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LegCo Panel on Financial Affairs
Meeting on 3 July 2001

Background Brief on the Proper Use of Fiscal Reserves

Purpose

This brief summarizes the deliberations on the use of fiscal reserves at meetings of the Finance Committee, Financial Affairs Panel and the Council, highlighting Members' suggestions on the proper use of the reserves.

Background

2. Recent discussion on the use of fiscal reserves started at the two briefings at the Finance Committee on the 2001-02 Budget: briefings by the Secretary for the Treasury on 2 March 2001 and by the Financial Secretary on 9 March 2001. According to the Administration, the purpose of the fiscal reserves is to meet Government's operating needs, absorb any fiscal deficits during the downswing of an economic cycle, or meet contingencies such as any major regional or world events with serious adverse financial implications on the economy of Hong Kong. As Hong Kong has adopted the currency board system to maintain currency stability, it is the Government's policy that fiscal reserves should be used to safeguard the stability of the monetary system in unforeseen circumstances as well. The guidelines adopted by the Government in determining the appropriate level of fiscal reserves is the total of 12 months' government expenditure and the Hong Kong dollar money supply under the M1 definition, allowing a range of plus or minus 25%.

3. On the budgetary principles, the Administration maintains that in drawing up the budget, the Administration has to follow the principles set out in Article 107 of the Basic Law of keeping expenditure within the limits of revenues, striving to achieve a fiscal balance and keeping the budget commensurate with the growth rate of Gross Domestic Product over a period of time. The current time-frame adopted by the Government to strive the fiscal balance is the five-year forecast period for the Medium Range Forecast.

4. Members continued to question the rationale for adopting the guidelines in determining the level of fiscal reserves, the purposes to be served by fiscal reserves and the interpretation of the budgetary principles as enshrined in Article 107 of the Basic Law. As a result, the subject was further discussed at the Financial Affairs Panel (the Panel) on 7 May 2001. A relevant question on foreign reserves was also raised by Hon Emily LAU at the Council meeting on 13 June 2001.

5. To enable the Panel to consider the subject of proper use of fiscal reserves from different perspectives, the Panel decided to invite academics and experts in relevant field to give their views on the subject at the meeting scheduled for 3 July 2001.

Summary of concerns

6. To facilitate the discussion at the Panel meeting on 3 July 2001, a summary of the concerns raised at the various meetings and the Administration's responses is provided at the **Appendix**.

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