



Beijing's stealthy advance towards Greater China

BY DAVID LAGUE, GREG TORODE, JAMES POMFRET, YIMOU LEE, FAITH HUNG, CLARE BALDWIN, CLARE JIM AND FARAH MASTER

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The battle for Hong Kong's soul

BY GREG TORODE, JAMES POMFRET AND BENJAMIN KANG LIM

JULY 2 HONG KONG / BEIJING

Since Britain handed back colonial Hong Kong in 1997, retired primary school teacher and Falun Gong devotee Lau Wai-hing has fully exercised the freedoms China promised this city of 7.2 million.

Lau and fellow believers regularly staged protests to explain the teachings of their spiritual movement and draw attention to the persecution of followers on the mainland, where the sect is banned. Until about a year

ago, their protests were uneventful. That changed when a noisy rival group set up their placards and banners on the same pavement in the busy shopping area of Causeway Bay.

The 63-year-old Lau and her fellow protesters said they've been punched, shoved and sworn at since the newcomers from the "Care for the Youth Group Association Hong Kong" arrived with their blaring loudspeakers. Each protest is now a battle to be heard. "It is much more difficult now given these attacks, this external pressure, these forces from China," said Lau amid the amplified din on Sogo Corner, Hong Kong's neon-lit version of New York's Times Square.

For critics of the pro-Beijing government in Hong Kong, groups like the Care for the Youth Group Association are part of a campaign from the mainland to tighten control over China's most freewheeling city. Increasingly, they say, Beijing is raising its voice. In the streets, boardrooms, newsrooms, churches and local government offices, individuals and organisations with links to the state and China's Communist Party are playing a bigger role in civil and political life, well-placed sources in Hong Kong and Beijing say.

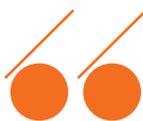
Whenever there are anti-government public protests, a pro-Beijing counter movement invariably appears. This year's 25th anniversary commemoration of the protests centred on Beijing's Tiananmen Square drew a rival demonstration to defend China's bloody crack-down on June 4, 1989.

Mainland officials based in Hong Kong now routinely seek to influence local media coverage.

Catholic priests in Hong Kong report that agents from China's security service have stepped up their monitoring of prominent clergy.

And, Beijing's official representative body, the Liaison Office of the Central People's Government in Hong Kong, now is able to shape policy in the office of city chief executive Leung Chun-ying, say two sources close to the city's leader.

Residents of this global financial centre could not help noticing a more overt sign of



In the past, the mainland compromised toward Hong Kong too much and was perceived to be weak.



China's rule in the former British colony: Huge Chinese characters spelling out "People's Liberation Army" in a blaze of neon alongside the military's waterfront headquarters that suddenly appeared at the beginning of June.

For Beijing's critics in Hong Kong, the 1997 handover is feeling more like a takeover.

"Blatant interference is increasing," says Anson Chan, who led Hong Kong's 160,000-strong civil service in the last years of British rule and continued in that role for several years after the handover.

Chan cited as examples pressures on Hong Kong companies not to advertise in pro-democratic newspapers, attempts to limit debate about democratic reform, and the higher profile increasingly being taken by Beijing's official representatives in the city.

"It's not another Chinese city and it shouldn't become one. Hong Kong is unique," said Chan.

XI'S TOUGHER LINE

In China's opaque political system, it is impossible to determine whether the party's growing clout in the territory is entirely the result of a campaign organised from on high, or partly the doing of mainland and local officials eager to please Beijing. Still, a tougher line on Hong Kong is coming from the top.

Despite promises that post-handover Hong Kong should enjoy a high degree of autonomy, China's President Xi Jinping, is said to have decided that Beijing has been too lenient.

"Xi Jinping has rectified (China's) policy for governing Hong Kong," a source close to the Chinese leader told Reuters in Beijing, requesting anonymity. "In the past, the mainland compromised toward Hong Kong too much and was perceived to be weak."

This tightening grip has fuelled resentment and sparked a civil disobedience movement called "Occupy Central", which threatens to blockade part of Hong Kong's main business district.

Mass protests can paralyse this high-density city. Business leaders have warned that Occupy could damage businesses: Four of the largest

multinational accounting firms placed advertisements in local newspapers warning against the movement, which has been branded illegal by Chinese authorities.

Occupy's primary aim is to pressure China into allowing a truly democratic election in 2017.

Beijing says Hong Kong can go ahead with a vote in 2017 for the city's top leader. But mainland officials stress that Hong Kong's mini-constitution, the Basic Law, specifies that only a nominating committee can pick leadership candidates. Pro-democracy activists demand changes that would allow the public to directly nominate candidates.

Nearly 800,000 people voted in an unofficial referendum that ended on Sunday, which called for Beijing to allow open nominations of candidates for the 2017 poll – a vote China's State Council, or cabinet, called "illegal and invalid", said the state Xinhua news agency.

Fears that the screws are tightening were heightened when Beijing published an unprecedented cabinet-level White Paper in June on Hong Kong. It bluntly reminded Hong Kong that China holds supreme authority over the city.

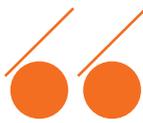
"The high degree of autonomy of (Hong Kong) is not an inherent power, but one that comes solely from the authorisation by the central leadership," it says.

The policy document took about a year to prepare and was approved by the 25-member, decision-making Communist Party Politburo around a month ago, a second source close to Xi told Reuters in Beijing.

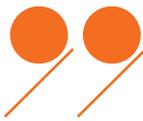
It's a tricky issue for China's new leadership. Hong Kong's democratic experiment is seen as a litmus test of Beijing's tolerance for eventual political reforms on the mainland, where calls for greater civil liberties and grassroots democracy have been growing, experts say.

President Xi, who has swiftly consolidated power in China since taking office by taking a hard line on domestic and foreign affairs, is unlikely to compromise on Hong Kong, the sources close to the leader said.

"Hong Kong is no different," the second source with ties to China's leadership said.



Pushing for democracy in Hong Kong is tantamount to asking the tiger for its skin.



“Pushing for democracy in Hong Kong is tantamount to asking the tiger for its skin.”

SHADOW CABINET

China’s Liaison Office in Hong Kong is housed in a skyscraper stacked with surveillance cameras, ringed by steel barricades and topped by a reinforced glass globe. Soaring above streets filled with dried fish shops and small traders, it is known in Cantonese slang as “Sai Wan”, a reference to the gritty western end of Hong Kong Island where it is located. Each day, hundreds of staff, mostly mainland Chinese, stream into the matte-grey building and its marble lobby with a large Chinese screen painting of pine trees.

Hong Kong is both part of China and outside of it as defined in the 1984 Joint Declaration, the treaty under which Britain handed over its former colony.

“One country, two systems” — conceived by China’s then-paramount leader Deng Xiaoping and British Prime Minister Margaret Thatcher — let Hong Kong keep its free-market economy and internationally-respected legal system, with the exception of foreign affairs and defence.

As China’s on-the-ground presence in Hong Kong, the Liaison Office’s formal role is described in China’s recent White Paper as helping to manage the Chinese government’s ties with the city, as well as “communication with personages from all sectors of Hong Kong society”.

Two high-level sources with close ties to Leung, the Hong Kong Chief Executive, say the Liaison Office does much more than that: It helps shape strategically significant government policies.

“The real cabinet is the shadow cabinet,” said one source close to Leung. “The chief executive’s office can’t do without the Liaison Office’s help on certain matters.”

The Chief Executive’s office did not directly respond to questions on the extent of its ties with the Liaison office. It said in an emailed response that China and Hong Kong shared a close relationship on multiple fronts, including

at “government- to-government level”. The office stressed Hong Kong’s autonomy and noted that the Basic Law says no Chinese government body may interfere in Hong Kong affairs.

China’s Liaison Office did not respond to faxes and phone calls seeking comment. The Hong Kong and Macau Affairs Office in Beijing, which has Cabinet-level authority over the territory from Beijing, did not respond to faxed questions.

The Liaison Office uses its broad networks, spanning grassroots associations, businessmen and politicians, to help the Hong Kong government push through policies needing approval from a largely pro-Beijing legislature. These have included the debate over democratic reforms in Hong Kong and a multi-billion-dollar high-speed rail link to China, one source said.

Liaison Office chiefs were once rarely seen. But the current director, Zhang Xiaoming, has taken on a far more public role since taking office 18 months ago - around the same time that Xi Jinping became China’s leader and Leung Chun-ying became chief executive in Hong Kong. Zhang has lunched with legislators and also attends society gatherings alongside local tycoons and business leaders. Zhang did not respond to requests for comment.

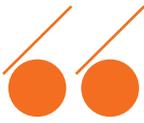
Liaison Office staff, including some from the propaganda department, regularly phone editors and senior journalists at Hong Kong media outlets.

Sometimes, these officials give what are known as “soft warnings” not to report sensitive topics, according to media sources and a report by the Hong Kong Journalists Association in 2013.

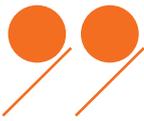
In one case, a television journalist was called by a Beijing official who mentioned an interview the journalist was planning. The journalist “learned that this was a warning meaning that he was ‘being watched’ and that he should not conduct sensitive interviews,” the report said.

COMMUNIST PENETRATION

Foreign diplomats and local academics believe



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the Liaison Office coordinates and implements the strategy of the Communist Party inside Hong Kong, although the hierarchy, membership and structure of the party in Hong Kong remain a secret.

Before the 1997 handover, the Chinese Communist Party focused on courting businessmen, academics and activists to secure influence and loyalty. It has now become more assertive, attempting to isolate party enemies, silence critics, and deliver votes, Hong Kong scholars and a source close to the Liaison Office say.

The vehicle for this strategy is a Beijing-based entity called the United Front Work Department, an organ of the Communist Party's Central Committee, whose mission is to propagate the goals of the Party across non-party elites.

The Liaison Office's Coordination and Social Group Liaison departments report directly to Beijing's United Front Work Department, according to a source in frequent touch with Liaison Office staff, who declined to be named.

"There is deeper penetration by the United Front in Hong Kong in recent years," said Sonny Lo, an academic and author of a book on China's underground control of Hong Kong. "In part, the United Front is working to counter and adapt to the rise of democratic populism and as a result we are seeing these new groups take to the streets.

"United Front groups are being more heavily mobilized to not just support government policy but to counter rival forces."

A legacy of the earliest days of Leninist communist revolutionary theory, the United Front Work Department's mission is to influence and ultimately control a range of non-party groups, luring some into cooperation and isolating and denouncing others, according to scholars of Communist history.

"The tactics and techniques of the United Front have been refined and perfected over the decades and we are seeing a very modern articulation of it in Hong Kong," says Frank Dikotter, a Hong Kong University historian and author of nine books on Chinese history.

The United Front - like the Communist Party itself - doesn't exist as a registered body in Hong Kong. There is no publicly available information about its network or structure. Neither the United Front Work Department in Beijing, nor the Liaison Office in Hong Kong, responded to questions from Reuters about the purported activities of the Front in Hong Kong.

But it is possible to trace links from some grassroots groups to mainland-owned businesses and the Liaison office.

A Reuters examination of the societies registration documents for the Care for the Youth Group Association obtained from Hong Kong police show that the group's chairman is Hung Wai-shing and the vice chairman is Lam Kwok-on.

Police and corporate filings also show Hung is a director of a New Territories clan association that researchers believe is a core part of China's United Front operations in the city's northern fringes close to the Chinese border.

Hung is also a director of several Hong Kong subsidiaries of Beijing Yanjing Brewery Co. Ltd, a state-owned Chinese brewery that stock exchange filings show is in turn majority owned by two investment vehicles ultimately tied to the Beijing city government.

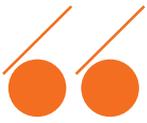
Reports in the *Ta Kung Pao* and *Wen Wei Po* newspapers in Hong Kong - both mouthpieces for Beijing - have described Hung socialising with Liaison Office officials in the New Territories.

Hung denied any connection to the youth association when Reuters visited him at his Yanjing Beer office in Hong Kong's Fanling district.

"What you refer to, the Care for the Youth association, I tell you I'm not involved," said Hung, a lean, middle-aged man with bushy eyebrows and thinning hair, who then called the police to complain about being questioned.

Youth care association Vice-chairman Lam is a regular at the anti-Falun Gong protests on Sogo corner. He ignored questions from Reuters about his role with the youth association at a recent demonstration.

Other street groups, including the one that



The visits of these agents, who travel into Hong Kong on short-term permits, have become more frequent and their tactics more assertive.



opposed Hong Kong’s Tiananmen commemoration, are run by individuals linked to a network of business chambers and associations in Hong Kong, including some that are at the vanguard of United Front work in the city, scholars say.

The chairman of one of those groups, the Voice of Loving Hong Kong, Patrick Ko, is shown in company filings to be a director of the Chinese General Chamber of Commerce, which the researcher Lo identified as an organisation under the United Front umbrella in Hong Kong.

Ko denied any ties to Beijing’s United Front Work Department. He said his group and the Chinese General Chamber of Commerce were “run by Hong Kong people”.

SECRET AGENTS

Behind the scenes, agents from Beijing’s powerful Ministry of State Security are also expanding China’s reach into Hong Kong, diplomats and members of various professions say.

The Ministry of State Security sits at the apex of China’s vast security apparatus, responsible for both domestic and external secret intelligence operations.

Professionals in Hong Kong have been invited, often discreetly through intermediaries, to “drink tea” with agents.

The visits of these agents, who travel into Hong Kong on short-term permits, have become more frequent and their tactics more assertive, say multiple sources who have had contacts with such agents.

Their targets include Hong Kong-based priests, journalists, lawyers, businessmen, academics and politicians.

Two sources told Reuters the agents offer gifts in exchange for information and favours.

“They said they have an unlimited budget” for gifts, said one Hong Kong-based professional in regular contact with agents.

Two priests said they received repeated visits from State Security agents after recent tensions between China and the Vatican

stemming from China’s moves to ordain bishops without the consent of the Holy See.

One priest recalled meeting a young and polite agent who “said he was a friend who wanted to help” while making it clear he was reporting to Beijing for State Security.

“It was clear he wanted secrets – gossip and views about (Hong Kong) relationships and trends and what might be going on at the Holy See,” said the priest who declined to be identified.

In recent months, the agents have been asking about the Catholic Church’s support for the Occupy Central movement, two priests said.

The Ministry of State Security did not answer calls to its main telephone number in Beijing; the government does not disclose other contact numbers for the ministry to foreign reporters.

While the battle for influence continues, there is no let up on Sogo Corner for Lau Wai-hing and her fellow Falun Gong devotees.

On a recent Saturday, not far from where Lau was standing, members of the Care for the Youth Group Association held a “wanted” poster carrying Lau’s photograph with the words “evil cult member” below it.

Lam, the group’s vice chairman, raised his portable loudspeaker rigged to a car battery. “Wipe out the evil cult Falun Gong,” he shouted, his voice reverberating down the busy street.

Lau, however, would not be deterred.

“People can see we only want to make ourselves heard. Hong Kong should give us that freedom.” 

Cover photograph by **Damir Sagolj**
 Additional reporting by **Yimou Lee**
 Editing by **David Lague and Bill Tarrant**



How China's shadowy agency is working to absorb Taiwan

BY YIMOU LEE AND FAITH HUNG

NOVEMBER 28 TAIPEI / HONG KONG

Ever since a civil war split the two sides more than 60 years ago, China has viewed Taiwan as a renegade province that needs to be absorbed into the mainland. To that end, the legion of Taiwanese businessmen working in China is a beachhead.

In June, hundreds of those businessmen gathered in a hotel ballroom in the southern Chinese city of Shenzhen. They were there to toast the new head of a local Taiwan merchants' association. They sipped baijiu liquor and ate

seafood as a troupe performed a traditional lion dance for good luck. An honored guest, senior Communist Party official Li Jiafan, stood to deliver congratulations and a message.

"I urge our Taiwanese friends to continue to work hard in your fields to contribute to the realisation of the Chinese dream as soon as possible," said Li, using a nationalist slogan President Xi Jinping has popularised. "The Chinese dream is also the dream of the people on both sides of the Taiwan Strait – our dream of reunification."

Li, who ended his speech to beating drums and loud applause, is a department chief in the Shenzhen arm of the United Front Work Department, an organ of the Communist Party's Central Committee. Its mission: to spread China's influence by ultimately gaining control over a range of groups not affiliated with the party and that are often outside the mainland.

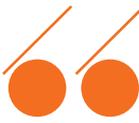
United Front documents reviewed by Reuters, including annual reports, instructional handbooks and internal newsletters, as well as interviews with Chinese and Taiwanese officials reveal the extent to which the agency is engaged in a concerted campaign to thwart any move toward greater independence by Taiwan and ultimately swallow up the self-ruled island of 23 million.

The United Front's 2013 annual work report for the Chinese province of Zhejiang, for instance, includes the number of Taiwanese living in the province, the number of businesses they run as well as an entry on background checks that have been conducted on the Taiwanese community in the province, an entrepreneurial hub near Shanghai.

The United Front hasn't confined itself to the mainland. It is targeting academics, students, war veterans, doctors and local leaders in Taiwan in an attempt to soften opposition to the Communist Party and ultimately build support for unification. The 2013 work report, reviewed by Reuters, includes details of a program to bring Taiwanese students and military veterans on visits to the mainland.

INFLUENCING POLITICS

Through the United Front and other Chinese



To attack the heart is the best. To attack a [walled] city is the worst.



state bodies like the Taiwan Affairs Office, which is responsible for implementing policies toward Taiwan on issues including trade and transport, Beijing has also tried to influence politics on the island, in part by helping mobilise Taiwanese businessmen on the mainland.

Many of them are heading back home this weekend to vote in mayoral elections that are being viewed as a barometer of support for Taiwan's ruling Nationalist Party, or Kuomintang (KMT), which favours closer ties with China than does the pro-independence Democratic Progressive Party (DPP). A large number of those businessmen, who a senior KMT source said will largely vote for the party, will be flying on deeply discounted airfares being offered by Chinese and Taiwanese airline companies.

"The goal is simple — peaceful unification," said a person with ties to the Chinese leadership in Beijing. Soft power, not armed force, is the strategy. "To attack the heart is the best. To attack a [walled] city is the worst," the source said, quoting Sun Tzu's "Art of War."

Questions sent by fax to the Beijing office of the United Front Work Department were not answered. The Chinese government's Taiwan Affairs Office referred Reuters to a statement on its website saying it does not comment on elections on "the island."

What's happening in Taiwan is part of a broader effort by Beijing to bolster its control over restive territories on its periphery.

The United Front has long been active in Hong Kong, which is ruled under the "one country, two systems" model that enshrines a wide range of personal freedoms for its residents and which China's leaders have proposed as a model for Taiwan. Reuters reported in July that United Front operations in Hong Kong had shifted from the backroom courting of academics and businessmen to the streets, where new groups of pro-Beijing agitators were attempting to silence critics of China.

"What the United Front is doing to Taiwan now is the same as what it has been doing in Hong Kong since the 1980s — a quiet, slow but extensive penetration," said Sonny Lo,

a professor at the Hong Kong Institute of Education and author of a book on China's covert control of the city.

Unlike Hong Kong, Taiwan is a fully democratic entity. It has an army but does not have membership in the United Nations, and China has refused to rule out the use of force to gain control of the island.

Since the KMT won the presidential election in 2008, cross-Strait ties have been warmer than ever. More than 20 trade deals, including the establishment of the first direct flights between Taiwan and the mainland, have been inked. No trade agreements were signed under the previous DPP-led administration. Earlier this year, Chinese and Taiwanese officials held their first official meeting since 1949.

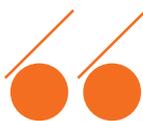
Taiwan's economy has become increasingly intertwined with China's. About 40 percent of Taiwan's exports are to China and some key sectors like technology have much of their manufacturing on the mainland. The world's biggest electronic components maker, Foxconn Technology Group, which assembles Apple Inc's iPhones, has many of its plants in China.

Taiwan presidential spokesperson Ma Weikuo said Taiwanese heading home to vote were exercising their right as citizens. "It is normal that Taiwanese businessmen living in Hong Kong, Macau, mainland China, Europe, Japan and other parts of the world want to return to Taiwan to vote," she said.

PRIZED HONOUR

The United Front's annual work reports and handbooks provide a window into the agency's methods. It has at least 100 offices in Zhejiang. The 2013 work report said 30,000 Taiwanese businesspeople and their families were living in the province and 6,800 Taiwanese enterprises had operations there at the end of 2012.

United Front officials reported creating a more friendly business environment by helping to smooth investment problems and resolve legal disputes for resident Taiwanese. In the Zhejiang city of Ningbo, one United Front office said it spent 110,000 yuan (about



There will be a force that helps protect your business on the mainland.



\$18,000) to buy life and traffic accident insurance for 137 Taiwanese businessmen.

Under a “three must visit” system in effect across the mainland, United Front officials are instructed to visit Taiwanese businesspeople and their families during traditional holidays, when a family member is ill and when someone is facing economic troubles.

“They help with our business as well as little problems in daily life such as car accidents, illness and schooling for kids,” said a Taiwanese man surnamed Lin, who works in the property sector in Changsha, the capital of Hunan Province.

One enticement China has dangled in front of the Taiwanese business community residing on the mainland, is provincial and municipal membership in the Chinese People’s Political Consultative Conference (CPPCC), which serves as an advisor to the government. It is a prized honour for businessmen whose livelihoods are directly dependent on the mainland. The position affords access to government officials and a form of protection in a country that lacks an independent judicial system.

“There will be a force that helps protect your business on the mainland,” said Lin. “They won’t make trouble if you are a CPPCC member.”

Holding CPPCC membership is a violation of Taiwanese law that bars citizens from taking positions in state or party bodies in China. It is, however, legal to be an honorary, non-voting CPPCC member. The Association of Taiwan Investment Enterprises on the Mainland (ATIEM), which lists some 130 Taiwanese business associations across China as members, met with Taiwanese President Ma Ying-jeou in December 2012 to try changing that.

Their bid to persuade him to allow Taiwanese citizens to become full-fledged CPPCC members ultimately failed. Taiwan’s Mainland Affairs Council announced that same month that Taiwanese could not sit on the CPPCC.

Earlier in 2012, Taiwan’s National Security Bureau had handed a list of 169 Taiwanese suspected of being CPPCC members to the

island’s Mainland Affairs Council, which implements policy toward China on a wide array of issues including business, shipping and travel. The council whittled the list down to 32. Ultimately, no one was punished after Taiwanese authorities determined those named were all either honorary CPPCC members or weren’t holders of a Taiwanese passport.

FAR-REACHING DEALS

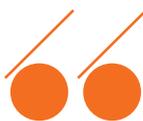
Taiwanese working on the mainland have actively lobbied for increased trade ties with China. ATIEM, the business lobby, lists some of Taiwan’s largest companies as members on its website. Several of the group’s founding members urged the Taiwanese government to sign far-reaching deals with China, arguing it would boost Taiwanese business on the mainland. They held meetings with Taiwan’s Mainland Affairs Council to help lay the groundwork, a senior member of the organization told Reuters.

Their efforts were rewarded when Taiwan signed trade deals in 2008 that for the first time allowed direct flights, shipping and mail links with the mainland.

ATIEM hasn’t always been on the winning side. In March, students occupied the Taiwan legislature in a bid to block passage of a deal that would have allowed for freer trade with China. The protests, dubbed the Sunflower Movement, fed off fears the pact would give China greater sway over Taiwan. The protest ended when parliament agreed to suspend a review of the bill.

ATIEM did not respond to questions sent by email.

Some Taiwanese officials warn against United Front encroachment. In late September, the head of Taiwan’s Overseas Community Affairs Council, which handles matters related to citizens living overseas, told a parliamentary committee that the United Front was stepping up work among Taiwanese business leaders and younger Taiwanese on the mainland and abroad.



China has some political intentions. But Taiwan has its own advantages in terms of systems, core values and soft power.



“They are drawing the Taiwanese who are more receptive to China over to their side, exerting pressure on Taiwan’s government and affecting its mainland policies,” Alexander Huang, a former vice chairman of Taiwan’s Mainland Affairs Council, which is responsible for ties with China, told Reuters. He didn’t cite specific examples.

Mainland Affairs Council spokesperson Wu Mei-hung said United Front activity shouldn’t be interpreted in an “overly negative way.”

“China has some political intentions,” she said. “But Taiwan has its own advantages in terms of systems, core values and soft power. All of these, we hope, will impact China via exchanges.”

The ruling KMT dismisses charges from the opposition DPP that it is benefitting from United Front activity. Kuei Hung-cheng, the KMT’s director of China affairs, acknowledged the close relationship between Taiwanese businessmen on the mainland and the Chinese authorities, but said that did not mean Beijing held sway over the party. “The KMT will not be influenced or controlled by the Chinese Communist Party. That is not possible,” he said.

A MAGIC TOOL

The United Front is a legacy of the earliest days of Leninist communist revolutionary theory. China’s version of the United Front, dubbed a “magic tool” on the agency’s own website, helped the Communist Party become established on the mainland and ultimately prevail in a civil war that forced Chiang Kai-shek’s Kuomintang (KMT) to retreat to Taiwan in 1949. The United Front has as its primary goal the promotion of “motherland unification” and blocking of “secession.”

A 2007 handbook for United Front workers in Beijing instructs cadres to “unite neutral forces in order to divide and attack enemies.” It also directs them to “make friends extensively and deeply with representatives from all sectors” in Taiwan and abroad to “form a mighty troop of patriots.”

A senior Taiwanese defence official, who did not want to be named, referred to the United Front’s tactics as a “war.” The ultimate goal was “to overturn the Republic of China,” he said, using Taiwan’s official name.

The front’s activities haven’t been confined to harnessing China-friendly forces. The southern Taiwanese city of Tainan, which is a bastion of the pro-independence DPP, has been singled out. One group in the city that has gotten special treatment is doctors, who have been invited on trips to the mainland, according to a 2011 work report from an organ associated with the United Front.

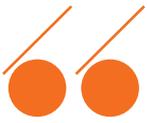
The visits had “successfully enhanced identification with the motherland among some pro-green Taiwanese,” the Taiwan Democratic Self-Government League, a nominally independent political group that is permitted to operate by the Communist Party, wrote in its report. Green is the color associated with the opposition DPP.

Some politicians in Taiwan unabashedly favor unification. Among them is Chang An-lo, the head of a pro-unification party. Known as the White Wolf, Chang was once a leader in a triad group, a traditional Chinese criminal syndicate, called the Bamboo Union. He lived for a decade in China as a fugitive from the law in Taiwan but ultimately was never tried. He also spent ten years behind bars in the U.S. on drug-smuggling charges.

Sitting in his office in Taipei dressed in a white jacket and black shirt, Chang says he and his party have regular contact with Beijing’s Taiwan Affairs Office and he has “friends in the United Front.” The Chinese government, he says, has provided all-expenses paid trips for members of his party to the mainland. “Getting carrots from China is better than getting sticks,” he says.

UNSPOKEN CONSENT

The United Front and the Taiwan Affairs Office are also deeply involved in an activity that in Communist China is strictly prohibited: democratic electoral politics.



There are 7 to 8 votes in my family. And am I not the one who decides to whom those votes go?



Taiwanese businessmen based in Shenzhen and Shanghai told Reuters they have been encouraged by United Front officials to head home to vote in past elections.

This year, the stakes are high for Beijing. The Democratic Progressive Party champions independence. The ruling KMT government backs a status quo position of “no unification, no independence, no war.”

Election airlifts helped the KMT to victory in 2008 and 2012. Close to a quarter million Taiwanese residents on the mainland headed home to vote in the 2012 presidential election, according to a senior member of the ruling party who estimates there are about one million Taiwanese working and living in China. As many as 80 percent voted for KMT leader Ma, who won a second term promising closer ties with Beijing, the official said, citing an internal survey.

This year, the airlift may not be enough to turn the tide in the most important mayoral run-off – in Taipei. Final opinion polls published by Taiwan’s leading media outlets showed the KMT’s candidate trailing an independent by 11.5 to 18 points. A victory for the independent would mark the first time in 16 years that the KMT has not ruled the capital.

But Beijing isn’t giving up. More than a dozen airlines, including state-owned Air China and Taiwan’s largest carrier China Airlines, have agreed to provide discounted flights from the mainland to Taiwan at the end of November, according to a notice sent to members by ATIEM. The Beijing-based organization lists the Chinese minister in charge of the Taiwan Affairs Office as an honorary chairman on its website.

A senior official at Taiwan’s China Airlines told Reuters that “with tickets selling at 50 percent off, airlines will incur losses.” But the carrier would nevertheless “100 percent meet the demand from Taiwanese businessmen.”

China Airlines spokesman Jeffrey Kuo said the company was offering “promotional tickets for all flights” because November was “the low season.” Air China did not respond to questions sent by fax and email to its Beijing office.

China’s Taiwan Affairs Office said it was aware that Taiwanese businessmen wanted to vote in the elections. ATIEM had negotiated with airline companies to allow them to fly home, it said.

He-tai Chen, president of the Taiwan Merchant Association in Shenzhen, said the Taiwanese business community on the mainland was “China’s best public relations tool.”

“There are 7 to 8 votes in my family,” he said. “And am I not the one who decides to whom those votes go?”

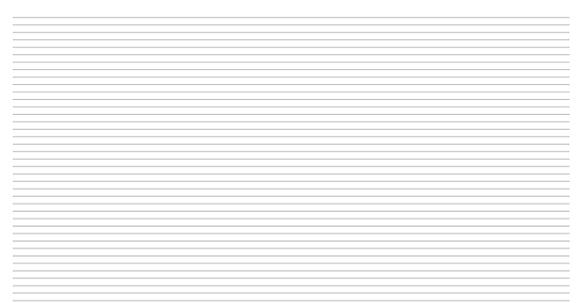
The United Front has also been working to penetrate other layers of Taiwanese society. As part of an operation called “Collecting Stars,” it has targeted military veterans in Taiwan, inviting them to China for visits. In May 2012, retired Taiwanese and mainland generals who were once sworn enemies met for an invitational golf tournament in Zhejiang, United Front documents show.

Outreach to students takes the form of summer camps, corporate internships and discover-your-roots tours to the mainland. Tsai Ting Yu, a 15-year-old junior high school student who joined a trip in 2013 and in 2014, said she attended classes with her mainland hosts and visited popular tourist sites, including the Great Wall and the Forbidden City.

“Before the trips, I kind of resisted the idea of China. But through the programs I got to know them better and that resistance gradually disappeared,” said Tsai.

She says she is now considering doing an undergraduate degree on the mainland. 

Additional reporting by Benjamin Kang Lim in Beijing and John Ruwitch in Shanghai
 Editing by Peter Hirschberg, Michael Williams and Bill Tarrant



How China spies on Hong Kong Democrats

BY DAVID LAGUE, GREG TORODE AND JAMES POMFRET

DECEMBER 15 HONG KONG

James To was growing uneasy. When the veteran Hong Kong Democratic Party lawmaker looked in his rear-view mirror, two silver Mercedes Benz saloons kept appearing behind his grey Volvo sedan.

For almost a week, one or the other was behind him on his daily commute. When he arrived at the Legislative Council building, the following car would park nearby and wait, sometimes for hours. With his suspicion hardening, on August 11 To complained to the

police, reporting the registration numbers of the two Mercedes in his detailed statement.

The next morning he pulled out of his home in the largely working class neighbourhood of North Point on Hong Kong island and headed to work. At the bottom of the street outside his building, he glanced in the mirror to see an unmarked car pull sharply into the path of a silver Mercedes behind him. Several men got out of the unmarked car. He kept driving, assuming the police had moved fast to intercept his tail.

He was right. Later, To says, the police informed him they had arrested two men and seized two Mercedes. What he didn't know was that the police had inadvertently foiled a surveillance operation being run by mainland China. Just ahead of the biggest pro-democracy protests in Hong Kong since the 1997 handover, the police had stumbled into a Chinese internal security operation aimed at monitoring the activities of pro-democracy figures in Hong Kong, according to two people with knowledge of the surveillance.

The mainland Chinese intelligence services have long been suspected of running covert operations in Hong Kong, but this has now been confirmed for the first time, Reuters has learned, with one of their surveillance teams taken into custody. The pair was part of a team watching To, according to the people familiar with the operation. Other teams have been assigned to track key figures in the pro-democracy movement and critics of Beijing's rule in the city, they say, with the aim of uncovering compromising information.

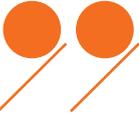
The arrested pair was quickly released without any public announcement. The police declined to divulge their identities to Reuters.

RETIRED POLICE OFFICERS

Retired senior Hong Kong police officers and managers at private security companies say mainland intelligence services have been recruiting former Hong Kong police to assist in political surveillance operations. Recruiters identify former officers with surveillance



Hong Kong law enforcement veterans would be valued for their local knowledge and contacts. As retirees, they are private citizens, which may mean there is a grey area in which they can operate.



training and pro-Beijing sympathies. They say more than 20 of these retired officers have been assigned to surveillance teams working alongside mainland agents.

One of the Mercedes cars that To reported to police is registered to a local resident who says he is a Hong Kong public servant. The man told Reuters he played no role in the surveillance. The other car was displaying a licence plate that is not registered to any vehicle, according to records of the Hong Kong government's Transport Department.

News of the mainland spying operation comes as many Hong Kong residents are already chafing at China's tightening grip on their city. The fear: Beijing is eroding the wide-ranging personal freedoms and independent law enforcement enshrined in the one country, two systems formula under which they have been governed since British rule ended in 1997.

Pro-democracy lawmakers, academics and political activists worry that Hong Kong is becoming more like mainland Chinese cities, where the internal security services join forces with the police to crush dissent.

They say the surveillance has intensified over the last 12 months, as the city's pro-democracy movement began planning for the campaign of civil disobedience that disrupted Hong Kong's central business district for more than two months from late September. For China's leaders, the upheaval presents one of the most serious popular challenges to Communist Party rule since the 1989 Tiananmen protests.

EMBARRASSING MATERIAL

The surveillance of To is just one example of the monitoring of Beijing's political opponents. Other lawmakers, political activists, academics and Catholic priests say they have been monitored or followed in recent months. In some cases, they suspect that the surveillance is aimed at unearthing material that could be used to discredit or embarrass them.

To says the surveillance is especially

intimidating at a time when Beijing is struggling to contain demands for fully democratic elections in the former British colony. "In these difficult times, we don't know what ... action they will take in an extreme case," he says. "I don't know what their motive is, you know, so it is always threatening behaviour."

The Liaison Office in Hong Kong, Beijing's official representative body in the city, did not respond to faxed questions from Reuters.

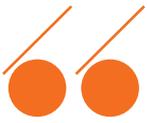
A spokesman for the office of Chief Executive Leung Chun-ying said it did not comment on individual cases. "All persons in Hong Kong, whether residents or not, have to abide by the laws of Hong Kong," the spokesman said.

Hong Kong police cleared out the main protest site late last week, bringing to an end more than 10 weeks of street demonstrations. To was among the pro-democracy politicians arrested on suspicion of obstructing police and illegal assembly as they gathered for a last show of defiance at the site. He was released after several hours.

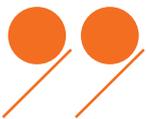
In written answers to questions from Reuters in October, a Hong Kong police spokesman confirmed that an investigation had been launched after "someone surnamed To" reported being followed. "On August 12, two local Chinese males aged 56 and 54 were arrested in North Point," the spokesman said, adding that they had been released on police bail.

The police described the case as suspected loitering, but did not give further details about the arrested men and did not respond to a question about whether the suspects were retired Hong Kong police officers. In a reply to Reuters last week, the police said the investigation had been "curtailed" due to insufficient evidence that any criminal offence had been committed.

Hong Kong law enforcement veterans would be valued for their local knowledge and contacts. As retirees, they are private citizens, which may mean there is a grey area in which they can operate, say legal experts. And, if one of these surveillance operations were exposed,



In a sign of Beijing's frustration with the Hong Kong protests, articles in China's state controlled media have accused foreigners of inciting the demonstrations.



the mainland security services could distance themselves from any fallout, according to foreign diplomats who follow political events in Hong Kong.

For To, it would be a bitter irony if former Hong Kong police were following him as part of a mainland-led operation. "In the past they never trusted Hong Kong people," he says, referring to Chinese officials. "So, now they trust Hong Kong people more in a sense."

UNITED FRONT WORK DEPARTMENT

The one country, two systems agreement does not explicitly prohibit China's vast security and intelligence apparatus from operating in Hong Kong, but it does require any investigation and enforcement action to be carried out by local police and under the city's laws.

These operations are headed by a bureau of China's powerful Ministry of State Security (MSS), according to security analysts, foreign diplomats and former Western intelligence officers. The MSS gathers information on political figures and potential threats from a wide network. And it collaborates with other Chinese security services and the Communist Party's United Front Work Department, an organ that aims to spread the party's influence at home and abroad and which is active in the city of 7.2 million.

China's Ministry of State Security did not answer multiple calls seeking comment to its only publicly available telephone number.

China routinely complains about what it says is foreign interference in its internal affairs. In a sign of Beijing's frustration with the Hong Kong protests, articles in China's state controlled media have accused foreigners of inciting the demonstrations. Beijing's hand-picked leader in Hong Kong, Chief Executive Leung Chun-ying, said in October that "external forces" were involved in the protests. He provided no evidence.

Many of Hong Kong's politicians, including pro-democracy figures, do maintain links with foreign diplomats, international

non-government organisations, human rights groups and think tanks. Among them is To, the local lawmaker tailed by the surveillance team, who once told U.S. diplomats in Hong Kong that his Democratic Party had been penetrated by mainland agents and was in a "dangerous position," according to a 2007 leaked U.S. cable published by Wikileaks.

DESIGNED TO INTIMIDATE

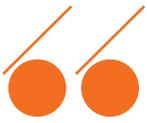
Sometimes, activists say, the surveillance of democracy leaders seems designed purely to intimidate. In May, Joshua Wong, one of the most prominent student protest leaders, visited Taiwan for a short vacation with two other members of the group Scholarism, which is now at the forefront of the pro-democracy movement.

The night they arrived in their ground-floor room at the Simple+ Hotel in Taipei, the phone rang. A male voice speaking Mandarin asked for Wong, saying a "Hong Kong friend" wanted to pay him a visit. The boys said Wong wasn't available. Later, they asked at the front desk if the call had come from outside the hotel, said the 18-year-old Wong. The desk attendant said no, leading Wong and his friends to conclude that the caller had been inside the hotel and knew their room number.

"Even my parents didn't know which hotel I was in or the exact time I was arriving. But that guy knew the details," Wong told Reuters.

Over a period of two days, at least two men followed Wong and his friends. One came within about two meters to snap pictures of them on his mobile phone. When the boys confronted the man, he said he had been hired to follow and photograph them, but was not part of the media. Wong has pictures of one of the men, which he posted on his Facebook page. He said he didn't bother to report the incident to police.

Derek Lam, a student activist on the trip with Wong, said he suspected the men following them were trying to collect dirt to tar the pro-democracy movement. The man they confronted, he said, told them he had



Sometimes, activists say, the surveillance of democracy leaders seems designed purely to intimidate.



instructions to photograph them, especially if they did anything like visit “women.”

Chan Kin-man, a founder of the democracy movement, said several men took turns to monitor his movements in late September, just before the protests erupted. Chan, an associate professor of sociology at Chinese University, described the men as “middle-aged” and said they were positioned at a bus stop opposite his apartment complex. They stayed for several days, working in shifts around the clock.

‘TRYING TO SLIP A TAIL’

Fellow academic Robert Chung, a Hong Kong University pollster, is accustomed to being attacked in the city’s pro-Beijing press over his surveys. His work explores sensitive topics, including attitudes to political reform and feelings about national identity. But earlier this year Chung was stunned when a report in one of these newspapers revealed he was being followed.

A full-page spread in the pro-Beijing *Ta Kung Pao* newspaper in May accused him of reckless driving, including running an amber light and making illegal turns. The report included a number of photographs of his car on different streets on different days over a period of weeks in March. The report also carried a graphic showing the routes he took and quoted a private investigator saying his “driving methods are similar to those used by spies trying to slip a tail.”

For Chung, the level of detail in the article suggested expertise beyond the skills of muck-raking reporters. “There was never any real evidence until I read that *Ta Kung Pao* story,” Chung told Reuters. “I believe they are professional agents.”

A spokesperson for the *Ta Kung Pao* chief editor said the report was done “independently” by the paper’s reporters.

Catholic priests in Hong Kong say they have been approached by MSS agents seeking gossip on local clerics and church affairs, as well as information on the Vatican’s thinking on China. The officers typically visit Hong

Kong on tourist visas but make their identities clear, seeking discreet meetings in cafes and restaurants.

TRIAD-STYLE ATTACK

For To, apprehensive about the silver Mercedes following him, it was a simple test that convinced him he needed to go to the police. On Monday, August 11, he stepped out of his apartment building with his three-year-old son, turned right and walked down the street in North Point.

Sure enough, one of the silver Mercedes was parked near his building. To and his son walked a few doors down into a small café. A man got out of the car and followed them, peering through the window.

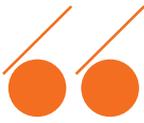
“That’s when I knew I had to act,” said To. “This was not normal.” That day, he went to the police.

To suspects one reason the police moved so fast after he reported the surveillance is that they might have feared for his safety. In February, on a street not far from To’s home, one of his close friends, investigative journalist Kevin Lau, was stabbed in a triad-style attack. Lau was lucky to survive.

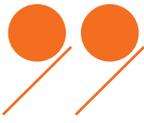
To had been quoted in one of the journalist’s more controversial articles in a Chinese-language newspaper. To said police warned him he needed to be alert and offered him protection but he declined. Police in Hong Kong and the mainland have arrested nine men in connection with the attack on Lau.

In his written police report, To described first seeing the Mercedes about four cars behind him on the way to work at the Legislative Council on Wednesday morning, Aug. 6. It followed him whenever he changed lanes and slowed whenever he slowed, he told police. That day, he saw the Mercedes parked outside his workplace with two Chinese men sitting inside. The same car followed him home.

The next day, Thursday, a second silver Mercedes followed him to the office and parked by a nearby building. Shortly before midday



Catholic priests in Hong Kong say they have been approached by MSS agents seeking gossip on local clerics and church affairs, as well as information on the Vatican's thinking on China.



on Thursday, To left his office and drove to the Hong Kong Jockey Club at the Happy Valley race course, he said in his report. The Mercedes that had followed him in the morning tailed him to the prestigious club.

The next morning, Friday, the second silver Mercedes was back on his tail when he drove to work, he reported. This pattern continued until the arrests.

After the police swooped, To said, they told him they took the two men and the two seized cars to a nearby police station. The police told him the two men refused to answer questions. They also told To there was no evidence to charge the pair with any offence. "They assured me I would not be followed anymore," To told Reuters.

'ALL A MISUNDERSTANDING'

As of the day of the arrests, one of the Mercedes that To reported to police was registered to a residential address in the container port district of Kwai Chung in Hong Kong's New Territories, according to Hong Kong Transport Department vehicle ownership records.

In an interview with Reuters outside his home in late October, the car's owner, Riky Li Kwok-ming, said the police had asked him to bring the Mercedes in for inspection. The police checked the vehicle and asked him if he had been following anybody, Li told Reuters. Li said the police allowed him to leave and he had not heard from them since.

Li denied he was a current or former police officer. He said he worked for the Hong Kong government but declined to give details. Li also said he hadn't followed anybody or let others use his car. He said he had been driving on Tanner Road in North Point, where To lives, because his office was in the same area.

When asked if he had been conducting surveillance while his car was parked outside the government office complex, Li said: "Of course not, I was just picking up my wife." Li said his wife also worked for the Hong Kong government, but wouldn't elaborate.

Reuters later located Li's car in a marked

parking bay in government offices in North Point. In a follow-up interview in the parking lot earlier this month, Li said he worked for the government logistics department and had been there for more than 10 years.

The Hong Kong authorities have yet to explain who was following To and why.

In his case, Riky Li Kwok-ming says the answer is simple: "This is all a misunderstanding." 

Additional reporting by Anne Marie Roantree, Clare Baldwin and Lizzie Ko in Hong Kong and Ben Blanchard in Beijing
Editing by Peter Hirschberg and Michael Williams



China tightens grip on Macau as dissent rises in gambling hub

BY FARAH MASTER AND JAMES POMFRET

DECEMBER 19 MACAU

B By night, Ieong Man Teng was dealing baccarat to gamblers at the Wynn Macau casino. By day, he was mobilising thousands of fellow dealers to protest on the street for better working conditions and higher pay.

That made him one of the people on Beijing's watch list earlier this year in Macau, the world's biggest gambling hub.

Ieong, 29, said associates of prominent businessmen in Macau and a Macau politician

who sits on the Chinese People's Political Consultative Conference (CPPCC) warned him in face-to-face meetings, including one at a local cafe, to tone down his activities. He did not name the politician.

"They said they were passing on a message from people up there (Beijing). I consider these to be threats," Ieong said.

A spokesman for the CPPCC, a largely ceremonial but high profile advisory body to China's parliament, told Reuters he did "not know anything about this". He did not elaborate.

Ieong's experience is part of a broader squeeze in Macau, where Beijing is tightening its grip after a series of grassroots protest actions in the former Portuguese colony. Unnerved by pro-democracy protests roiling neighbouring Hong Kong, China has moved firmly in Macau to stifle any parallel challenge to the central government's authority.

PRESIDENT XI VISITS

President Xi Jinping visits Macau on Dec. 19-20 to celebrate the 15th anniversary of its handover to the mainland with the territory at a crossroads.

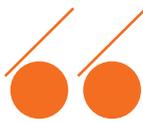
Macau's gambling take, which makes up 80 percent of its revenues, has suffered the biggest decline since the industry was liberalised in 2001. This is partly because Xi's sweeping crackdown on corruption has scared off high-rollers, including corrupt officials.

Xi is also helping inaugurate a second five-year term for Macau Chief Executive Fernando Chui, who was re-elected by a pro-Beijing panel in August amid unprecedented political protests.

Au Kam San, a pro-democracy Macau lawmaker, said Beijing still viewed Macau as more controllable than Hong Kong. But the protests from July to October by Ieong's gambling union, in a city where casinos raked in \$45 billion last year, troubled Beijing.

"The gambling union is much more important and it has a higher risk for Beijing because it's mobilizing potential is much stronger," Au said. "It's seen as a threat to Beijing."

The fact that gaming is so closely connected



They said they were passing on a message from people up there (Beijing). I consider these to be threats.



with the mainland means that Beijing cannot just look at economic growth and tax revenue “when looking at Macau’s overall well-being,” Li Fei, deputy secretary general of the National People’s Congress Standing Committee said in a speech in Macau on Dec. 3. “It must think from the perspective of China’s economic and social stability and development.”

Beijing’s Liaison Office in Macau and the Macau government did not respond to Reuters’ questions sent by fax and email.

ACADEMIC FREEDOM

Like Hong Kong, Macau is ruled under the one country, two systems model that affords its residents wide-ranging personal freedoms that don’t exist on the mainland. Critics say these have been eroding under pressure from China.

Last month, the University of Saint Joseph issued a document, titled “USJ policy on political activities,” that places limits on political discussion at the Catholic institution. When asked to provide a copy of the guidelines, the University’s Pro-Rector for Academic Affairs and Development Vincent Yang told Reuters they were for internal use only and declined to give more details.

The guidelines were issued after a professor at the University, Eric Sautede, was dismissed in June after writing a column in a local newspaper extolling a candlelight vigil in Macau commemorating the 25th anniversary of the Tiananmen Square student-led protests.

Peter Stilwell, the rector of Saint Joseph’s, said Sautede was sacked for violating the primary principle of the Church, “which is of non-intervention in local political debate”.

Bill Chou Kwok-Ping, a professor at the University of Macau and prominent civil rights activist, was let go in August for similar reasons. The University said it chose not to renew Chou’s contract because he violated professional conduct regulations by not remaining politically neutral.

Macau’s Tertiary Education Services Office is discussing guidelines that would assess universities and tertiary institutions

for various issues, including funding, on the basis of whether they adhered to the principle of “love China, love Macau”, according to a person who attended the meeting.

The tertiary office did not respond to Reuters’ questions sent by email.

UNIVERSAL SUFFRAGE

Situated at the mouth of China’s Pearl River delta, Macau has traditionally been sympathetic to Beijing, with around half of its 600,000 population having emigrated from the mainland over the past three decades. As a result, there has been little grassroots protest in the city since China resumed control in 1999.

That changed in May. A record 20,000 people took to the streets to protest poor public services and a bill that provided lavish perks for senior civil servants.

Then, in August, Macau activists organised an unofficial referendum asking residents whether they trusted their chief executive — as the territory’s head of government is called — and if full universal suffrage should be introduced. At the same time in Hong Kong, tensions were rising over a plan by activists, also demanding full democracy, to paralyse the central business district.

The results of the Macau referendum showed that 89 percent of the nearly 9,000 people who took part didn’t trust Chui. The sole candidate for chief executive in the August election, he was chosen by a panel of 400 largely pro-China loyalists. Data released on the poll’s online site also showed that 95 percent of the participants said they were in favour of allowing all registered voters to cast ballots for a chief executive.

Macau authorities moved quickly to disrupt the referendum, shutting polling booths. They also arrested five people for breaching privacy laws because the ballot asked for telephone and ID card numbers to prevent fraudulent voting.

“ESCALATING THE MOVEMENT”

Jason Chao, one of those detained, told Reuters he fled Macau for a few days at the end

of the referendum to dispose of all the data, defying orders from police to hand over the information. Chao, a computer software developer and leading member of the New Macau Association, said he refused to let police officers search his apartment.

“There’s a trend for them to use the criminal justice system as justification for getting information from you, for searching your house,” Chao said in an interview in Macau, referring to the local authorities and the Chinese government. “They’re doing it to essentially deter us from escalating the movement.”

Ahead of Xi’s visit, Chao has met with men he described as plain clothes policemen and had informal meetings with representatives from Beijing, who described themselves as researchers but were not affiliated with any institution, he said.

Macau police declined to comment on questions sent by email.

Chao said he was told his group’s annual pro-democracy protest held on the anniversary of Macau’s handover could go ahead as long as it didn’t target President Xi.

“They invited me to lunch and didn’t put it in a straight-forward manner,” he said. “They diplomatically said that if you decide to do your annual demonstration as normal, it will be fine as long as you don’t do other things targeting Xi Jinping.” 

Additional reporting by **Ben Blanchard** in Beijing
Editing by **Bill Tarrant**, **Peter Hirschberg** and
Clarence Fernandez

The mainland's colonisation of the Hong Kong economy

Beijing has struggled to tame Hong Kong politically. But in business it's a different story as mainland Chinese companies consume ever bigger chunks of the city's economy.

BY CLARE BALDWIN, YIMOULEE, AND CLARE JIM

DECEMBER 31 HONG KONG

When Xi Jinping wanted to deliver a political message to Hong Kong as protesters demanding free elections were threatening to take to the streets, he summoned the tycoons who dominate the city's economy. The words from the Chinese leader at the September 22 meeting in Beijing were uncompromising but not surprising. He would not entertain any demand for full universal suffrage in Hong Kong, according to two people who attended.

Just six days later, pro-democracy activists made good on their threat, unleashing more than two months of street demonstrations. But while Xi's message that day in the Great Hall of the People failed to deter the protesters, in speaking directly to the city's business and professional elite he was showing where Beijing believes real power in Hong Kong resides.

And it is here, in the city's business sector, that China is inexorably tightening its grip on the former British colony. Even as Beijing struggles to tame Hong Kong politically, Chinese companies are consuming ever bigger chunks of the city's key sectors including real estate, finance, power, construction and the stock market.

Many of these industries have for decades been dominated by the business titans who attended the meeting with Xi. Men like Li Ka-shing, Asia's richest man, casino and hospitality billionaire Lui Che-woo and palm oil magnate Robert Kuok. Now they are witnessing a mainland business invasion of the city.

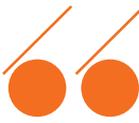
One of the most telling signs of change is the space mainland Chinese companies lease in Central district, the heart of Hong Kong's financial centre. These firms now account for over 50 per cent of new leases signed for offices there, according to a September report from Hong Kong-based brokerage CLSA. That's up from 20 percent in 2012, the report said.

The trend is the same in all major business districts. Mainland occupancy of 25 key Grade A office buildings, or prime office space, in the districts of Central, Admiralty, Sheung Wan and Wan Chai increased from 13 percent in 2008 to 21 percent earlier this year, according to commercial real estate services firm CBRE.

"We do expect more mainland financial firms moving into Hong Kong," said Simon Smith, senior director of research and consultancy at real estate services provider Savills Plc in Hong Kong. "They like landmark properties, high-profile buildings. They often like naming rights if it's available."

'PRICE IS NOT AN ISSUE'

The office directory at Hong Kong's 88-floor



Price is not an issue for them. That's why they offered prices that surprised everyone.



International Finance Centre has a growing number of mainland companies on the list. Among them is China Development Bank International Holdings Ltd, which held its opening ceremony in 2011 and serves as the offshore investment firm of China Development Bank, the country's biggest policy lender.

"If you go to the International Finance Centre now and compare it to five years ago, it's very easy to see that there are many more Chinese enterprises represented," property analyst Nicole Wong, an author of the CLSA report, told Reuters.

In a market accustomed to stratospheric land prices, state-owned Chinese developers this year stunned long-established local property giants with winning bids exceeding auction forecasts by up to 20 per cent. Of the six available plots sold since the middle of last year in Kai Tak district, one of Hong Kong's largest developments of residential and commercial complexes, two went to China Overseas Land & Investment (COLI) and one to Poly Property Group.

"Price is not an issue for them," said a former senior executive of a Hong Kong-listed developer who was responsible for bidding at land auctions before he left the company in June. "That's why they offered prices that surprised everyone."

A spokesperson for Poly said the company had no comment. COLI did not respond to questions sent by email.

While it was predictable business ties would expand after the 1997 handover, Beijing has made it clear that economic integration is central to reinforcing its sovereignty over Hong Kong, which is ruled under the one country, two systems model that affords the city's 7.2 million residents broad personal freedoms. Part of Beijing's vision is to draw Hong Kong into a Pearl River Delta mega-economy that would also include the giant southern Chinese cities of Shenzhen and Guangzhou just across the border.

In 2011, a chapter was dedicated to Hong Kong for the first time in China's five-year blueprint for national economic development. The

12th Five-Year plan, covering the years from 2011 to 2015, lays out how Beijing wants to connect Hong Kong with the Pearl River Delta's increasingly prosperous middle class consumers.

'IT WILL BE LIKE NEW YORK'

Under the plan, Hong Kong would be a leader for the region in shipping, trade, services and distribution. In finance, Hong Kong would serve as an offshore market for the mainland currency, the renminbi.

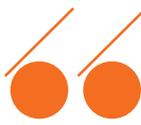
New transport links from Hong Kong now under construction, including a high speed rail to Guangzhou and a bridge across the Pearl River Delta to the mainland city of Zhuhai near Macau, would allow the rapid movement of commuters and visitors.

"It will be like New York where you have people working in Manhattan and living on Long Island or in New Jersey and commuting in to work every day," said Hong Kong entrepreneur Allan Zeman, who developed the Lan Kwai Fong pub and restaurant area popular with expatriates. "People who can't have a home here (in Hong Kong) will live in Shenzhen and be able to come here in 10 minutes."

The mainland's construction behemoths, including state-owned China State Construction International Holdings Ltd, are also grabbing market share. Hong Kong's permanent secretary for Development (Works), Wai Chi-sing, said in an interview that while mainland firms accounted for less than 15 percent of public works contracts by value in the mid 1990s, they now accounted for more than a third.

While mainland Chinese companies are rapidly expanding into Hong Kong, Western banking and financial institutions still have a strong presence in the city. Global bank HSBC Holdings Plc, for instance, employed more than 28,000 people in Hong Kong at the end of 2013.

For Beijing, growing economic clout has not been mirrored by increased popular support. Frustrated by Hong Kong residents' lack of identification with the mainland 17 years after



Hong Kong without the mainlanders would be a very small city. Ocean Park and Disney without the mainlanders would be nowhere. They'd be losing money.



the handover, China has at times resorted to covert means to bolster its control. Earlier this month, for instance, Reuters reported that retired Hong Kong policemen were part of a mainland-led surveillance operation to tail leading pro-democracy figures in the city.

Although the street protests ultimately petered out, at their height they drew tens of thousands, presenting Xi Jinping with his most serious popular challenge since he took power two years ago. While the protesters have demanded full universal suffrage, the mainland authorities insist that only a handful of Beijing-vetted candidates can stand in the next elections for the city's political leader in 2017. Hong Kong's current chief executive, Leung Chun-ying, got the backing of Xi and Premier Li Keqiang during a visit to Beijing last Friday, according to reports in China's state-run media.

A Hong Kong government spokesman said in an email response that economic integration with the mainland has been mutually beneficial, citing the growing number of mainland companies listed on the Hong Kong stock exchange and the city's role as the largest offshore renminbi centre. The Hong Kong and Macau Affairs Office in Beijing did not respond to questions from Reuters.

NOT ALWAYS AMICABLE

Rather than foster understanding, growing economic integration has at times raised tensions. One source of friction is the real estate market where wealthy mainland Chinese have bought up property in Hong Kong, helping to push up home prices that are already out of reach for many of the city's residents.

"One might have assumed that the inflow of mainland money and companies and people here, and the favorable economic policies of the mainland should have increased emotional integration rather than just economic integration but it hasn't," said David Zweig, chair professor of social science at Hong Kong University of Science and Technology. "For the rich people here, the heart has followed the dollar but for the middle class and for students

it hasn't."

That's been evident, at times, on the streets of Hong Kong. While the growing influx of mainland tourists has been good news for the city's retailers – the number of Chinese visitors catapulted from 28 million in 2011 to 40.7 million last year – interactions between mainlanders and Hong Kong residents are not always amicable. In one incident that made headlines earlier this year, locals got into a scuffle with a mainland couple who had allowed their toddler to urinate in the street.

"Hong Kong without the mainlanders would be a very small city," says Allan Zeman, explaining the business elite's attitude to the growth in tourism. "Ocean Park and Disney without the mainlanders would be nowhere. They'd be losing money." Zeman developed Ocean Park, one of the city's main amusement parks.

When Xi met the delegation of tycoons and professionals on the eve of the demonstrations, he gave no indication he was worried, according to one delegation member who gave Reuters an account of the Chinese leader's remarks. Instead, Xi appeared to signal that the city's troubles were relatively minor compared to other problems in his in-tray.

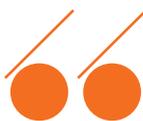
Before commenting on Hong Kong, Xi gave some of the richest men on earth a tour of China's foreign policy challenges. He told the tycoons that China was now a major force in the world and most of his attention would be focused on ties with bigger nations including the U.S. and Russia, the delegate said.

When he eventually turned to Hong Kong, Xi said Beijing had no intention of altering any of its policies and urged the tycoons to support the city's chief executive. He also said the Hong Kong economy was falling behind those of Singapore, Taiwan and South Korea.

Li Ka-shing, Lui Che-woo and Robert Kuok, three of the tycoons who were part of the delegation that met Xi, did not respond to questions from Reuters.

DOWNPLAYING THE PROTESTS

In an interview earlier this month, another



For the rich people here, the heart has followed the dollar but for the middle class and for students it hasn't.



delegate, former Hong Kong Law Society president Ambrose Lam said Xi had ruled out any departure from the guidelines already laid out for the city's political future. Without citing the Chinese leader directly, Lam said he didn't think the protests were a big issue for the Chinese leadership.

It would have been different, he said, if they had happened 30 years ago when Hong Kong's economy was more important to China. But the city's gross domestic product is now only 3 percent of China's, he added. At the time of the handover in 1997, it was almost a fifth.

Still, summoning the city's business leaders suggests Beijing may be more concerned than it is prepared to acknowledge. The city's business leaders were also called to the capital in the aftermath of a 500,000-strong protest in 2003 when China attempted to introduce controversial new security laws. The proposed laws were withdrawn and the then chief executive, Tung Chee-hwa, was eventually forced to resign.

As the mainland ponders how to contain demands for political change, its economic footprint in Hong Kong continues to expand. In retail banking, subsidiaries of mainland banks operate nearly 500 branches in Hong Kong, accounting for about 40 per cent of the total number of branches, according to figures from SNL Financial, a financial service research company.

Hong Kong's financial system has also become more intertwined with the mainland, especially as it has emerged as the premier hub for offshore renminbi business. The market in so-called dim sum bonds, bonds denominated in renminbi but issued outside the mainland, is rapidly closing on its Hong Kong dollar counterpart.

The bonds, named after a popular Hong Kong cuisine, were first issued in 2007. Since then, the outstanding value of dim sum bonds has soared to around 700 billion renminbi, according to industry estimates. That's nearly 60 per cent of the value of Hong Kong dollar bonds, according to data compiled by the Asian Development Bank.

And mainland companies have long been making inroads into the local stock market. They now account for 54 percent of the companies traded on the Hang Seng Index.

MAINLAND GIANTS MAKE INROADS

As part of Beijing's plan for the Pearl River Delta, Guangdong and Hong Kong will seek to integrate their transport, energy and power grid infrastructure. For its part, the Hong Kong government is pushing to boost electricity imports from mainland China to reduce pollution and the dominance of two local utilities backed by powerful families, say industry experts who have been involved in consultations with the government.

Hong Kong's grid is not interconnected with China Southern Power Grid, which supplies electricity to Guangdong and four other southern provinces. Plugging Hong Kong into the Chinese grid would create competition for the city's dominant local utilities — CLP Holdings, backed by the wealthy Kadoorie family, and billionaire Li Ka-shing's Power Assets Holdings — and further strengthen Hong Kong's ties with mainland China. The two local firms have enjoyed guaranteed returns for decades under what is known as the Scheme of Control.

But the mainland grid giants are making inroads. China Southern Power Grid last year bought a 30 percent stake in CLP's power unit Castle Peak for \$1.6 billion, while State Grid Corporation of China spent about \$1.2 billion to buy into the local initial public offering of HK Electric Investments, a spinoff of Power Assets, early this year.

Hong Kong's Environment Bureau said in an email response that importing electricity from mainland China was one of two options under consideration. HK Electric said via email that local power generation through the increased use of natural gas was its preferred option. CLP said it had shared its views during the government consultations.

One area where mainlanders have yet to make headway is the city's elite clubs. With the exception of some clubs like the Aberdeen

Marina Club and the Jockey Club which offer hefty debentures, it is difficult for newcomers like mainland Chinese to get membership as some of these establishments have waiting lists that can be as long as 20 years.

But at places like the Ladies Recreation Club (LRC) and the Hong Kong Golf Club, members say there is definitely more Mandarin being spoken.

“Mainlanders haven’t quite got in any meaningful way into the clubs,” says a Hong

Kong resident who is a member of three clubs. “But it is only a matter of time.” 

Additional reporting by **Anne Marie Roantree, Saikat Chatterjee, Charlie Zhu, Xiaowen Bi, Michelle Chen, Michelle Price, Donny Kwok and Lizzie Ko**

Writing by **David Lague**

Editing by **Peter Hirschberg and Bill Tarrant**

