

OFFICIAL REPORT OF PROCEEDINGS**Meeting of 26th February 1964****PRESENT:**HIS EXCELLENCY THE GOVERNOR (*PRESIDENT*)

SIR ROBERT BROWN BLACK, GCMG, OBE

HIS EXCELLENCY LIEUTENANT-GENERAL SIR RICHARD WALTER CRADDOCK,
KBE, CB, DSO

COMMANDER BRITISH FORCES

THE HONOURABLE EDMUND BRINSLEY TEESDALE, MC

COLONIAL SECRETARY

THE HONOURABLE MAURICE HEENAN, QC

ATTORNEY GENERAL

THE HONOURABLE JOHN JAMES COWPERTHWAITTE, CMG, OBE

FINANCIAL SECRETARY

THE HONOURABLE KENNETH STRATHMORE KINGHORN

DIRECTOR OF URBAN SERVICES

THE HONOURABLE ALEC MICHAEL JOHN WRIGHT

DIRECTOR OF PUBLIC WORKS

DR THE HONOURABLE TENG PIN-HUI, OBE

DIRECTOR OF MEDICAL AND HEALTH SERVICES

THE HONOURABLE WILLIAM DAVID GREGG

DIRECTOR OF EDUCATION

THE HONOURABLE DHUN JEHANGIR RUTTONJEE, OBE

THE HONOURABLE FUNG PING-FAN, OBE

THE HONOURABLE RICHARD CHARLES LEE, CBE

THE HONOURABLE KWAN CHO-YIU, OBE

THE HONOURABLE KAN YUET-KEUNG, OBE

THE HONOURABLE WILLIAM CHARLES GODDARD KNOWLES

THE HONOURABLE SIDNEY SAMUEL GORDON

THE HONOURABLE LI FOOK-SHU, OBE

MR GORDON ERIC MATHER (*Deputy Clerk of Councils*)**ABSENT:**THE HONOURABLE JOHN CRICHTON McDOUALL
SECRETARY FOR CHINESE AFFAIRS

MINUTES

The Minutes of the meeting of the Council held on 12th February 1964, were confirmed.

OATHS

MR W. D. GREGG took the Oath of Allegiance and assumed his seat as a Member of the Council.

HIS EXCELLENCY THE GOVERNOR: —We welcome you to the Legislative Council, Mr. GREGG.

PAPERS

THE COLONIAL SECRETARY, by Command of His Excellency the Governor, laid upon the table the following papers: —

<i>Subject</i>	<i>LN No</i>
Sessional, Paper, 1964: —	
No 14—Annual Report by the Director of Commerce and Industry for the year 1962-63.	
Draft Estimates of Revenue and Expenditure with Explanatory Memoranda for the year ending 31st March 1965.	
Report of the Public Works Subcommittee of Finance Committee for the year 1964-65.	
Hong Kong Annual Report, 1963.	
Registration of Persons Ordinance, 1960.	
Registration of Persons (Re-registration) (No 7) Order, 1964	27
Trade Marks Ordinance, 1954.	
Trade Marks (Amendment) Rules, 1964	28
Registration of Persons Ordinance, 1960.	
Registration of Persons (Cancellation of Registration and Identity Cards) (No 6) Order, 1964	29
Registration of Persons Ordinance, 1960.	
Registration of Persons (Re-registration) (No 8) Order, 1964	30

ADDRESS BY HIS EXCELLENCY THE GOVERNOR

Honourable Members: a leading columnist in a British newspaper not so very long ago seemed very concerned to array us as mourners on our own behalf. "Ah!" said Mrs GAMP, walking away from the

bed, "he'd make a lovely corpse". This is a sad occasion for me because I am presiding at my seventh and last Budget Session of the Legislative Council in Hong Kong, but it is in no way whatever an occasion for Mrs Sarah GAMP's ministrations. There is nothing moribund about Hong Kong or its people. The subject about which I am speaking is so young, vigorous and vital that I cannot imagine anything less accurate or less appropriate than an obituary notice with or without illustrations. I cannot imagine anything less in touch with the reality of the scene in Hong Kong, filled as it is by the liveliness, inspiration and achievement of its people. Governors may come and Governors may go, but Hong Kong goes on from strength to strength as it writes the proud narrative of a wonderful people.

Indeed it becomes more and more impossible to describe the extent and liveliness of Hong Kong's activities during the period of a year, so that I can only hope to touch on certain aspects this afternoon. If I may, I shall first comment on the international trading position, which is so important for the state of our economy. In 1963 our domestic exports rose in value by not less than 15½%, surpassing the previous year's increase over 1961. The reason for part of this increase is the higher selling prices for our exports, due to the greater value added in the manufacturing and marketing prices in Hong Kong, and this arose partly from higher qualities, partly from firm trading conditions. This is remarkable when you recollect our difficulties over water and the restrictions imposed on our two principal export markets, and we have to divide the credit amongst our industrialists, merchants, technicians, factory employees and Government policy, the policy of free competition and unfettered enterprise. And a fair share of this credit must certainly go to the expert work of the Director of Commerce and Industry and his officers.

There is much talk these days of the liberalization of trade, but, equally, the talkers hedge their remarks about with many reservations, none of which seems likely to help Hong Kong. There is the theory that Hong Kong is not a developing country, and that, if any new trading benefits are to be worked out for developing countries, Hong Kong should not necessarily share these. Perhaps this would not be objectionable provided there was acceptance of the ancillary claim that Hong Kong then is a developed country and should trade with other developed countries on the same non-discriminatory basis as applies to the conduct of trade between these other countries.

How are we coping with these conditions? Well, we have brought to a reasonably satisfactory conclusion long, complex cotton textile negotiations with the United States and with the British Cotton Industry, and we have succeeded in these because of close co-operation between officials, businessmen and industrialists. The Trade and Industry

Advisory Board, the Cotton Advisory Board, the General Chamber of Commerce and the Federation of Hong Kong Industries have given valuable help in these delicate, highly technical and often controversial discussions. We have also been fortunate in the number of individuals who have given up their time to undertake tiring journeys and engage in lengthy consultations in the interest of good relations and closer understanding with our trading partners. A notable mission during the year was that to the countries of Western Europe under the leadership of Sir Sik-nin CHAU. The General Chamber and the Federation, furthermore, have expanded their activities in commercial public relations. They have appointed a representative at large in Western Europe and will shortly open an office with another representative in New York. We have also been active in ECAFE commitments where we have plenty to learn and, I believe, much to contribute. In 1963, we became a member of the Asian Productivity Organization. I shall have more to say on our trading position later on.

The field of construction engineering saw much activity during the year. Private buildings completed were of the value of \$560 million, 70% more than in 1962. Government spent more than \$190 million on building works and it spent a further \$242 million on civil engineering and waterworks projects. So the total volume of work carried out by the construction industry in 1963 was of the order of \$1,000 million. In these circumstances it is not surprising that there has been a noticeable increase in building costs during the year.

It is estimated that, in terms of standard type accommodation, excluding resettlement the nett gain of people housed in permanent conditions during the year was 139,000. This certainly represents some headway, but the housing situation is acute. At the end of 1963 the authorized population of resettlement estates was just under 605,000, an increase of nearly 95,000 over the preceding year. There are probably also 40,000 in the estates who are additions to households, giving rise to an unwelcome degree of overcrowding. We still have not hit the target of 100,000 a year, but the Director believes that, given the necessary conditions, he can put up resettlement accommodation at a figure markedly above the present target. One advantage he now has is in the 16-storey block which should be in general use in all new estates and in extensions to existing ones. But despite the building under way, and despite all the efforts of the Resettlement Department under most difficult conditions, it became evident during the year that squatting was no longer being contained. There were several reasons for the upsurge of new squatters: the natural growth of population, the large influx of refugees during 1962, and the increasing displacement of tenement dwellers as a result of the redevelopment of old property in the private sector. The time had come for a reappraisal of the operations which, with minor adjustments and refinements, had met with a

large measure of success over a period of ten years, and, last June, I appointed a Working Party under Mr McDouall to advise on desirable changes of policy affecting resettlement, low-cost housing, the clearance of squatters and the provision of temporary resite areas. Four Unofficial members of the Urban Council and certain senior Government officials became members of this working party. They put in an immense amount of detailed work and have presented a valuable report. I am most grateful to the Chairman and to the members of this Working Party. The report has yet to be published but salient features in it are that, although the resettlement population is of the order of 645,000 souls, squatter population has increased since 1956 by 73% to about 580,000; that, if we resettled no more squatters we could expect their numbers to increase by 30,000 in a year's time; and that, if we are really to keep ahead under prevailing conditions, we shall have to accept a very marked increase in our building programme. And in this connexion, you are well aware that, quite apart from the claims on Government funds of other forms of housing, there is, of course, the difficult question of land. Our real objective must be to turn more and more to the planning of new townships in the New Territories. But it is not sufficient to build estates in new areas if there is no source of livelihood adjoining or within easy reach of the residents of such estates. We require planned townships of the kind on which we are already embarked at Kwai Chung and for which we have plans under consideration at Castle Peak and Sha Tin.

The programme for Government low-cost housing has gained momentum, and there should be housing for a population of about 76,000 before the end of this year. It is clearly very popular; at the end of last year the number of registrations exceeded 165,000, which, even allowing for many duplications, represents more than half a million people.

As you know the Government policy which the Housing Authority is carrying out relates to people with incomes between \$400 and \$900 a month, a group which it believes forms more than 30% of the Colony's urban population. The Authority has had an encouraging year and the total population of its 15,451 flats numbers 96,000. It now hopes it can carry out a programme for 53,700 flats to accommodate 328,000 people in the period of its ten-year plan. The estimated cost is \$470 million but the Authority believes that it will be able to finance this programme to the extent of \$100 million at least from surplus revenue. It is Government's intention to do what it can in support of this programme.

I might add here that the Housing Society continues to play its important role, and by the end of last year it had built altogether 7,363 flats housing 44,861 persons.

In our social welfare work we aim at more constructive services designed to strengthen and support the natural desire for economic and social independence. We have a great asset in the sturdy individualism and strong support within the family which are characteristic of the people of Hong Kong. The Social Welfare Department has received the Report of its three Consultants, with expert advice both on training for social work at the academic level, which the Universities and Government are now considering, and on in-service training, in which field the training unit, set up with an initial grant from UNICEF, has already shewn valuable results. We are only beginning to switch now from amateur to professional, and we must press on with more and more training. The Department is doing excellent and imaginative work, and we are fortunate in the co-operation extended by the voluntary agencies in meeting the challenge and in attempting to supply the new needs of the community.

There is one aspect of social work which maybe we do not immediately enter as a credit in our account, but it most certainly is. I refer to the enlightened administration of our Prisons Department. We have two training centres in being and one projected at Shek Pik. These will be sufficient to ensure that all offenders under 21 need not be sent to prison at all—and it is still a gaol sentence for them in most countries. We have two open prisons: Chi Ma Wan, for first offenders with sentences of 3 years and under, and Tai Lam, for convicted drug addicts with first-time sentences of three years and under; and we have two more on the way, one on Lantau and another near Starling Inlet, which will take reconvicted persons with sentences of 3 years and under. We hope that, within the next two years, all short-sentence prisoners will be in open institutions, which I think I am right in saying has been achieved nowhere else. And, while we do not claim to be anywhere near victory in dealing with drug addicts, yet more than half of the addicts trained at Tai Lam have not relapsed and have not been reconvicted for any offence. That spells progress. What the Commissioner and his staff have done has aroused international interest and most favourable comment.

1963 was notable for the opening of the Queen Elizabeth Hospital, for the enactment of the Medical Clinics Ordinance and for our acceptance in principle of the School Medical Service. For some time now we have been working on a programme of development of medical services and, earlier this month, we tabled a White Paper on this subject. We based forward planning to 1972 on certain population trends, on the evidence that a large part of the population cannot afford unsubsidized out-patient medical care or unsubsidized in-patient treatment, and we accepted it as our aim that, over the next ten years, we should try to provide clinic and hospital services to meet the most urgent medical and health needs. We intend to follow this report as a general

route rather than as the tramlines to our destination. The financial considerations are serious. If we are to meet the target of 7,100 additional hospital beds within the decade, it will mean an increase in the current expenditure from just over \$100 million to \$320 million, and the capital cost of the works would be \$380 million. A planning committee is now in position to keep the programme under constant review.

The main object of our Medical Clinics legislation is to assess the work of clinics maintained by those who claim to give adequate medical service at low cost to the under-privileged. Eventually, we hope on the one hand, to preserve the genuine charity clinics and, on, the other hand, to eliminate those which, under the guise of charity, are operating as commercial undertakings on a profit-making basis. We shall appoint a committee to review the working of the Ordinance after it has been in operation for 18 months, and we shall then analyse the information obtained and decide on the role of these charity clinics in the general provision of medical care in Hong Kong.

For the projected School Medical Service, we now have a provisional Board which will advise on the measures necessary to bring the service into operation by September of this year.

During 1963 it became clear that Cholera El Tor, which had become widespread in the region, was now endemic. There were in all 115 patients, of whom 6 died, two deaths being attributable to other causes. The outbreak itself lasted from June until December, and we must expect cases at any time in the year, although they will probably be more numerous during the warm season. It is most important for all of us to protect ourselves and our families regularly by inoculation against its re-introduction into the community.

The outstanding development in education during the year was the birth, following the valuable report of the Fulton Commission, of the Chinese University, a federation of Chung Chi, New Asia and United Colleges. Thanks to the work of the Provisional Council set up in June, under the dynamic chairmanship of Mr C. Y. KWAN, we were able to inaugurate the University in October. We are fortunate to have Professor LI Choh-ming as Vice-Chancellor, and I wish him and our new University well. The achievement is notable, the set task challenging, the prospect immense. I have no doubt of the ultimate success of this new university; its foundation has been welcomed in other parts of the world.

The success so far achieved in the establishment of the Chinese University owes not a little to the wholehearted co-operation that its sister university has given. I am particularly pleased at the excellent relations existing between the universities. The University of Hong

Kong itself has continued to expand during the year, but perhaps more remarkable is the high standard reached by numbers of students who are proceeding to higher degrees and awards. The University already has an excellent reputation for the quality of its graduates, and there has been a notable procession of students who have obtained higher academic qualifications. Over 150 graduates are reading for higher degrees at the University.

Our industries need not only the technologists who are the normal product of a university but also technicians, supervisors and craftsmen. For these we continue to depend largely on our Technical College which, last September, had a total enrolment of over 9,500 full-time and part-time students. Furthermore, the general question of apprenticeship training has been under detailed study by a standing committee and the Labour Advisory Board has, in general, endorsed its recommendations. Consultations are to take place shortly with industry with a view to improving the conditions of apprenticeships as well as the standards of training given. It may be possible to extend the machinery proposed for apprenticeships to cover the broader field of vocational training, so that we can assess the full needs of industry for skilled manpower and we hope to meet them on a common basis whatever the length of the training period.

During the year a Commission visited Hong Kong to report on the education provision in the Colony. Its members were both from Hampshire—Mr R. M. MARSH, the County Education Officer, and Mr J. R. SAMPSON, the County Treasurer—and we are grateful that they could be released to come for this study and also for the work they put into the preparation of their report. We have published this and now a Working Party, with Government and non-Government members, the latter in the majority, is studying the recommendations. In the meantime, there is no question of placing a general moratorium on educational development. The enrolment both in registered primary and secondary schools continues to increase, and the scheme for the re-organization of primary and secondary education took effect in September 1963.

We must all be watching with interest the part which the City Hall is playing in the life of the community. Since it was opened it has been in almost continuous use for a wide range of activities. I am afraid I do not have time to describe these, but it is fair to say that the City Hall has centralized a number of cultural activities covering the library, the museum and art gallery where exhibitions are held, the theatre and the concert hall, and that there has been noticeable a growing interest in the various national cultures which are represented in Hong Kong. The presence of young people of all races at various functions is an encouraging sign. I believe that the City Hall has

stimulated and quickened cultural life in Hong Kong, and that this mutually inter-active state of affairs should greatly benefit the community.

I referred earlier to major construction works but I did no more than mention water which, this year, calls for rather fuller comments. A critical shortage of water has overshadowed our lives for the past 10 months. We have been passing through a period of extreme peril, and we are not yet out of danger. This crisis has been a further test of the character of our people, and what a splendid response they have given: the calm and orderly behaviour of the ordinary men and women queuing at standpipes during the hot summer months; the ingenuity with which factories and businesses of all kinds have kept going on very limited supplies: our Government servants, particularly in the Public Works and Marine Departments, who have worked tirelessly and resourcefully to meet and surmount the problems which the crisis has presented. At the beginning of the summer there was a hint of criticism over the adequacy of Government's long-term water planning. I believe that most people now see the crisis in its true perspective. There is no need for me to recount the huge and costly reservoir projects, some complete, some still in progress, on which we have embarked since the war. And you are all only too well aware, from frequent and recent references, of the most immediate projects such as the completion of the Shek Pik reservoir last October, and our advance into the next stage of the Plover Cove Scheme. Even if we had decided some years ago to invest in desalinization, and on a greater scale than previously contemplated anywhere else in the world at that time, we would not have escaped the effect of last year's exceptional drought. In the final analysis, because of our massive requirements, our resources depend to a very large extent, and will continue to depend, on the amount of rainfall we can store. And so the drought of 1963 created a major emergency: a year in which rainfall was 10" less than the lowest figure ever recorded by the Royal Observatory. Continuously for 14 months we received less than average rain, and over this period we recorded only 36" against an average of 87" .

Hong Kong has faced drought periods before, but never so prolonged or so serious. Hong Kong has imported water before, but never on the present scale nor at such cost; indeed, I wonder whether any territory has ever embarked on an operation of this nature and magnitude, literally to preserve its existence. In Hong Kong we mounted it in just over one month. From July onwards until the end of January with the much appreciated help and co-operation of the Chinese authorities we have been sending between 8 and 11 tankers to the Pearl River continuously, and during that period they imported 2,240 million gallons of water. The significance of this operation is clear when you consider that, over the same period, our consumption was

only about 7,000 million gallons and that, during the winter months, the tankers were, and still are, providing us with about one-third of the water we consume.

I wish to pay tribute again to the committee, under Mr ROBERTSON, who initially studied the problem and recommended the most effective methods of importing water, and to Mr TRENERRY, Government's General Agent whose expert advice has been invaluable in the chartering and operation of the tanker fleet. Time does not permit me to recount in detail all the difficulties faced and overcome in introducing and perfecting these unprecedented measures. You may read about them at greater length in the Annual Report now in your hands. A Water Emergency Committee has been meeting every week since the beginning of May to oversee and to report to the Executive Council on all aspects of the crisis. Sub-committees have dealt with detailed facets of the emergency; for instance, the problem of additional supplies for essential industries, the satisfactory berthing of tankers and the passage of their precious cargo through thousands of feet of hastily laid steel pipes, the complex chartering on a steadily rising world market of ships of suitable draught and pumping capacity, and the planning of continuous schedules of voyages to the Pearl River against operating problems and difficulties of salinities. The Colonial Secretary, Mr TEESDALE, has been Chairman of the Committee and, in addition to the admirable direction which he has given to its work, he has proved most resourceful and completely indefatigable in co-ordinating the work of all those engaged in dealing with the emergency. I commend him most warmly for the part he has played and is still playing. The story of the handling of this emergency is a fascinating one, revealing energy and ingenuity unified in a determination to keep our supplies of water from falling below the present critical level. In addition, the Public Works Department turned their efforts to a variety of projects to bring more water into use. They assembled pumps on the Indus River, and, over a period of 7 months last year, 1,700 million gallons of water which would not otherwise have been available have been pumped into our distribution system. The Department arranged for the sinking of wells near the Shum Chun River and these have already contributed over 100 million gallons. Later in the year wells were sunk in the urban areas to replace water obtained from streams in the New Territories on which so many of our small industries were dependent and which were showing signs of drying up. The Fire Brigade and Auxiliary Fire Services laid down 15 miles of pipeline, most helpfully provided from England, to bring into use seawater rather than fresh water to fight fires. Our four-hour period of supply every fourth day presented acute problems of distribution, and these the officers of the Water Authority have largely overcome by careful and regular rearrangement of zones in order to meet complaints of inadequate pressure with the minimum amount of delay.

The cost of all these measures and of many others which there is no time to describe has been very heavy indeed. The latest estimate up to 15th February gives a figure of about \$38 million. There could have been no way of saving this expenditure if we were to avoid individual rationing with all that implies and the gradual closure of a major part of our industrial capacity. I cannot speak too highly of all those who worked unremittingly to avert this catastrophe and of the people of Hong Kong who have borne with patience, fortitude and uncomplaining good humour the restrictions which we have been forced, in the public interest, to impose for so long.

I commented earlier that I would have more to say about our trading. Our trading has achieved a maturity which now makes an impact on the economies of other nations and compels us to seek an adult relationship with the reality of international trade. The past six years since 1958 have seen an unparalleled economic expansion in Hong Kong. Although, as yet, we have no national income statistics, everything points to the economy expanding at between 10% and 15% a year compound during at least the last four or five years of this period. It is also apparent that individual incomes have increased very significantly although, because of our growth of population, not quite in the same proportion. The population has increased by about 37%. Total exports have increased by 60%, re-exports of Hong Kong products by about 90%; this figure, of course, rather under-states the real increase in earnings, because exports now include a much higher proportion of Hong Kong content. The number of registered factories has increased by 30%, but their average size is much larger as employment in them has risen by 135%. Industrial wages have increased by about 60%, while the retail price index, which in 1958 stood at an average of 117 now stands at 124. Electricity consumption has grown by about 100%. Recurrent revenue, with only minor tax changes, has more than doubled, and capital revenue has increased six-fold as a consequence of the boom in land values. Bank deposits have risen by 300%, and bank advances to commerce and industry by rather more. Surely this is an astonishing picture of sustained growth? I wonder whether it is matched anywhere else?

What are the causes of this momentous development, and in what state has it left our economy, and with what prospects? It is not in Hong Kong's nature to be over-introspective, or retrospective, and only professional economic researchers could do justice to the theme; but I should like to comment on one or two features of it.

The mainspring of our growth has clearly lain in the qualities of our people, their thrift, industriousness and quickness to react to economic stimuli—all old-fashioned virtues. And these have been given

full scope by the economic environment we have maintained in Hong Kong: a stable currency, low direct taxation, freedom of enterprise, and absence of governmental control or interference with the free interplay of the forces of the market. These have been and remain the preconditions of our ability to overcome the handicaps that nature and geography have imposed upon us, and, in the pursuit of these, Government's general policy is well known and constant. We are doctrinaire about it only to the extent that we shall not change it unless it can be shewn that such change will bring benefit to the people of Hong Kong.

Looking back, it seems that world circumstances were particularly propitious to our sudden burgeoning. The scars of the Korean War had healed; our economy had adjusted itself; we had laid firmly the foundations of a new model of industrial economy. And, at this time, when our older markets were shrinking, or, at least, developing little further, we discovered the markets of the developed world—and they discovered our industrial possibilities. This was a time when these countries were themselves finally emerging from the problems of the immediate post-war period into a new phase of more liberal trading practices, and, in the case of America, a time when Japanese trade development had been halted in many fields. These markets were richer and more stable. Their established channels of marketing and distribution were ready and open to us, once we had demonstrated that we could produce what they wanted in the right quality and at the right price. If I were to single out one industry as having given impetus to this new trend, it would be the garment industry, which was especially well placed to take advantage of the opportunity; it required little capital and was, even in the West, still a labour-intensive industry. The trend, however, spread widely and rapidly to other industries.

These markets have given us greater security, not only because they have diversified our outlets, but also because they are in themselves more firmly fixed and have greater consuming power. Furthermore, while the developing countries are anxious to replace our simple manufactures with their own, the developed countries are, by and large, in spite of our experiences in some fields, notably cotton textiles, resigned to our manufactures replacing theirs, within decent periods of readjustment, while they themselves move forward into more and more complicated and capital-intensive production. It is this progress in the West that has given and will continue to give us increasing chances for our development, either on our own or in partnership with them. We must follow closely in their wake, although we can never hope to catch up with them because our only competitive advantage is clearly lower labour costs; I do not see how we can compete on the basis of capital-intensive industry. But if we are to tread on their heels we

ourselves shall have to develop progressively into technically more complicated processes and into higher quality ranges. This is our task now and we must get on with it.

The other phenomenon is that expansion has taken up most of the slack in our economy, in terms of employment and finance, and, for that matter, of such land as we can develop at once, although we had taken steps some years before to prepare for this. Indeed, it has introduced elements of stress and strain from over-extension. We can note this in many sectors both public and private. Examples are the rapid increases in real wages and in the rise in rents and land values. This does not mean that we are as yet employing all our resources to the full or to the best advantage. There is a large reservoir of labour in self-employment, for example. Maintained expansion and rising wages should continue to draw these people into more productive employment.

Some may fear that this inflation will push us out of our markets. But, provided we remain true to our liberal policies, are we really justified in such fears? In our conditions cost inflation is in general a sign of increased prosperity and of maturity. The full stretch of our economy has had the effect of mitigating the phenomenon by which, in the past, we have sold our products at below what the buyer would willingly pay because we have been in competition largely with ourselves. It is a good thing, surely not a bad thing, that our prices should be forced up to correct world competitive levels by the high tension of our economy; and socially and politically it is most valuable that labour should enjoy so large a share of the increment.

Are we then not in danger of going too far? I do not think so: the laws of the markets ought to prevent this. In other countries artificially stimulated internal demand is the thing that feeds inflation. The demand for our product lies abroad and we cannot ourselves artificially stimulate and maintain it. If our prices are tending to go too high, we can no longer sell, and our costs must fall, or cease to rise, until we are in a competitive position again. This may, at times, cause painful and immediate readjustment, but we may be able to make the necessary adjustments by increasing productivity rather than by decreasing wages or similar devices. High wages stimulate labour-saving developments and expectation of profit is, shall I say, an explosive widener of bottlenecks. One condition, however, must be that we retain our flexibility, that we react swiftly to changing conditions; which means allowing free play of market forces. May we not regard cost inflation, caused by high export demand, as a consequence of increasing prosperity rather than as a premonition of ruin? Does it not assure us that we are not selling our skills and our resources to the rest of the world too cheaply?

May I relate this to our social development in the context of the economy? In spite of 120 years of commerce, the development of industry and if industrial exports to the West created a new situation for which we were not quite ready, a new role in world trade which we did not quite understand. We were not aware of the attitudes of our fellow industrialists in the West; we were not aware of the problem we posed for them or of the strength of their reaction. We did not fully realize the importance of meeting them with a united front, laying aside our own internal rivalries. I think we have come a long way since 1958 in our understanding. Industry may not yet speak quite with one voice on all matters, but it recognizes the need to speak with one voice. Although it resents some of the reactions of other countries, it takes in the background of these reactions and the political limitations on complete freedom of trade; and it accepts that the preservation of freedom may entail some limitations on the abuse of it. These are all difficult matters, but I believe that we have now reached adult maturity and have a recognized, and often respected, place in the councils of world trade.

What are our prospects? There seems no reason why we should not go on to even greater prosperity, provided we remain true to our liberal policies. There will be much for everyone to do, Government, industry, commerce and labour. We must find more land for industry; we must have more technical education to equip us for technological change; we must make our voices heard in the market places and in the councils of the world. Above all we must do nothing to lessen the incentives to enterprise or stunt or misdirect its free and full deployment.

Economic progress, of course, is not an end in itself. Its *raison d'être* is to enhance the well-being of the whole community. All who participate in industry, in the community services and retail sectors of our economy and make expansion possible must share the fruits of progress. Our basic aim is to raise the standard of living of our people, and I do not accept that we have failed to make progress, despite the enormous problems which we face, problems intensified by the high rate of natural increase and by the necessity thrust upon us from time to time to absorb exceptionally large numbers of immigrants. Those who have lived in Hong Kong for any length of time cannot fail to have observed the steady increase in the general standard of living. The best guarantee of social progress in Hong Kong is full employment in an efficient and expanding economy which not only permits but also promotes a process of levelling up rather than levelling down. We must, therefore, always carry through extension in the field of social legislation with a close eye to its effect on economic expansion; and, in our context economic expansion means primarily expansion of exports. The uncertainties of international trade, which we face at all times, and the need for flexibility in our industrial structure to enable

us to react quickly to changing conditions, these prevent progress in this field from being as rapid or as continuous as ideally it should be, but our aim remains to ensure that we continue to move forward and that we create and maintain conditions where the benefits of our increased productivity are shared benefits.

I have spoken at too great length, I fear, but, before ending, I should like to say once more how grateful I am to my Unofficial colleagues on Executive and Legislative Councils, to the nominated and elected Unofficial members of Urban Council, who do so much valuable work for the community, and to all the members of the community who serve on our multifarious committees and take part in our social services in so many fields, and, not least, to the Civil Service which has rendered sterling, imaginative and loyal service to Hong Kong. Hong Kong is very fortunate in the high standards which its Civil Service maintains and in the high state of efficiency and morale of its Police Force. It has been an inspiring experience for me to serve in Hong Kong: a wonderful association and partnership in the work of integrating all within the community, of rehabilitating the handicapped and the under-privileged, and of diversifying and intensifying industrial production. If Hong Kong were a ship, and I had to say whether or not it was seaworthy, I would certify that it was: "100 A1 at Lloyds". (*Applause*).

RESOLUTION REGARDING THE DRAFT ESTIMATES OF REVENUE AND EXPENDITURE FOR 1964-65

THE FINANCIAL SECRETARY moved the following resolution: —

Resolved that the draft Estimates of Revenue and Expenditure for 1964-65 be referred to a Select Committee composed of the Colonial Secretary (*Chairman*), the Financial Secretary and all the Unofficial Members.

He said: Sir, last year I began by saying that it would be a rather unexciting budget. I am happy to be able to say the same again this year. Indeed, I find it a little difficult to find new things to say or new topics to discuss, so steady and continuous is the upward line of our progress. I am tempted to recite the plain figures and leave them to speak for themselves. I will not, however, let honourable Members off with that, but in any event I can hardly avoid being somewhat repetitious.

I will start as usual with the final results of the last complete financial year, 1962-63. The revised estimates suggested a surplus on general account of \$41 million, but I said at the time that I could not see the surplus coming out at less than \$100 million. The final figure

was in fact \$140 million. This, together with appreciation of investments amounting to \$26 million, raised the general revenue balance to \$659 million at 31st March 1963. The Revenue Equalization Account remained at \$138 million so that total reserves were \$797 million or rather less than eight months revenue at that time.

For a complete picture of financial operations on public account the Development Loan Fund's results must be added. They showed an excess of expenditure over receipts amounting to \$17 million which reduces the overall surplus from \$140 million to \$123 million.

I now pass to the current year. The original estimate of revenue was \$1,197 million and of expenditure \$1,360 million, giving a deficit of \$163 million.

Actual results have followed the course with which we have become familiar in recent years. The expansion of the economy has continued at a rate which appears to be somewhere between 10% and 15% and has resulted in a similar expansion of revenue. I said last year that, while we could not plan on this happening and must relate the estimates to a reasonably normal rate of growth, I for one would not be surprised if it did. The revised estimate of revenue is now \$1,354 million or \$157 million more than the original estimate for this year, and \$101 million, or 8%, more than the actual figure for 1962-63. For recurrent revenue alone the increase is 12% compared with 10% in the previous year. This is, of course, with no change in rates of taxation, although there have been some minor changes in fees. Capital revenue has maintained roughly the exceptionally high rate of the previous year.

Increases have been fairly widespread throughout the range of sources of revenue, particularly those reflecting economic activity and consumer spending.

Earnings and Profits Tax, which reflects the activities of the previous year, has been particularly fruitful. The revised estimate is \$262 million; this is \$39 million over the original estimate and \$47 million, or the exceptionally large increase of 22%, over the previous year's level. Some of this increase may have to be discounted because the change in property tax arrangements introduced three years ago has not worked out its effects yet, and more tax than usual collected this year may have to be refunded next year. But even so it appears that 1962-63 was an even more prosperous year in terms of earnings and profits than we had supposed.

Stamp Duty has recovered from its slight depression of last year, largely owing to activity in the property market; assignments have produced an extra \$7 million. Last year's total for all stamp duties was \$53 million; this year's revised figure is \$62 million, a 17% increase.

Duties on liquor, tobacco and hydrocarbon oils have also all done better than expected. I have revised the estimate on liquor upwards by \$7 million to \$59½ million and on tobacco by \$8 million to \$94 million. These are 15½% and 10½% respectively over last year's figures; and this although certain changes in assessment introduced by the new Dutiable Commodities Ordinance during the course of the year cost somewhere between \$2 million and \$3 million in tobacco duty.

On hydrocarbon oils the original figure of \$60 million has been revised to \$64 million, or about 10% over last year's level. This is partly due to the suppression of the misuse of non-automotive diesel oil for automotive purposes. I spoke last year of the abuses which were then prevalent and of our doubts whether the colouring and marking device would be effective in preventing them. The introduction of the Dutiable Commodities (Marking and Colouring of Hydrocarbon Oils) Regulations in October 1963, which gave teeth to the device, and the development by the Government Chemist of new tests for the detection of tampering, have fortunately proved very effective. The Preventive Service have done an excellent job and numerous successful prosecutions have taken place both for using non-automotive fuel illegally and for tampering with it. It seems that evasion of duty was taking place before this to the extent of nearly \$5 million a year, but the revenue position now appears to be satisfactory. There is therefore no need to consider further the idea I mentioned last year of replacing the duty on diesel fuel with a substantial increase in the annual registration fee for diesel vehicles. The way is also clear for bringing the rate of duty on diesel fuel up to that for petrol—but I have no intention of proposing it this year.

The estimated yield from interest on surplus funds has been raised from \$42 million to \$52 million. This is due to a variety of reasons, one being the further accumulation of surplus funds instead of their expected running down.

Land sales were conservatively estimated at \$146 million compared with the actual figure of \$208 million last year. The estimate has now been revised substantially upwards to \$190 million. This revision mostly represents an increase in premia received from modifications of lease conditions, from exchanges and from lease renewals. Premia on new leases will be close to the original estimate, at a figure about 25% below last year's level; this partly reflects the temporarily depressed market for residential land in some higher class areas.

The original expenditure estimate of \$1,360 million has now been revised to \$1,315 million, a figure which, if realized, will be \$201 million or 18% above last year's level. Of this total \$52 million represents special expenditure on the water emergency, but the increase

on normal activities is the still substantial sum of \$149 million or 13½%. I am doubtful, however, if the final figure will quite reach this level, but it should not be far short.

The shortfall on originally estimated expenditure is \$45 million or, if the water emergency is not taken into account, \$97 million. If the revised estimate is reasonably correct, this will have been slightly closer estimating than last year, a difference of 7% compared with 9%.

The main shortfall (more than two-thirds of it) is, once again, I fear, in Public Works Non-Recurrent, where the original estimate of \$509 million has been revised downwards to \$439 million (excluding the water emergency), which by a coincidence is within \$1½ million of the original estimate for 1962-63. This compares with actual expenditure of \$378 million in 1962-63 (and \$282 million in 1961-62) and is rather disappointing particularly as costs have been rising. Architectural work for which the Department itself was responsible was well up to the estimate but private architects' work fell very short and expenditure on engineering works, both general and on water projects, has been well below the original estimate. There have been extenuating circumstances in that the water emergency has diverted much time and energy; and I would not blame my honourable Friend the Director of Public Works either for this or for any over-estimate of expenditure, as he was not responsible either for last year's estimates or for last year's weather.

Other sources of under-spending are scattered through the departments and reflect the difficulties in the way of a rapid expansion of the government machine, particularly in an economy itself rapidly expanding and pre-empting a large share of available resources. This under-spending is understated by the results as there was an increase during the year in the wages of certain artisans and lower grades estimated to cost \$8 million for the year.

The revised estimates for last year therefore turn the original deficit of \$163 million into a surplus of \$39 million. I suspect that it will in fact be nearer \$75 million, and for comparative purposes we should really add the \$52 million spent on the water emergency. This gives a swing from estimated deficit to actual surplus of similar dimensions to that of last year—for which I once again do not apologize. Of the estimated swing of \$202 million, \$157 million represents an under-estimate of revenue and \$45 million an over-estimate of expenditure. This latter figure corrected for the water emergency is \$97 million. Last year's actual swing between original estimate and final out-turn was \$304 million compared with a now estimated, corrected figure of \$254 million for this year.

To complete the picture two other public accounts must be brought into account. Firstly the revised estimates of the Development Loan Fund, which are at Appendix III in the draft Estimates, show an excess of payments over receipts amounting to \$60 million; and secondly the transferable surplus accruing to the Exchange Fund during the year is of the order of \$50 million. When added to the general revenue account these produce an estimated surplus on all public financial operations of approximately \$29 million. This is a small sum in relation to the scale of our current operations although, as I have said, it may turn out rather larger.

Now we come to the next financial year, 1964-65. The draft Estimates have been in the hands of honourable Members since last week.

My estimate of revenue next year at current tax rates is \$1,376 million compared with this year's revised estimate of \$1,354 million. The difference between the various elements of these figures is shown on pages 195 and 196 of the Memorandum on the draft Estimates.

The estimate of recurrent revenue is based once again on a reasonably normal rate of growth taking into account such factors as population growth and increased Government activity. It is certainly conservative in that it does not presuppose a continuation of our recent exceptionally rapid rate of growth, although it does assume rather more than the maintenance of the levels reached by the extensive growth of recent years. It would not be prudent to bank on a continuation of our current economic miracle into its fifth year although the signs are favourable at the present moment.

The biggest margin for probable error is, as it has been for the last two or three years, in capital revenue from land. This has been estimated at \$154½ million compared with actual revenue of \$208 million last year and this year's revised estimate of \$190 million. It is not expected that lease renewals will bring in so much as this year. Demand for industrial land remains strong but most of that is sold on instalment terms. The demand for residential land has recovered a little, but the estimate assumes a slight fall in premia on new leases for all purposes. I am hopeful that this is an under-estimate; but much depends on the rate at which we are able to put on the market land ready for development.

Earnings and Profits Tax has been put at \$279 million compared with a revised figure of \$262 million this year. This reflects this year's good business results; but there is the uncertainty I have already mentioned about refunds of Property Tax, and the true increase this figure represents may be greater than appears.

There is very little worthy of special mention in the other revenue heads, but I might draw attention to a re-arrangement whereby all revenue connected with the Airport and Air Services has been grouped into a single head—Head 9. Total revenue from these sources is estimated to reach nearly \$19 million. The setting up of a system of pro-forma accounts for air services has nearly been completed. Preliminary figures suggest that revenue is now approximately covering the cost of services before any charge is made for land occupied by the Airport. Clearly a notional charge should be made for the extensive and valuable area of land occupied but it is not easy to determine exactly what it should be.

Expenditure is estimated at \$1,494 million or \$180 million more than the revised estimate for this year. It represents the continuation of, for the most part, already programmed expansions of Government activity over its whole field.

The estimate for personal emoluments at \$432 million is \$52 million over the revised estimate for 1963-64. The corresponding figure last year was \$55 million, although the increase may in fact turn out to be only \$45 million. I must pay a tribute again to the Establishment Committee for their labours in scrutinising requests for additional posts and to the staff of the Establishment Branch of the Colonial Secretariat for their work in the same field. Their work eased mine very substantially. These estimates of personal emoluments do not, of course, take into account the cost of any increased emoluments which may be granted to the public service as a whole in consequence of its current claims.

Other recurrent expenditure is put at \$436 million or \$44 million over the revised estimate for this year. The corresponding figure last year was \$41 million, although the increase looks in fact like turning out at \$45 million. As usual a considerable part of this increase represents increased subventions in various fields; the total increase is \$16½ million, of which Educational Subventions account for almost three quarters. Non-recurrent subventions are \$5½ million higher than last year. There is a larger than usual increase in Social Welfare subventions, amounting to about \$1,160,000 or 26%. The increase in the previous year was \$650,000. The total estimate for Social Welfare subventions is \$5,634,000.

The biggest increase is again in Public Works Non-Recurrent where the estimate is \$548 million (not counting a final, I hope, \$15 million for the water emergency) compared with the revised estimate of \$439 million this year. The amount for the categories of buildings and engineering are roughly the same as for last year, but waterworks is up \$31 million to \$158 million. The total Architectural Office figure of \$250 million includes an increase in expenditure on Resettlement housing from \$72 million to \$106 million.

The Public Works Sub-Committee has carried out its thrice yearly reviews of the public works programme and its reports of these reviews are in the hands of honourable Members. I must express my gratitude to the sub-committee for their assistance and advice.

Two matters considered by the Sub-Committee during the year are worthy of special mention. The first concerns the effect of rising labour costs on tendering by contractors for Government projects. It appeared that they were reluctant to tender or, if they were prepared to do so, were tending to over-price their bids substantially as a reinsurance against large-scale increases in these costs. Arrangements were agreed for a modified labour cost variation clause in building contracts. The clause appears to have achieved its object.

The second matter was a review of the engineering capacity of the Public Works Department in relation to the work it was being asked to undertake. A similar review of architectural staff had taken place the previous year. This led to recommendations for increases in staff which were accepted. In the light of the success this year of the architectural side of the Department in reaching its planned output, it may now be time to review its staff again.

As usual, the question presents itself whether the target of \$548 million can be met. This is the first year that my honourable Friend the Director of Public Works has himself been wholly responsible for the estimates. He is reasonably confident that the target can be attained if all goes smoothly. An increase of \$109 million in spending in one year is in fact not much greater than the actual increase of \$96½ million between 1961-62 and 1962-63. But, the more particularly if spending on private works continues at its current level, I cannot help fearing that we will fall significantly short of the target. It is not easy to expand operations to this extent at a time when the construction industry is already at full stretch. I have wondered at times if there was a case for restricting private development, for example, by licence, in order to ease the achievement of the public programme. But this would be foreign to our philosophy and in any case the industry has shown remarkable ability to expand under the stimulus of demand. But we have to be careful not to push it beyond the limits of its ability to expand or we will merely raise expenditure without achieving a real increase in output.

The difference between estimated revenue and estimated expenditure is therefore an estimated deficit of \$118 million, which is rather less than in recent years. No doubt this result will be looked on with some scepticism and I must confess that I share that scepticism, or rather optimism. Although I cannot suggest at all confidently what the actual result will be, I think it will be rather better than this. Those who criticise mis-estimating misunderstand to some extent the nature

of the annual estimates. On the expenditure side their main function, particularly in times of full public coffers, is the control, in some, but not excessive, detail, of expenditure of public funds on agreed programmes and objectives within the practical limits of efficient and economical expansion. Now, while I have a shrewd idea, on the basis of experience, what total expenditure on all counts may be, the uncertainties about the multiplicity of individual heads and subheads of expenditure is such that I cannot tell precisely where it will fall. But the annual estimates are intended to determine as far as possible the pattern of Government spending for the year and each head and subhead of expenditure must be provided with an adequate sum to carry out its intended purpose. If they were not, I would have to come back to Finance Committee time and time again during the year for supplementary provision and the control of expenditure by this Council would be dispersed and diminished. There is in consequence a tendency to over-provide in total. This tendency has been modified by provision for virement between certain subheads and by arbitrary cuts in departmental estimates where I have felt it reasonably safe to make them; but it still persists to a substantial extent.

Revenue estimates are intended to show whether or not, on a reasonable view of the future, present taxes are likely to be adequate—or excessive, taking into account reserves and the possibility of borrowing if appropriate, to meet the calls upon the public purse. The difficulties here are of a different nature. The estimates depend almost wholly on judgement of future developments outside Government control and it is easy to be wrong for there is little to guide one, particularly in Hong Kong's rather volatile and undirected kind of economy. In general, in an era of rapid expansion, there is a tendency to under-estimate, and it is, indeed, only prudent to err in this direction. This is particularly so when, as at present, economic expansion has been unprecedentedly rapid and prolonged.

The estimated deficit or surplus is then, in a sense, merely the mathematical resultant of the separate revenue and expenditure estimates. As I have seen it written recently a propos of American budgetary technique (although in a slightly different context), the state of the economy determines the deficit—or surplus, as the case may be. In our present economic state there is usually reason to suspect that the actual results will be significantly better, and to hope that they will be substantially better than the figures suggest. For these reasons we have never in recent years used our estimated deficits as a justification for substantially increased, taxation, nor, conversely, to reduce the rate of expansion of the public service. I shall say something later about longer term considerations which are both more important and more speculative.

In a period of financial stringency things are different. Estimating becomes much tighter, not only because of the greater need for economy, but also because the limitations on expenditure tend to be financial, not physical, and departments have little difficulty in spending to the hilt. That it one of the reasons why a Financial Secretary's life is paradoxically easier when money is scarce than when it is plentiful; he is riding with a tighter rein.

Economists of the modern school will no doubt protest that I have said nothing of the use of budget deficits or surpluses for the control of the economy in general. I doubt if such techniques would ever be appropriate in Hong Kong's exposed economic position; and I think they are certainly not appropriate at present, when in strict orthodoxy they would suggest the need to plan for a very substantial surplus "to take the heat out of the economy". Although we have in fact run substantial surpluses in recent years we have not done so with deflationary effect because we have not removed them from the economy but have left them inside the Colony's banking system to continue to work for the economy. \$500 million or 55% of reserves are so held at present.

I should add at this stage, for the sake of completeness, that the estimated deficit on the operations of the Development Loan Fund next year is \$66 million; and a rough guess at the surplus from the Exchange Fund is \$45 million. These two figures would increase the estimated deficit on total public account to \$139 million.

There is one point about the Development Loan Fund I might mention. Now that legislative sanction has been given for the transfer of surpluses out of the Exchange Fund, a first instalment of \$150 million is being transferred from that Fund to the Development Loan Fund, leaving a transferable surplus balance of about \$248 million still available. Of the \$150 million, about \$80 million goes at once to extinguish an advance from general revenue; the remainder should see the Development Loan Fund through to the end of the next financial year. As honourable Members are aware, the Fund is used principally for the finance of housing and of school construction.

I have confessed that I do not really believe in a deficit next year as large as \$118 million. With that belief and our present reserves, there is clearly no justification for any increase in taxation for general revenue purposes this year and I do not propose any. There are, however, two matters that I must take up.

The first concerns tobacco duty. The Dutiable Commodities Ordinance which was passed in October last year introduced a change in the practice of assessing duty on imported cigarettes. The practice was previously to charge duty on the gross weight, that is, on the weight

of the paper, glue and filter, if there was one, as well as on the weight of tobacco. In the case of locally manufactured cigarettes, however, the duty was (as it still is) levied on the raw tobacco before manufacture. This did not have much practical effect in the days before filter tips became fashionable but their advent introduced a substantial element of preference (about 10%) for filter cigarettes manufactured in Hong Kong, in inadvertent breach of our policy of no protection.

Normal practice elsewhere is, I understand, to charge duty only on the net weight of tobacco and provision was made to this effect in section 65 of the new Ordinance. The effect of this change was two-fold, first and less serious, it removed the element of adventitious protection from domestic manufactures; second and more serious, it meant a loss of duty of something like \$4½ million a year at present consumption levels.

I did not propose a compensating increase in duty when the Ordinance was passed because there was a possibility that I would have to propose a further substantial increase at Budget time and I did not want to do it in two steps. Also revenue was coming in well without it.

I propose, however, that duties should now be increased so as to bring in roughly the amount of revenue lost. The full increase in duty on imported cigarettes necessary for this would be just over one dollar a pound or about five cents a packet of twenty. I propose, however, that the increase should be only 80 cents a pound or about four cents a packet of twenty. I trust that the trade will not pass on this increase to the consumer. I am not aware that they reduced their prices when the change was made last year. I propose at the same time that the duty on raw tobacco for local manufacture should be increased by 25 cents a pound or about one and a quarter cents a packet of twenty; this will make up the remainder of the lost duty (plus, I must confess, about \$1 million more) and the net effect will restore only in part the protection which has fortuitously arisen in recent years. (It will also restore it in slightly different form because the increased duty proposed on imports applies to non-filter as well as to filter cigarettes). I have not proposed to remove the preference completely so as not to discriminate against the tobacco industry in comparison with the brewery which still enjoys a preference. For the sake of completeness and to avoid any reverse protection, I propose that the duty on manufactured tobacco imports, other than cigarettes and Chinese prepared tobacco, should also be raised by 25 cents a pound. This is of little revenue significance.

Your Excellency this morning signed an Order under the Public Revenue Protection Ordinance bringing these proposals into effect from two o'clock this afternoon. A resolution confirming this Order will be brought before Council at the earliest opportunity. If passed, it will

reduce the estimated deficit on ordinary account by \$5½ million to \$112½ million; and, incidentally, take tobacco revenue over \$100 million for the first time.

The second subject is water, both in relation to the present emergency and to the longer term future. A Greek poet said: "The best thing is water; although gold like burning fire shines through the night above all other proud wealth". We have in the last few months been exemplifying this order of priority and converting gold into water at an alarming rate. By the time the present dry season is over we are likely to have spent about \$66 million on emergency water supplies or the equivalent of normal revenue from water charges for nearly three years. In addition, revenue this year from water charges is now estimated at \$10 million under the original estimate and the water accounts are likely to show an appreciable loss, even without taking into account emergency expenditure. I am proposing that the emergency expenditure be written off against general revenue and not included in the pro-forma Water Accounts; but that the loss on the year's operations due to reduced revenue should be brought to account therein.

During the last twelve years or so our rate of investment in water supplies has never been limited by purely financial considerations, although of course we can never ignore them; practical engineering and land problems have been the main determining factors and also the very long time it takes to plan and build schemes of the magnitude we have had to undertake. Now the emergency is leading us to look for new and additional sources of water and to step up our capital investment above its already alarming rate. The cost of insurance against years like last year may be very high. I issued a warning last year that the cost of producing water was rising and that water charges would have to be increased; and also that I thought that a more substantial part of future capital requirements should be raised from water charges themselves. Developments arising from the crisis reinforce the case for these measures.

Our investigation into the cost of present and future supplies has not yet been completed and I cannot give any precise indication of what I may eventually propose. Costing is not an easy process as the vagaries of nature mean that the amount of water sold may vary considerably from year to year, whereas the greater proportion of cost is fixed. Future calculations may be made even more difficult by the introduction of new elements into the workings such as desalinization, where fixed costs are the lesser proportion of total costs, and high running costs may make it uneconomic to operate the plant for more than a minimum number of days in a reasonably wet year. It has been suggested to me that to overcome these costing difficulties costs should be worked out and charged a year in arrears (like a co-operative dividend in reverse) so

that actual costs can be exactly determined and recovered. This has theoretical attractions but I can see overriding difficulties and we may have to be content in the end with a fairly arbitrary rate which may have to be adjusted upwards or downwards from time to time in the light of the actual results.

I should draw attention here to the pro-forma Water Accounts. They have been re-organized to present a fairer picture of the financial result of waterworks operations and appear at Appendix H of the draft Estimates. The accounts for the last complete year, 1962-63, show an operating surplus of just over \$5 million. Although water receipts are paid into general revenue, this surplus is treated in the accounts as accruing to the water undertaking and as being applied to reduce capital charges.

Investigation has also been proceeding into the possibility of introducing a scale of charges ascending with consumption per household or per tenement, or with differential rates for summer and winter, so as to charge more for extravagant consumption or for consumption during the dry season. It is, however, clear that there are serious practical difficulties in the way of such procedures (not only those connected with the question of separate meters); but no decision has been taken yet.

This leads me to another water topic—the appropriate daily period of supply we should be aiming at. I find myself considered inhumane or unprogressive or sometimes merely odd, by some of my colleagues as well as members of the public, when I suggest that it is not axiomatic that a twenty-four hour supply in all circumstances must be our immediate aim. I cannot myself see any grounds for the belief that a twenty-four hour domestic water supply is an inalienable right of civilized man. It may be, if he can afford it and is prepared to pay the price. But here we come up against the problem of determining the public's preferences and priorities in the spending of its money and also of determining the true cost to the community. I would not take issue with a doctrine that a twenty-four hour supply should be available if charged for at commercial costs, because they measure the true cost to the community in terms of choice between competing uses of scarce resources. And at commercial prices a twenty-four hour supply may in fact be quite easy to provide because on a commercial basis rates would be very high, probably several times those calculated on the present non-commercial basis, and consumption would therefore be substantially lower. But clearly charges at this level would be a hardship for those who are contented with less at lower prices; and I think there must be, in the case of a public utility like water, an overriding principle that the rate should be low enough for everyone to pay for enough to meet his reasonable needs. What cannot in my view be justified is investment of very large amounts of public capital (for which there are so many competing

demands) for the provision of a supply for maximum consumption on the basis of normal Government pricing at non-commercial interest rates and redemption periods. In our circumstances this would probably be a waste of resources which could be put to much better social and economic use. If we could devise a method of charging a very high rate for excess consumption all would be well and we could have our twenty-four hour supply for those who can afford it. But I am not optimistic about being able to devise a workable system. I myself do not believe therefore that a twenty-four hour domestic supply in all circumstances, or even in average circumstances, is a reasonable aim, in our geographic situation and in our present economic circumstances, although it may be at some time in the future. If now in the process of ensuring our reasonable minimum needs at all times, even in the worst circumstances, we happen to produce a twenty-four hour supply in normal circumstances, or can produce it at very little extra cost, that is not economically objectionable; it is even beneficial as it keeps average cost down. Whether this will happen or not, we cannot yet tell.

I should like, before I move the Resolution, to speak on one further general point of financial policy and practice—the apparent paradox of annual surpluses, low rates of taxation and inadequate public services.

First of all, the situation must be looked at both in the short term and in the long term. Short term, the fact is that public services cannot be expanded, with efficiency and economy, at faster than a certain rate. Spending itself can be raised easily enough by inflating costs, either directly by raising the wages and salaries of the public service or indirectly by imposing excessive pressures on scarce resources. But money cannot be converted into houses or trained teachers or hospitals at the touch of a magic wand. There are limitations to our physical and intellectual resources. Money has not in fact been in general the limiting factor in the expansion of public services in recent years, although I am always concerned to ensure that expansion is carried out as economically as possible. I will not express a judgement on whether we have done as much as was humanly possible in the many and various fields of public service; but our rate of expansion in many of these fields has been quite exceptional in comparison even with other richer countries at any stage of their development. Of course, our needs too have been comparatively greater and have come upon us and have demanded solutions in a shorter space of time.

I have said that money has not been the limiting factor in recent years; this is in the short term. For longer terms it is not quite as true. We have to look ahead as far as we can, and assess as well as we can, both our resources and our needs and attempt to reconcile them; and this future reconciliation must condition our view of the proper level and content of our immediate policies. When introducing my first Budget

two years ago I attempted to make this point. I pointed out that we were at present able to meet the high cost of certain services based on imported standards only because we were providing them for a small part of the population, a situation which had arisen by historical accident; and that I feared that if we went on expanding at current standards and levels of cost we might find ourselves one day with all our resources gone and still inadequate services. What we have to do is shape these services now in such a way that we can as soon as possible provide them in full at costs, both capital and recurrent, we can afford. Timing is of importance in this as well as the rate and extent of expansion, because savings on recurrent costs now may be a condition of future capital expansion.

I should like to exemplify this from education because this is fresh in people's minds from the Marsh/Sampson Report. To put all primary education and existing secondary education at once on to the same basis as aided and Government schools, if that were educationally possible, which I am sure it is not, would add something of the order of \$160 million in recurrent costs for this one social service alone and would pre-empt a very large proportion of the margin we at present see between recurrent revenue and expenditure over the next four years and on which we must rely for the capital element in our expansion. To provide it all free would add another \$30 million or so (these are very rough figures). Education alone would then be costing us the equivalent of an Earnings and Profits Tax rate of over 17%. I believe a comparative figure from the United Kingdom, for what that is worth, is under 10%. I have not attempted to reckon closely the capital cost but it might be the equivalent of more than two years of Resettlement building at the present rate. I do not say that we will not be able to meet costs of this relative order over the whole field of public service at some future date while keeping taxation within bounds; but there is no evidence at present that we will be able to. What evidence we have is that we must either reduce costs or continue to provide a limited public service—or fail to keep taxation within bounds.

To guide us in trying to reach conclusions as to the proper target for expansion of services, both quantitatively and qualitatively, we make projections of revenue and expenditure each year, for five years ahead. These are based on reasonable rates of economic growth and on the approved development programmes for the various major social and other public services, these plans themselves being subject to periodic review, both as to their pace of implementation and their content. Not all services have been so programmed as yet and not all are susceptible of programming. These forward looks are subject to a very wide margin of error; we cannot see accurately one year ahead, far less five. But, as I said last year, a glimmer of light is better than no illumination at all.

The last forecast prepared covers the years 1963-64 to 1967-68 and showed over the period a deficit of \$565 million after using up all but our basic reserves. At the end of the period all but our basic reserves would be gone and the margin between recurrent revenue and expenditure would have been reduced to \$165 million. The figure of \$565 million has already been adjusted downwards by some \$200 million in respect of the improved results of 1963-64, but much of this may be offset by additional capital expenditure on waterworks, including desalinization plant, on public housing and on other unforeseen commitments.

I have racked my brain in an attempt to determine whether there is some hidden bias in these procedures which determines that our pace of expansion of expenditure can never reduce significantly the gap between revenue and expenditure, and so produces regular annual surpluses. But I can find no such inherent bias. It is simply that in recent years our economic growth has been such that expenditure could not, and indeed should not, keep pace. The regular forward look does, in such times, tend to under-estimate future potential and increased expenditure cannot be generated later at break-neck speed. But I am sure that the regularity of the pattern in recent years is fortuitous. One bad year, or two years of normal growth, and we would soon know this all too well.

There are two other points I might make. We have been very fortunate in recent years in the extraordinary buoyancy of the revenue, due to our remarkable rate of economic expansion. Surpluses have piled up because we cannot, even if we thought we should, expand public services to keep pace with increasing revenue. That revenue has increased in this way is in no small measure, I am convinced, due to our low tax policy which has helped to generate an economic expansion in the face of unfavourable circumstances. Recurrent revenue has more than doubled in the five years since the year 1958-59 with no significant change in taxation; this increase is equivalent to an increase in the Earnings and Profits Tax rate, on that year's income, from the actual 12½% to something like 80%. High taxation could not itself have produced this increased yield.

It is difficult to believe that the rate of expansion of the revenue will not fall; we certainly cannot assume that it will not. It is a fortunate feature of our building up of reserves from recent surpluses that we will be able to proceed with the implementation, I hope accelerated implementation, of programmes of expansion over the next few years without having to face the prospect of taxation at levels likely to cripple our economy. Economic expansion remains the door to social progress and I am convinced that in our circumstances low taxation can in general produce a greater growth in revenue than can tax increases. I am not saying, however, that there is no scope for tax increases too; there clearly is.

That leads me to one final point, the choice between fees and taxation as a means of financing public services. If one accepts that in general social services should be made available to all on the basis of ability to pay, one has the choice of two opposite principles of action, although they need not be mutually exclusive—either progressive taxation and free services or fees covering costs with remission for those who cannot afford them. The former method is appropriate, in my view, in rich developed countries where the principle of progressive taxation can be applied without unduly adverse economic or social results, and the wastes inherent in full and free services can be afforded. In less advanced or poorer countries, where neither economy nor society is geared to progressive taxation and waste cannot be tolerated, fees remittable in case of need seem to me clearly more appropriate. We do not consistently follow either course. Our system of taxation can barely be called progressive but many of the well-to-do enjoy quite heavily subsidised social services.

I myself think that at our present stage of development we come closer to the category of society where fees should be charged to cover costs with remission for those who cannot afford them. This conforms with the adjuration frequently addressed to me to rely on indirect rather than direct taxation. Remittable fees may indeed be regarded as a form of progressive indirect taxation. I do not think that we could take progressive direct taxation very far at present without adverse economic effects, although I do not say that when the time comes we shall not be able to take it rather further than we do at present. But even if we can look forward to a sufficiency of social services one day, free of charge where appropriate, we can hardly accept it as equitable if, as is likely, the extent of subsidies enjoyed by the well-to-do must retard significantly, in the intermediate period, the extension of subsidised or free services to the poor. I have seen it claimed that the well-to-do have a right now to fully subsidised services because they pay for them in taxes. This is palpably not so in our present tax situation with its relatively low rate of direct taxation. If these taxes are to be regarded as payment for social services, then our poorer fellow-citizens are paying more than their fair share of other public expenditure. I sometimes suspect they do as it is but, in this hard world Hong Kong lives in, it may be a condition of the economic and social advancement our community is enjoying.

This is a question of general principle which arises, I think, in relation to all public services, except, perhaps, social welfare where the services themselves are provided in relation to need, and ability to pay is normally, by definition, irrelevant. The question is, for example, being debated at present in connexion with education and will arise also in connexion with the new Medical Development Plan which was tabled in this Council two weeks ago.

I have perhaps strayed a little too far from the straight path of public finance into fields where economic wisdom and social justice appear, but I believe only appear, to come into conflict, and I had better return to the business of the day. (*Applause*).

THE COLONIAL SECRETARY seconded.

The question was put and agreed to.

REGISTRATION OF UNITED KINGDOM PATENTS ORDINANCE

THE ATTORNEY GENERAL moved the following resolution: —

Resolved, pursuant to section 11 of the Registration of United Kingdom Patents Ordinance, that the Registration of United Kingdom Patents (Fees) (Amendment) Rules, 1964, made by the Registrar of Patents on the 23rd day of January 1964, under section 11 of that Ordinance, be approved.

He said: Sir, the Explanatory Note appended to the Rules sufficiently explains their purpose and I have nothing further to add.

THE COLONIAL SECRETARY seconded.

The question was put and agreed to.

ADJOURNMENT

HIS EXCELLENCY THE GOVERNOR: —That concludes the business for to-day, gentlemen. When is it your pleasure that we should meet again?

THE ATTORNEY GENERAL: —Sir, may I suggest Monday, 16th March.

HIS EXCELLENCY THE GOVERNOR: —Council stands adjourned until Monday, 16th March.