



HIGH REPRESENTATIVE
OF THE UNION FOR
FOREIGN AFFAIRS AND
SECURITY POLICY

Brussels, 26.4.2017
JOIN(2017) 15 final

JOINT REPORT TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

Macao Special Administrative Region: Annual Report 2016

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Summary

Since the handover of Macao to the People's Republic of China in 1999, the European Union (EU) and its Member States have closely followed political and economic developments in the Macao Special Administrative Region (SAR) under the 'one country, two systems' principle. The EU adheres to its 'One China' policy and supports the 'one country, two systems' principle and its implementation.

This annual report on developments in Macao is issued in line with the commitment given to the European Parliament.

In 2016, the 'one country, two systems' principle continued to work well, to the benefit of the Macao SAR, China as a whole, and the international community.

The Chief Executive was elected, unopposed, in 2014. This was the third time in a row that only one candidate stood for election as Chief Executive. Macao's Basic Law and other legislative acts do not provide for the possibility of universal suffrage. However, the EU encourages the Macao authorities to consider ways to promote greater public involvement in the election of the Chief Executive, thereby enhancing the legitimacy of the position and contributing to good governance.

The fundamental rights and freedoms of citizens continued to be respected. Macao's media continued to express a broad range of views despite some concerns about increasing self-censorship.

Macao's market-based economy continued to function efficiently, although economic growth suffered from a marked decline in gaming revenues in the first two quarters, on which Macao is over-reliant. Macao's fiscal reserves remained in surplus. GDP growth rebounded in the third quarter, registering an increase for the first time in 2 years. To reduce over-reliance on the casino industry, the government launched its first ever Five-Year Development Plan (2016-2020).

A key priority is improving the lives of ordinary people, who face mounting living and housing costs. Macao continues to suffer from an acute labour shortage. However, imported labour has become a sensitive issue, and there is no political consensus on how to address it. The Macao government needs to be modernised and made more efficient; administrative reforms are ongoing.

EU-Macao relations continued to flourish, with a growing portfolio of cooperation activities and solid trade relations. Owing to the sharp contraction in Macao's economy, EU-Macao trade shrunk in 2016. Priorities for 2017 include cooperation on economic diversification, the fight against trafficking in human beings, legal affairs, regulatory matters and research and innovation.

Political developments

The Macao government concentrated on improving the region's law-based governance, transforming the economy to make it sustainable and improving the population's living standards by reducing social inequality and increasing the supply of government-built housing.

Macao's Basic Law and other legislative acts do not provide for the possibility of universal suffrage. However, the EU encourages the Macao authorities to consider ways to promote greater public involvement in the election of the Chief Executive, thereby enhancing the legitimacy of the post, increasing public support and strengthening governance.

On 9 August, lawmakers approved the amended Legislative Assembly Electoral Law, which aimed to tighten campaigning rules. The number of directly elected seats remained unchanged. The aim of the amendments was to ensure that the election process was conducted with integrity. Pro-democracy lawmakers called it a missed chance for democratic progress and called for more substantial reforms, including a discussion on the introduction of universal suffrage.

On 16 December, the Legislative Assembly passed amendments to the Electoral Law. They include new requirements for oath-taking by elected officials and the eligibility of individuals to participate in electoral campaigns. The Secretary for Administration, Sonia Chan, said the amendments were necessary following the interpretation of the National People's Congress Standing Committee regarding Hong Kong lawmakers.

On 12 August, the Legislative Assembly approved the draft legislation complying with a United Nations Security Council resolution on fighting terrorism and the proliferation of weapons of mass destruction, which will allow assets to be frozen.

In the spring, the government submitted a controversial draft to the Legislative Assembly on 'Interregional Judicial Assistance in Criminal Matters' regarding the extradition agreement between Macao, mainland China and Hong Kong. In May, the Legislative Assembly rejected the draft of this multilateral deal and sent it back to the government for review, citing 'technical problems'. After a brief period of reflection in June, the government withdrew its draft proposal until a consensus has been reached between Macao, mainland China and Hong Kong, saying that it took longer than expected to reach an agreement due to differences between the jurisdiction regimes in different territories. Civil society and the legal profession had expressed their concerns about the implications of a possible extradition agreement. They also complained about not having been properly consulted.

Around the same time, law enforcement agencies in Macao admitted to having turned over at least three people, two of them Hong Kong permanent residents, to the mainland authorities in recent years, despite court rulings saying that such extraditions were unlawful. This created further cause for concern regarding the ongoing discussions on an extradition agreement. In 2015, the United Nations Committee Against Torture highlighted in its conclusions on Macao

the issue of the surrender of fugitives, but the Macao authorities do not seem to have satisfactorily addressed this. The EU reiterates the importance it attaches to the rule of law and respect for human rights, and the need to comply fully with international law in matters such as extradition agreements.

Equal opportunities, rights and freedoms. Under the ‘one country, two systems’ principle, the rights and fundamental freedoms of the people of Macao continued to be respected and the rule of law was upheld. Macao enjoys a high level of civil liberties and respect for human rights and fundamental freedoms. Nonetheless, the government remained opposed to a proposal by the UN Committee Against Torture to establish an independent human rights body, arguing that this recommendation was not applicable to Macao as a special administrative region of the People’s Republic of China.

The **media** remained sufficiently diverse and were able to express a range of views without restriction. There appears to be a degree of self-censorship, particularly in Chinese language media and when reporting on Chinese affairs. The international media operate freely. However, the Macao Journalists Association said it was deeply concerned that reporters were repeatedly insulted and shoved when covering the Pearl Horizon protests on 20 December. The Association said such behaviour was a violation of press freedom and expressed concern that a journalist from Hong Kong’s Apple Daily newspaper was denied entry to Macao to cover the protests. This is not the first time journalists and members of political groups from Hong Kong have been denied entry.

There are continuing concerns about **discrimination** on the grounds of **sexual orientation** and **gender identity**, particularly in employment, education and healthcare. Same-sex relationships are yet to be included in the legislative act that makes domestic violence a criminal offence. The UN Committee on Economic, Social and Cultural Rights has urged Macao to adopt comprehensive anti-discrimination legislation for lesbian, gay, bisexual and transgender people. More legislation is also needed to promote gender equality, for example in the area of sexual harassment.

The Macao government made further substantial efforts to combat cross-border crime, in particular **trafficking in human beings**. The Human Trafficking Deterrent Measures Concern Committee, an interdepartmental body comprising government, law enforcement, justice and social affairs representatives, continued to tackle trafficking in human beings and implement measures aimed at prevention and victim protection. Despite a large number of complaints, the number of prosecutions and convictions for trafficking remains low. The government expressed its willingness to tackle the issue and welcomed cooperation with international partners, including the EU.

Macao has not effectively enforced freedom of association and collective bargaining as enshrined in International Labour Organisation Conventions. Proposed private bills on trade unions and collective bargaining have been rejected repeatedly in the Legislative Assembly. While employees are free to take part in trade union activities and industrial action, they are

not protected from retaliation. Article 70 of the Labour Relations Law allows employers to terminate employment without just cause by offering a modest amount of compensation. In 2016, lawmakers rejected the trade union bill for the seventh time, even though it received more votes than in the previous year. Many legislators cited Macao's underperforming economy and 'bad timing' as the main reasons for rejecting the bill.

Robust **anti-corruption** measures continued to be implemented even though the year saw some high-profile cases. The Commission Against Corruption (CCAC) criticised the government for breaching the law in a land swap deal involving a local factory. It said the deal was invalid and called for the site to be listed and protected.

Economic developments

Macao's economy has experienced a significant downturn over recent years as the casino industry was hit by the slowing Chinese economy and the anti-corruption campaign on the mainland. Macao's GDP plummeted by 20.3 %¹ in real terms in 2015. The contraction gradually eased in the third quarter of 2016, when GDP growth rebounded by 4 % in real terms, registering the first positive quarterly growth in two years. Overall, the economy shrank by 2.1% in real terms in 2016. Gaming revenue rebounded in the second half of 2016, after more than two years of continuous decline. Total gaming revenue fell by just 3.3 % to MOP 230.8 billion in 2016, a significant improvement on the double-digit drop in 2015. Tourism steadily recovered thanks to two new casino resorts, Wynn Palace and the Parisian. Total visitor arrivals edged up by 0.8 % to 30.9 million in 2016. Mainland China remained the most important source of tourists for Macao, contributing to two-thirds of visitor arrivals in the first 11 months of 2016, followed by Hong Kong (21 %), Taiwan (3.5 %), Korea (2.1 %) and Japan (1 %).

To reduce over-reliance on the casino industry, the government launched its first ever Five-Year Development Plan (2016-2020) in September, setting out comprehensive development targets to improve livelihoods and achieve economic diversification. It aims to turn Macao into an international hub for tourism and leisure and create a commercial and trade platform between China and Portuguese-speaking countries (the 'Centre and Platform' policies). The plan also includes increased efforts to achieve moderate economic diversification and strengthen regional cooperation, particularly with Guangdong province, as stipulated in China's 13th Five-Year Plan (2016-2020).

The Five-Year Development Plan proposes specific policy measures to reduce the economy's reliance on gaming in the long term. These include: capping gaming tables at an annual growth rate of 3 % for 10 years starting in 2013; increasing the share of non-gaming elements from 6.6 % of total gaming-related revenue at present to 9 % by 2020; raising employment

¹ Unless otherwise stated, economic indicators pertaining to the Macao economy have been sourced from the Statistics and Census Service of the Macao SAR government.

participation in retail, hotel and manufacturing sectors; strengthening financial services; and setting up the Macao SAR Development Fund (essentially a sovereign wealth fund) by 2019.

The Plan also covers a range of initiatives to promote creative industries, infrastructure development, smart city development, environmental protection and to strengthen healthcare, education and housing. It contains a reference to the ‘One Belt, One Road’ initiative and Macao’s possible role in this, particularly in terms of the maritime route and as a business facilitator for Portuguese-speaking countries. Following the revision of its maritime boundaries in 2015, Macao is seeking to promote its maritime economy and maximise its contribution to the ‘One Belt, One Road’ initiative.

In November, Chief Executive Fernando Chui presented his 2017 policy address to the Legislative Assembly. The government pledged to encourage operators to build boutique hotels and shopping malls, roll out an action plan to help local SMEs take part in large-scale exhibitions and expand the Young Enterprise scheme and offer quality training to young people.

The policy address also contained a set of welfare measures and subsidies, including the popular cash handouts to Macao residents for the tenth year in a row.

Macao’s fiscal position remained strong with deep reserves. Its fiscal reserves were estimated to reach MOP 468 billion, equivalent to 130% of GDP. This is extremely high for a territory with less than half a million people (excluding foreign workers). Macao has consistently recorded a fiscal surplus despite a significant drop in gaming taxes in 2015 and 2016.

Macao continues to suffer from an acute labour shortage. The unemployment rate has been at or below 2 % for the past four years, with 1.9 % recorded in 2016. Its economy therefore relies heavily on foreign workers and professionals. Despite the economic downturn, there were over 180 000 non-resident workers in 2016, representing 45 % of the working population. Imported labour has become a sensitive political issue. In November, the Secretary for Economy and Finance, Lionel Leong, reiterated in the Legislative Assembly that the Macao government would secure employment opportunities for local residents and would roll out a mechanism for non-resident workers to leave the Macao SAR. Legislators complained about the abuse of the labour import scheme, which resulted in job losses and stagnant wages for local workers as well as slower career progression for some managers. However, businesses have repeatedly complained about the lack of suitable professionals to handle their expanding operations.

China’s 13th Five-Year Plan contained a dedicated chapter on Macao (together with Hong Kong) and emphasised deeper cooperation between the mainland and Hong Kong/Macao. China expressed support for developing cooperation platforms for Guangdong-Hong Kong-Macao as well as for Hong Kong and Macao to play an important role in the Pan-Pearl River Delta region and in developing the Guangdong-Hong Kong-Macao Big Bay Area. In March, the State Council issued guidelines on promoting cooperation within the Pan-Pearl River Delta region, which includes 9 provincial regions — Fujian, Jiangxi, Hunan, Guangdong, the

Guangxi Zhuang autonomous region, Hainan, Sichuan, Guizhou and Yunnan — as well as the Hong Kong and Macao Special Administrative Regions (the ‘9+2’). China’s central government sees the region as a pioneer in reform, a key area for the mainland to secure cooperation opportunities with Hong Kong and Macao as well as a crucial area for making progress on the One Belt, One Road Initiative.

As a result, Macao continued to promote further integration with the Pearl River Delta region and sought to establish a niche position for itself as a bridge between China and Portuguese-speaking countries under the Forum for Economic and Trade Cooperation. Besides the Pearl River Delta region, the Macao Chief Executive’s policy address also mentioned greater cooperation with other Chinese provinces/municipalities such as Jiangsu, Beijing and Tianjin, and with the traditional industrial regions in the mid-western and north-eastern regions of China.

In October, Macao hosted the Fifth Ministerial Conference of the Forum for Economic and Trade Cooperation between China and Portuguese-speaking Countries. The Chinese Prime Minister Li Keqiang attended the forum, which aimed to boost China’s economic relationship with the developing world and to chart a new course for Macao. Mr Li’s visit was interpreted not only as offering clear support for Macao’s economic policies, but also as an expression of overall satisfaction with the Macao SAR, including its political development. He announced a further 19 measures designed to transform Macao’s economy, which include:

- China’s central government supporting Macao in developing an RMB clearing centre between China and Portuguese-speaking countries and helping it to develop financial leasing, e-commerce and export credit insurance.
- A Sino-Portuguese joint fund with headquarters in Macao for cooperation projects between large mainland e-businesses and non-banking payment organisations.
- China’s central government continuing to support Macao in areas like Chinese medicine, smart city development, tourism and its involvement with the neighbouring city of Hengqin.
- China also helping Macao establish cultural exchange centres, bilingual training centres and a youth innovation centre for exchanges with these countries.

Hong Kong and Macao initiated talks on their Closer Economic Partnership Arrangement (Hong Kong-Macao CEPA) in mid-July and started negotiations in October. The Hong Kong-Macao CEPA will cover trade in goods, trade in services and investment. However, it will not cover the free movement of people across the border for education or work. After the Hong Kong-Macao CEPA has been signed, China, Hong Kong and Macao may build upon their CEPAs to establish a new, common platform to advance further liberalisation and facilitation of trade and investment in the ‘Greater China’ region — the so-called Guangdong-Hong Kong-Macao Big Bay Area mentioned in the 13th Five-Year Plan.

Macao is still vulnerable to money laundering as the casino industry provides plenty of avenues for illegal money coming from the mainland. To counter this, Macao’s casino

regulator (the Gaming Inspection and Coordination Bureau, also known by its Portuguese acronym DICJ) revised its anti-money laundering rules in May.² ‘Instruction 1/2016’ requires casinos and junket operators to engage in more detailed anti-money laundering procedures. The new set of rules more than doubles the number of provisions. It stipulates that casino and junket operators must review the money laundering risks involved in their activities at least every two years and introduce ‘effective measures’ to tackle such risks. The rules require casino and junket operators to ‘identify and closely monitor transactions’ involving ‘politically exposed persons’. Instruction 1/2016 also expressly forbids casino and junket operators to conduct business with people using aliases or under cover of anonymity. Nevertheless, it has been alleged that even though Macao has made considerable efforts to develop an anti-money laundering framework that meets international standards, its junkets still show vulnerabilities. In 2016, the Financial Intelligence Office of the Macao SAR signed memoranda of understanding/cooperation agreements with Bangladesh, Canada and Israel.

In 2016, Macao joined the ‘inclusive framework on Base Erosion and Profit Shifting (BEPS)’ of countries and jurisdictions that have pledged to collaborate on the implementation of measures to combat multinational tax avoidance as part of the OECD/G20 BEPS framework. Macao has therefore committed itself to:

- adopting minimum standards on treaty shopping;
- implementing country-by-country reporting for transfer pricing;
- limiting the benefits of its intellectual property or other preferential tax regimes;
- fully implementing the mutual agreement procedure in their tax treaties.

This will be a significant factor in the process leading to the establishment of an EU list of non-cooperative jurisdictions, which will be drawn up in 2017. Macao successfully passed the Phase I and Phase II peer reviews conducted by the Global Forum on Transparency and Exchange of Information for Tax Purposes in 2011 and 2013 respectively, confirming that both its legal framework and current operations meet internationally agreed standards on the exchange of tax information. To date, Macao has concluded tax treaties with 20 jurisdictions, 5 of which are double tax agreements and 15 of which are Tax Information Exchange Agreements.

In December, Macao and the United States signed an intergovernmental agreement (IGA), which aims to help financial institutions in the Macao SAR comply with the Foreign Account Tax Compliance Act (FATCA). The Monetary Authority of Macao stated that the IGA would reduce the reporting burden and help its financial institutions comply with FATCA as it covers exemptions for financial institutions or products with a low risk of tax evasion by US taxpayers.

EU-Macao bilateral relations in 2016

² The previous anti-money laundering instruction had been issued in 2006. The new rules (Instruction No 1/2016) are available on the official website of the DICJ in Chinese and Portuguese.

As a result of the contraction in Macao's economy, EU-Macao bilateral trade fell significantly in 2016. EU exports to Macao dropped by 20.2% to EUR 603 million while imports from Macao declined by 6.5% to EUR 86 million. The EU has been recording trade surpluses with Macao since 2009, reaching EUR 516 million in 2016. Major EU exports included high-end leather goods, fashion, watches and jewellery, food and beverages and motor vehicles. In 2016, the EU was still Macao's second largest source of imports after mainland China.

However, the fluctuations in Macao's economy in 2016 had an impact on the EU's trade and investment interests and on the profits of European companies. The EU and its business community are keen to work with the Macao government to diversify its economy, improve the sustainability of its economic development and promote bilateral trade and investment flows. EU businesses could play an important role by providing expertise and services in the many ongoing infrastructure projects and expansion plans of private investors.

The 21st EU-Macao Joint Committee meeting was held in Brussels on 5 December 2016. During the meeting, Macao informed the EU of the recent publication of its Five-Year Development Plan (2016-2020), which sets out the blueprint for its economic and social development. The EU and Macao exchanged views on the development of their taxation policies. The EU welcomed Macao's commitment to implementing the automatic exchange of information in 2018 and encouraged it to take appropriate steps for the effective and timely activation of this exchange with the EU and other partners, so as to fulfil its commitment in accordance with OECD standards. The EU also welcomed Macao's recent decision to join the Inclusive Framework on BEPS. It encouraged Macao to pursue its efforts towards a fully open, transparent and non-discriminatory government procurement framework in line with international standards. Both sides welcomed the progress made by the Third Macao-EU Cooperation Programme in the Legal Field, whose aim is to promote the modernisation and development of Macao's legal system. Both sides emphasised that the EU-Macao co-funding mechanism will encourage Macao researchers to take part in the EU's Horizon 2020 research and innovation programme. The two sides agreed to explore cooperation on the environment and green technology, particularly in the Macao International Environmental Cooperation Forum and Exhibition. The EU and Macao agreed that continuing the training programme in conference interpretation and translation in Chinese and Portuguese would meet the EU's and Macao's needs for qualified interpreters in both languages. The EU also noted Macao's efforts to combat human trafficking. Both sides looked forward to strengthening their cooperation in this area following the joint workshop on trafficking in human beings held in January.

Given the increasing role of European businesses operating in Macao, the EU and Macao agreed that direct exchanges between these businesses and the Macao SAR government would be further strengthened by establishing a regular dialogue between the European business community, represented by the Macao European Chamber of Commerce, and the Macao authorities. European companies will be able to use this platform to communicate with the government on business environment and regulatory issues. The platform could also

provide Macao's authorities with a forum to seek views on relevant policies as and when required. The ultimate objective would be to contribute to Macao's economic diversification and long-term competitiveness.

As Macao suffers from acute shortages of labour and skilled managers, European companies rely heavily on expatriate staff and foreign workers. Obtaining work permits for them has proven difficult. The EU is willing to work with the Macao authorities and with the European business community to help identify areas of economic activity where the situation is particularly acute. Giving qualified professionals easier access to Macao's labour market would help boost its competitiveness.

As part of its agenda for fair taxation at global level, the EU pursued the work towards a common EU list of non-cooperative jurisdictions. During its preparatory work a "Scoreboard" was compiled based on a pre-assessment of all third countries. Macao was flagged on the transparency and the preferential Corporate Income Tax (CIT) regime risk indicators. The Scoreboard is not a preliminary EU list and does not entail any judgement of third countries.

The Macao European Chamber of Commerce (MECC)³ and the European Chamber of Commerce in Hong Kong jointly coordinated the large European participation in the Macao International Environmental Cooperation Forum & Exhibition in March and the Macao International Trade and Investment Fair in October. The MECC's role and relevance are expected to grow once the EU-Macao business-to-government dialogue has been set up.

The European Union Academic Programme, managed by a consortium led by the University of Macao, organised many new activities such as hosting visiting speakers, seminars, research and academic exchanges, the EU-themed short film challenge, a regular radio show on EU-related topics and a "Model EU" competition.

In the future, the EU will continue to deepen its relationship with Macao, increasing economic and trade links, improving cooperation with business and civil society and promoting mobility and exchanges with the people of Macao. Priorities include:

- greater cooperation to diversify Macao's economy;
- seizing opportunities arising from infrastructure projects and public procurement;
- maximising the potential benefits of the Closer Economic Partnership Arrangement between Macao and mainland China to the benefit of both local and European companies established in Macao;
- cooperating on legal and regulatory affairs, research and innovation, and continuing cooperation on trafficking in human beings.

³ The MECC is a hybrid chamber that has both direct company members and members from the national chambers of EU countries. It currently includes the British Business Association of Macao, the France Macau Business Association, the German Macau Business Association, the Irish Chamber of Commerce in Macau, the Macao-Romania Chamber of Commerce and the Portuguese-Chinese Chamber of Commerce and Industry.