMENT ON HIS RETURN FROM CONSULTATIONS IN LONDON THAT HONG KONG'S FUTURE MUST BE SEEN AS A "STEP-BY-STEP" PROCESS FURTHER DIMMED ANY LOCAL HOPES OF AN AMICABLE, QUICK ARRANGEMENT.

7. (C) DESPITE PRESS REPORTS, THE DEPUTY POLITICAL ADVISOR (POLAD) DENIES THAT PRC OFFICIALS HAVE DECIDED UPON ANY ONE GAME PLAN FOR HONG KONG. HE SEES VARIOUS ASSESSMENTS EMANATING FROM CHINA'S TOP LEADERS. PRC OFFICIALS, HE MAINTAINS, HAVE DEFINITELY DISCARDED ANY IDEA OF RENEWING THE LEASE. ACCORDING TO POLAD, CHINA'S TWO MAIN STATE OBJECTIVES -- TO PRESERVE SOVEREIGNTY OVER HONG KONG AND TO MAINTAIN HONG KONG'S PROSPERITY -- MAY BE CONTRADICTORY. PRIME MINISTER THATCHER, FOR HER PART, WILL NOT CONCEDE TITULAR SOVEREIGNTY TO CHINA WITHOUT GETTING AGREEMENT ON CONTINUED BRITISH ADMINISTRATION IN RETURN. ANY PRC/UK AGREEMENT ON HONG KONG WOULD HAVE TO BE COINED IN THE VAGUEST POSSIBLE TERMS, YET THESE TERMS MUST BE DEFINITIVE ENOUGH TO ALLOW BRITISH LAWYERS TO LIFT THE 1997 TIME BARRIER. THE UK, HE MAINTAINED, CAN NOT EXPECT THE CHINESE TO CONNIVE TO HELP BRITAIN LIFT THE 1997 BARRIERS. WHILE BRITISH ADMINISTRATION MUST CONTINUE, IT DOES NOT HAVE TO BE FEATURED IN A PUBLIC DECLARATION. THE POLITICAL ADVISOR'S OFFICE IS UNABLE TO LEAP INTO THE FRAY TO TRY TO CALM THE HONG KONG POPULACE. LONDON HAS IMPOSED STRICT GUIDELINES TO REFRAIN FROM PUBLIC DISCUSSIONS ON 1997 AND THE GOVERNOR'S RECENT CONSULTATIONS. POLAD EXPRESSED FEARS THAT THE NERVOUSNESS IN HONG KONG SEEN IN THE SLIDING DOLLAR AND DECLINING STOCK MARKET INDEX, WHICH HE SEES AS ORIGINALLY CAUSED BY A CULMINATION OF FACTORS, IS NOW MORE AND MORE CENTERED IN UNCERTAINTY OVER HONG KONG'S FUTURE. SINCE THE POPULACE THINKS UNCERTAINTY WILL CONTINUE, THE STOCK MARKET MAY CONTINUE TO FALL. IT'S ALL TERRIBLY INBRED, HE COMPLAINED.

8. (C) WE WOULD PREDICT THAT HONG KONG IS IN FOR A SPELL OF THE JITTERS. HONG KONG CAN BE A SKITTISH, LEMMING-LIKE COMMUNITY WHERE THE HERD MENTALITY REIGNS. CONFIDENCE, HONG KONG'S MOST PRECIOUS BUT INVISIBLE COMMODITY, IS BEING UNDERMINED. THE QUESTION IS HOW LONG WILL IT LAST AND WILL IT INTENSIFY. BECAUSE OF THE PRESENT SHAKINESS, POLAD SAID THE UK GOVERNMENT

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EXDIS

MANILA PLEASE PASS TO SECRETARY LEHMAN

E. O. 12356: DECL: 8/16/97

TAGS: PEPR, PGOV, MILI, HK, CH, US

SUBJ: SECRETARY LEHMAN DISCUSSION WITH HONG KONG GOVERNOR

1. SUMMARY: IN A MEETING WITH SECRETARY LEHMAN, GOVERNOR YOUDE POURED COLD WATER ON THE CURRENT INTENSE SPECULATION HERE ON HONG KONG'S STATUS. HE WAS NOT AWARE OF ANY PRC DECISIONS ON THE ISSUE. BEIJING'S SHARED INTEREST IN HONG KONG'S CONTINUED PROSPERITY ENHANCED CHANCES OF WORKING OUT A MUTUALLY SATISFACTORY SOLUTION. IT WAS MOST UNLIKELY THAT ANYTHING DRAMATIC WOULD COME OUT OF THE THATCHER VISIT THIS SEPTEMBER, BUT THE PM WOULD BE UNDER THE GUN TO BRING BACK SOMETHING TO CALM JITTERY HONG KONG NERVES.

2. THE GOVERNOR BELIEVED THAT BEIJING WOULD WELCOME A STRENGTHENED U. S. NAVAL PRESENCE IN THE REGION AS A COUNTER TO THE SOVIET EFFORT TO COMPLETE CHINA'S ENCIRCLEMENT. HE SAW DENG AS A STRONG PROPONENT OF A CHINESE STRATEGIC RELATIONSHIP WITH THE U. S., ALTHOUGH WORRISOMELY IT IS NOT KNOWN WHETHER ANY OF DENG'S ASSOCIATES SHARE HIS STRATEGIC VISION.
END SUMMARY.

3. SECRETARY OF NAVY JOHN LEHMAN'S AUGUST 14 CALL ON GOVERNOR YOUDE FEATURED DISCUSSIONS OF HONG KONG'S STATUS, U. S. -PRC RELATIONS AND THE US NAVY REBUILDING PROGRAM. NOTWITHSTANDING HONG KONG'S PREVAILING JITTERS INDUCED BY A COMBINATION OF CONCERN OVER THE ECONOMY AND THE 1997 LEASE ISSUE, THE GOVERNOR WAS IN A RELAXED, UPBEAT MOOD. HE NOTED THAT FOR ALL THE TALK ABOUT A FALTERING ECONOMY, HONG KONG STILL EXPECTED TO REGISTER 5 PERCENT REAL GROWTH IN GNP THIS YEAR -- A REMARKABLE PERFORMANCE WHEN MEASURED AGAINST THE REST OF THE RECESSION-PLAGUED WORLD. HE POURED COLD WATER ON THE CURRENT INTENSE SPECULATION ON HONG KONG'S STATUS. IT WAS ALL UNFOUNDED. TO THE BEST OF HIS AND LONDON'S KNOWLEDGE, THE PRC HAD NOT FORMULATED ITS POSITION ON THE ISSUE. MOREOVER, BEIJING'S INTEREST

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IN HONG KONG'S CONTINUED PROSPERITY AND ITS REPEATED ASSURANCES ABOUT PRESERVING HONG KONG'S ROLE AS A FREE PORT AND TRADE AND FINANCIAL CENTER PROVIDED STRONG GROUNDS FOR WORKING OUT A MUTUALLY SATISFACTORY SOLUTION. THIS WOULD TAKE SOME TIME. BEIJING HAD OTHER, MORE PRESSING DOMESTIC AND FOREIGN POLICY PRIORITIES. IT WAS UNLIKELY THAT PM THATCHER'S SEPTEMBER VISIT TO THE PRC WOULD PRODUCE ANY MAJOR MOVEMENT ON HONG KONG. HOWEVER, GIVEN THE CURRENT MOOD HERE AND THE INTENSE FOCUS ON THE VISIT, THE PM WOULD HAVE TO BRING BACK SOMETHING CALMING FOR HONG KONG. HE WAS REASONABLY OPTIMISTIC BEIJING WOULD BE RESPONSIVE TO THIS NEED.

4. IN RESPONSE TO QUESTIONING, THE GOVERNOR THOUGHT THAT THE TAIWAN ISSUE WOULD IMPORTANTLY INFLUENCE THE PRC'S APPROACH TO HONG KONG. IT WOULD CUT TWO WAYS. ON THE PLUS SIDE, THE PRC WOULD BE INTENT ON SHOWING TAIWAN THAT A SETTLEMENT COULD BE 117CHED WHICH WOULD PRESERVE THE EXISTING LIFESTYLE. ON THE MINUS SIDE, THE PRC MIGHT BE STICKY ON SOVEREIGNTY AND RELATED SYMBOLS FOR FEAR OF SETTING AN UNFAVORABLE PRECEDENT FOR TAIWAN.

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EXDIS

MANILA PLEASE PASS TO SECRETARY LEHMAN

APPEARING TOUGH TOWARD THE U.S. CHINESE SUPPORT OF THE WEST EUROPEAN POSITION ON THE GAS PIPELINE WAS IN KEEPING WITH BEIJING'S LONGSTANDING ADVICE TO WEST EUROPEAN NATIONS TO SHOW MORE INDEPENDENCE FROM THE UNITED STATES, BUT WITHIN THE GENERAL FRAMEWORK OF U.S.-WEST EUROPEAN STRATEGIC COOPERATION. HE HAD BEEN ON THE RECEIVING END OF SUCH ADVICE MORE TIMES THAN HE CARED TO REMEMBER WHILE SERVING AS UK AMBASSADOR TO THE PRC. HE HOPED THAT THE U.S. WOULD NOT LET CHINESE CRITICISM GET UNDER ITS SKIN. HE WAS CONVINCED THAT DENG XIAOPING STRONGLY VALUED CHINA'S STRATEGIC RELATIONSHIP WITH THE U.S. DENG SHARED ZHOU AND MAO'S ABILITY TO THINK STRATEGICALLY. WORRISOMELY, IT IS NOT KNOWN WHETHER ANY OF DENG'S ASSOCIATES POSSESS THIS BROAD VISION AND UNDOUBTEDLY THERE WERE SOME WITHIN THE LEADERSHIP WHOSE ATTITUDES WERE SHAPED BY NARROW, NATIONALISTIC CONSIDERATIONS. THEY WERE PROBABLY CAUSING PROBLEMS FOR DENG, BUT IT WAS MOST DIFFICULT TO ESTIMATE THEIR STRENGTH OR EVEN TO BE SURE OF THEIR IDENTITY.

7. COMMENT: ALTHOUGH THE GOVERNOR HAS OBVIOUS REASONS FOR PUTTING THE BEST POSSIBLE FACE ON THE CURRENT SITUATION, HIS PRESENTATION CAME ACROSS AS FRANK AND UNCALCULATED.

8. THE GOVERNOR HAS MAINTAINED A LOW, ALMOST INVISIBLE PROFILE OVER THIS PAST UNSETTLED WEEK. THIS HAS PROVOKED SOME MURMURED CRITICISM ABOUT HIS FAILURE TO DEMONSTRATE STRONG LEADERSHIP TALENTS AT A TIME OF WIDESPREAD CONCERN. IN MOOD, APPEARANCE AND FROM WHAT HE SAID, THE GOVERNOR BETRAYED NOT THE SLIGHTEST SIGN OF WORRY OVER ANY IMAGE PROBLEM THAT MAY BE BREWING FOR HIM.

9. SECRETARY LEHMAN HAS NOT SEEN THIS MESSAGE.

LEVIN

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AUTHORIZATION OF THE EXECUTIVE SECRETARY

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E.O. 12356: DECL: OADR
TAGS: PEPR, HK, CH, UK
SUBJECT: HMG DEBATES FUTURE OF HONG KONG
REF: HONG KONG 13893

1. ~~CONFIDENTIAL~~ - ENTIRE TEXT

2. SUMMARY: THE BRITISH AREN'T SAYING MUCH ABOUT
WHAT THATCHER WILL TELL THE CHINESE ON HONG KONG.
THEY WORRY THAT LEAKS OF BRITISH PLANS COULD HARDEN THE
CHINESE POSITION AND PERHAPS BUILD UNREALISTIC
EXPECTATIONS IN HONG KONG. END SUMMARY

3. OUR FCO CONTACTS HAVE BEEN VERY CAUTIOUS IN DESCRIBING
BRITISH THINKING ON HONG KONG'S FUTURE; THE PICTURE WHICH
EMERGES IS THEREFORE SKETCHY AND SOMEWHAT CONFUSED.
WE HAVE BEEN TOLD BY VARIOUS SOURCES (1) THAT THERE
COULD BE NO QUESTION OF AN AGREEMENT EMERGING FROM
THATCHER'S TALKS, (2) THAT AN AGREEMENT MIGHT BE FORTH-
COMING, BUT THAT OPTIMISM NOW COULD RAISE HONG KONG
EXPECTATIONS AND LEAD TO PANIC LATER IF NOTHING IS
ACHIEVED, AND (3) THAT THERE IS A SERIOUS CHALLENGE
WITHIN HMG TO THE IDEA THAT BRITAIN SHOULD SEEK TO
CONTINUE IN HONG KONG AFTER 1997. THE ARGUMENT FOR
WITHDRAWAL IS THAT BRITAIN RECEIVES NO GOVERNMENT
REVENUES FROM HONG KONG; THAT ITS INVESTMENTS THERE ARE
NOT SIGNIFICANT; AND THAT UNLIKE THE CASE OF THE FALKLAND
ISLANDERS, THERE ARE NO RACIAL/ETHNIC TIES TO BIND BRITAIN
TO HONG KONG'S POPULATION. BALANCING THIS ARE THATCHER'S
OWN EXTREMELY STRONG FEELINGS TOWARD SOVEREIGNTY.

4. DESPITE CONFLICTING SIGNALS, IT APPEARS FROM OUR
DISCUSSIONS THAT THE FCO IS CONSIDERING THREE OPTIONS:

- 1. "MOST ATTRACTIVE" ACCORDING TO ONE FCO SOURCE:
 - 1. U.K. WOULD RECOGNIZE NOMINAL CHINESE SOVEREIGNTY OVER
ALL OF HONG KONG; CHINA WOULD GUARANTEE CONTINUATION
OF THE STATUS QUO -- I.E., CONTINUED BRITISH
ADMINISTRATION -- BEYOND 1997.
- 2. U.K. WOULD RECOGNIZE CHINESE SOVEREIGNTY; CHINA
WOULD LEASE HONG KONG TO U.K. FOR ANOTHER 50 YEARS.
FCO BELIEVE CHINA COULD NOT ACCEPT THIS PLAN.
- 3. AFTER 1997 HONG KONG WOULD GOVERN ITSELF UNDER
NOMINAL CHINESE SOVEREIGNTY WITH A GUARANTEED PRC
HANDS-OFF POLICY. FCO BELIEVE THIS COULD WORK, BUT

- ANNOUNCEMENT OF SUCH A PLAN NOW WOULD DESTROY
- INVESTOR CONFIDENCE IN THE NEAR TERM.

S. U.K. BOTTOM LINE: CONTINUED STABILITY AND PROSPERITY
ARE THE GOAL. ONE FCO OFFICIAL FORESEES THAT THATCHER
VISIT WILL SET THE STAGE FOR ONE TO THREE YEARS' OF
CONTINUED PRIVATE TALKS ON HONG KONG'S FUTURE, AS
REPORTED REFTEL, DURING WHICH CHINESE WOULD BE "EDUCATED"
INTO ACCEPTING A SOLUTION THAT WOULD SATISFY INVESTORS.
ANOTHER FCO OFFICIAL APPEARS TO BELIEVE THIS OUTCOME OF
THE TALKS WOULD NOT BE SUFFICIENT TO MAINTAIN INVESTOR
CONFIDENCE AND THAT MORE WILL BE REQUIRED. ALL INSIST
THAT NO FINAL POLICY RECOMMENDATION HAS YET BEEN PRESENTED
TO MRS. THATCHER. STREATOR
BT

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3 options

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LIMITED-OFFICIAL USE SECTION 01 OF 02 HONG KONG 13312

USICA FOR PGM/RC, VOA/NEWS/CA

E.O. 12356: NA
TAGS: PINT, PEPR, HK, UK, CH
SUBJECT: HONGKONGERS WANT STATUS QUO PRESERVED, SAYS POLL

REF: FBIS HK 130430, 130432, 130434, 130456, 130458

1. SUMMARY

A RECENT PUBLIC OPINION POLL FOUND THAT HONG KONG RESIDENTS, FACED WITH VARIOUS SCENARIOS FOR HONG KONG'S POLITICAL FUTURE, WOULD MOST LIKE TO SEE A CONTINUATION OF THE STATUS QUO, WHILE A MAJORITY CONSIDERED OUTRIGHT REVERSION TO THE PRC THE LEAST DESIRABLE ALTERNATIVE. IF THE LATTER WERE TO HAPPEN, 22 PERCENT OF THE RESPONDENTS SAID THEY WOULD SEEK TO LEAVE HONG KONG "BY EVERY MEANS." HOWEVER, THESE PROSPECTS ARE STILL DISTANT FOR MOST HONG KONGERS; A LARGE MAJORITY SAID THAT UNCERTAINTY OVER HONG KONG'S FUTURE WAS NOT HAVING ANY EFFECT ON THEIR OWN LIVES AT PRESENT. END SUMMARY.

2. ON AUGUST 12 THE HONG KONG OBSERVERS, AN INDEPENDENT PUBLIC INTEREST GROUP, PUBLISHED THE RESULTS OF A DETAILED PUBLIC OPINION POLL THEY HAD COMMISSIONED ON HONG KONG RESIDENTS' ATTITUDES TOWARD THEIR PRESENT AND FUTURE LIFE IN THE COMMUNITY (REFTELS). THE SURVEY, WHICH COST HK\$ 64,000, WAS CONDUCTED BY SURVEY RESEARCH HONG KONG LTD. SURVEY RESEARCH INTERVIEWED 1,000 RESIDENTS BETWEEN THE AGES OF 15 AND 60, CHOSEN AT RANDOM FROM SAMPLING FRAMES INTENDED TO REFLECT THE GEOGRAPHIC AND SOCIAL COMPOSITION OF HONG KONG'S POPULATION. THE INTERVIEWS WERE CONDUCTED BETWEEN MAY 10 AND JUNE 11. THE 1997 ISSUE AND HONG KONG'S POLITICAL FUTURE WAS ONLY ONE OF THE SUBJECTS COVERED, THOUGH THE RESULTS IN THIS AREA ATTRACTED THE GREATEST LOCAL ATTENTION WHEN THE SURVEY WAS MADE PUBLIC. RESPONDENTS WERE ALSO POLLED ON THEIR VIEWS ON LOCAL GOVERNMENT, THE QUALITY OF LIFE, AND WHAT IS IMPORTANT TO THEM IN LIFE.

3. COMMENT

SURVEY RESEARCH IS A PROMINENT, WELL-REGARDED LOCAL MARKET RESEARCH FIRM, AND WE HAVE NO REASON TO DOUBT THE VALIDITY OF ITS METHODOLOGY. THE HONG KONG OBSERVERS IS A GROUP OF MOSTLY WESTERN EDUCATED CHINESE WHICH IS DEDICATED TO WINNING A LARGER ROLE FOR THE PEOPLE OF HONG KONG IN GOVERNMENTAL DECISION-MAKING. END COMMENT.

4. THE SURVEY SOLICITED RESPONSES TO FIVE ALTERNATIVE FUTURES FOR HONG KONG: THE STATUS QUO, BRITISH ADMINISTRATION UNDER CHINESE SOVEREIGNTY, A SPECIAL ECONOMIC ZONE OF CHINA, INDEPENDENCE, AND SIMPLY "RETURN TO CHINA." NINETY FIVE PERCENT CONSIDERED THE STATUS QUO ACCEPTABLE; BRITISH RULE WITH CHINESE SOVEREIGNTY WAS ACCEPTABLE TO 64 PERCENT OF THE RESPONDENTS; 42 PERCENT WOULD ACCEPT A SPECIAL ECONOMIC ZONE ARRANGEMENT; 37 PERCENT BELIEVED INDEPENDENCE WAS ACCEPTABLE AND 26 PERCENT FOUND RETURNING HONG KONG TO CHINA ACCEPTABLE. ASKED WHICH ALTERNATIVES THEY MOST AND LEAST PREFERRED, THE STATUS QUO WAS THE CLEAR FAVORITE, MOST DESIRED BY 69 PERCENT, WHILE RETURN TO CHINA WAS THE UNEQUIVOCAL LOSER, LEAST DESIRED BY 55 PERCENT.

5. INTERESTINGLY, WHILE 89 PERCENT OF THE RESPONDENTS CONSIDERED HONG KONG THEIR HOME, 43 PERCENT SAID THEY WOULD EMIGRATE IF THE CHANCE WAS PROVIDED. THAT PERCENTAGE ROSE TO 53 IF HONG KONG WERE RETURNED TO CHINA. MORE OMINOUSLY, 22 PERCENT OF ALL RESPONDENTS SAID THEY "WOULD TRY EVERY MEANS" TO GET OUT IF HONG KONG WERE RETURNED TO THE PRC.

6. THOUGH THE PEOPLE'S WILL SEEMED FAIRLY CLEAR FROM THE SURVEY, THE INTENSITY OF THEIR FEELINGS IS OPEN TO SOME DOUBT. ASKED HOW OFTEN THEY DISCUSSED HONG KONG'S FUTURE, 53 PERCENT SAID NEVER, 28 PERCENT SELDOM AND ONLY 19 PERCENT OFTEN. ASKED IF UNCERTAINTY WAS AFFECTING THEIR OWN LIVES, 84 PERCENT SAID NO.

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ACTION EA-12

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COMMENT.

THESE ATTITUDES, RECORDED IN MAY-JUNE, MAY HAVE ALTERED
SOMEWHAT IN THE CURRENT JITTERY MOOD, BUT THERE ARE STILL
MANY PEOPLE WHO SAY THEY ARE NOT WORRYING ABOUT THE 1997
ISSUE. SOME SAY THAT DATE IS STILL TOO FAR AWAY, AND
TOO MANY UNFORESEEN THINGS CAN HAPPEN IN THE MEANTIME.
FATALISM IS ALSO FED BY A SENSE OF POWERLESSNESS.
WHILE 95 PERCENT OF THOSE POLLED AGREED THAT THE PEOPLE
OF HONG KONG SHOULD PLAY A ROLE IN DECIDING ITS FUTURE,
ONLY 38 PERCENT THOUGHT THEY WOULD HAVE A CHANCE TO DO SO.

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E.O. 12356: DECL: 8/19/88
TAGS: ECON, EFIN, PEPR, HK, CH, UK
SUBJECT: HONG KONG CALMS DOWN AT LEAST TEMPORARILY

REF: (A) HONG KONG 13029, (B) HONG KONG 13030

1. (U) HONG KONG'S CASE OF THE JITTERS, REPORTED IN REFTELS, SUBSIDED THIS WEEK, AT LEAST TEMPORARILY. HONG KONG INVESTORS' SPIRITS WERE LIFTED WITH THE HOPE THAT LOWER U.S. INTEREST RATES WOULD FINALLY LESSEN THE RECESSION EXPERIENCED BY HONG KONG'S MAJOR TRADING PARTNERS. THE MOOD WAS UP IN ALL MARKETS--STOCKS, FOREIGN EXCHANGE, AND GOLD. PROPELLED BY THE NEW YORK STOCK MARKET'S RECORD GAINS, THE HONG KONG MARKET RALLIED FOR THE FIRST TIME IN MORE THAN TWO WEEKS, TO CLOSE AUGUST 18 62.37 POINTS HIGHER AT 1041.03. AT NOON AUGUST 19, IT STOOD AT 1054.25. THE HONG KONG DOLLAR STRENGTHENED SLIGHTLY TO DOLS HK6.045 EQUALS U.S. ONE DOLLAR ON AUGUST 19 REFLECTING IN PART THE U.S. DOLLAR'S WEAKNESS. THE EFFECTIVE EXCHANGE RATE INDEX FIRMED CORRESPONDINGLY TO CLOSE AUGUST 18 AT 88.3 (BASE YEAR 1971 EQUALS 100). THE DECISION BY SOME MAJOR U.S. BANKS TO DROP THEIR PRIME RATE TO 14 PERCENT MEANS THE DIFFERENTIAL BETWEEN THE U.S. AND HONG KONG PRIME RATE HAS BEEN CLOSED, SINCE THE HONG KONG RATE ALSO STANDS AT 14 PERCENT. THE OUTFLOW OF FUNDS CAUSED BY THE INTEREST RATE DIFFERENTIAL HAS STOPPED.

2. (U) RECENT PRESS ARTICLES HAVE CRITICIZED THE HONG KONG GOVERNMENT'S CLUMSY HANDLING OF ITS COMMENTS ON THE LAND SALE TO THE BANK OF CHINA. PEOPLE HERE NOW SEEM TO REALIZE THAT THE BANK OF CHINA IS INDEED INVESTING SUBSTANTIAL FUNDS IN HONG KONG--SOME HK ONE BILLION DOLLARS FOR THE LAND AND AN ADDITIONAL HONG KONG ONE BILLION DOLLARS FOR CONSTRUCTION COSTS. TREVOR BEDFORD, CHAIRMAN OF HONG KONG LAND (A MAJOR PROPERTY FIRM) HELPED RESTORE CALM, SAYING IT WAS OBVIOUS THE BANK OF CHINA DEAL WAS A POLITICAL ONE AND MERITED SPECIAL CONCESSIONS.

3. (C) WHILE THE ECONOMIC SCENE HAS IMPROVED SOMEWHAT, LITTLE HAS HAPPENED ON THE POLITICAL FRONT EITHER TO BOLSTER OR TO WEAKEN FURTHER INVESTORS' CONFIDENCE. THE STORY CONTINUES TO CIRCULATE IN THE LOCAL PRESS OF A "CHINESE PLAN" TO REPLACE HONG KONG'S BRITISH FLAG AND GOVERNOR. HOWEVER, CONOFF HAS LEARNED THAT THE SOURCE OF ONE ACCOUNT OF THE "PLAN" (REFTEL A) SEEMS TO BE BACKING OFF FROM HIS ORIGINAL LINE. THIS PERSON (A MEMBER OF A UNITED FRONT ORGANIZATION, NOT OF MCNA AS REPORTED REFTEL) TOLD AN AMERICAN ACADEMIC IN LATE JULY ABOUT "THE PLAN," GIVING THE IMPRESSION THAT IT WAS BASED ON FIRM INFORMATION ON A RECENT POLICY SHIFT. AFTER THE ACADEMIC'S STORY IN THE AUGUST 18 ASIAN WALL

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STREET JOURNAL CREATED A STIR, THE SOURCE TOLD ANOTHER PERSON THAT HIS KNOWLEDGE OF THE PLAN WAS BASED ONLY ON ACCOUNTS OF VARIOUS HONG KONG TRAVELLERS TO BEIJING. THE AUTHOR BELIEVES HIS SOURCE, ALARMED BY THE IMPACT HIS PLANTED STORY MADE AMID LAST WEEK'S NEAR-PANIC, IS TRYING TO DISTANCE HIMSELF FROM IT.

4. (C) COMMENT: THE RETURN OF RELATIVE CALM - IF NOT CONFIDENCE - TO THE HONG KONG MARKET IS THE RESULT OF INTERNATIONAL ECONOMIC EVENTS AND SOME REFLECTION ON LAST WEEKS EMOTION-CHARGED WAVE OF SELLING. NEVERTHELESS, THE UNDERLYING CAUSES - THE WEAKENED HONG KONG ECONOMY, THE INTERNATIONAL RECESSION, AND CONTINUED UNCERTAINTY OVER THE 1997 ISSUE - ALL REMAIN.

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E.O. 12356: DECL: 8/19/88
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SUBJECT: HONG KONG CALMS DOWN AT LEAST TEMPORARILY

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CHINA-FOREIGN RELATIONS-HONG KONG (7/1/82-8/24/82)

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B-4 Release would disclose trade secrets or confidential or financial information [(b)(4) of the FOIA]

B-6 Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA]

B-7 Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]

B-8 Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]

B-9 Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

C. Closed in accordance with restrictions contained in donor's deed of gift.