

**LEGISLATIVE COUNCIL
PANEL ON PLANNING, LANDS AND WORKS**

Capital Injection into the Urban Renewal Authority

INTRODUCTION

This paper sets out the Government's proposal to inject \$10 billion into the Urban Renewal Authority (URA) to implement the urban renewal programme.

BACKGROUND

2. Hong Kong faces an urban decay problem. In 2001, there were about 9 300 private buildings in the Metro Area[#] which were 30 years' old and above. In ten years' time, this number will increase by about 50% to some 14 000 buildings.

3. The Urban Renewal Authority Ordinance (URAO) (Cap. 563) was enacted in July 2000. The URA was established in May 2001 to undertake an urban renewal programme comprising 200 projects identified in the Government's Urban Renewal Strategy and 25 uncompleted projects of the former Land Development Corporation (LDC).

4. Under the URAO, urban renewal includes the redevelopment of dilapidated buildings, promoting the rehabilitation of older buildings and the preservation of buildings of historical, cultural or architectural interest. The main policy objective is to improve the environment of the older urban areas and the living conditions of the residents therein. The Government has set out in the Urban Renewal Strategy the following targets for the urban renewal programme –

- (a) redevelopment of some 2 000 ageing or dilapidated buildings;
- (b) improvement of the environmental quality of 67 hectares of old and run-down urban areas;
- (c) rehousing some 27 000 tenant households;

[#] The Metro Area covers Hong Kong Island, Kowloon, Tsuen Wan and Kwai Tsing.

- (d) provision of around 60 000 m² of open space;
- (e) provision of about 90 000 m² of floor space for use as community/welfare facilities; and
- (f) provision of seven new schools.

FINANCIAL SUPPORT

(A) Need for Government Support

5. The URA is tasked to undertake projects in areas where urgent redevelopment is required in view of the state of dilapidation of the buildings, and where the living conditions of the residents are poor. A considerable number of these projects have limited redevelopment potential. The land assembly cost could sometimes exceed the value of the site after redevelopment. Many of the projects are also of little interest to private developers on their own due to land assembly difficulties.

6. In accordance with the transitional provisions under the URAO, the URA has taken over all the assets and liabilities of the LDC, including the on-going projects. Mainly due to the losses from one on-going project taken over from the LDC, the URA has not started in a strong financial position. The URA estimates that the total deficit for the ten on-going projects of the LDC would amount to around \$1.7 billion upon their completion.

7. To take forward the urban renewal programme, the URA will need to raise finances through joint venture partnership with private developers and bank borrowings. It also requires financial support from the Government.

8. We have assessed the extent of the Government's financial support required to jumpstart the urban renewal programme against the approved Corporate Plan (CP) of the URA for the period 1 April 2002 to 31 March 2007 and the approved Business Plan (BP) for the period 1 April 2002 to 31 March 2003. In the process, we have taken into account the following considerations –

- (a) the objective that the urban renewal programme should be self-financing in the long run;
- (b) the projected financial needs of the URA to carry out its mandate of redevelopment, rehabilitation and preservation;

and

(c) the Government's fiscal position.

The programme of work and the associated financial projections in the Annex CP and the BP are summarised at the Annex.

9. As part of the Government's financial support package for the URA, urban renewal sites for new projects set out in the URA's CPs and BPs to be approved by the Financial Secretary (FS) from time to time may in principle be granted to the URA at nominal premium, subject to satisfying FS of the need therefor. The value of any land premium foregone will be reflected in the accounts of the URA. Similarly, land required to meet the URA's rehousing needs as identified in the approved CPs and BPs may in principle be made available at nominal premium, subject to satisfying FS of the need therefor.

10. To address the immediate financial needs of the URA and to launch the urban renewal programme on a sound financial footing, we propose to seek funding approval from the Finance Committee (FC) of the Legislative Council for a commitment of \$10 billion under the Capital Investment Fund as capital injection into the URA. Subject to the FC's approval of the \$10 billion commitment, equity will be injected in phases in the coming five financial years.

(B) Implications of Government Financial Support

11. The proposed capital injection, and the land premium concessions for urban renewal and rehousing sites of the URA together constitute a significant contribution to the urban renewal programme. This sizable subsidy for renewing our urban fabric underlines the Government's financial commitment to improving the living conditions of residents in older urban areas and better the environment for the whole community.

12. With the Government's capital injection and the land premium waived as capital, the URA should be well-placed to raise finances at a corporate level in a cost-effective manner. The proposed \$10 billion commitment would demonstrate the Government's support for the URA to banks, creditors and potential joint venture partners. It would allow the URA to raise the balance required for taking forward the urban renewal programme through borrowings at competitive rates and joint ventures with developers where appropriate.

13. The URA estimates that, with the Government's financial support and the finances that it will raise on the market, it will achieve a break even situation with a cash balance of \$10 billion and no liabilities in 2014/15, the end of the implementation period of all the projects in its first CP. This is in line with our objective that the urban renewal programme should be self-financing in the long run.

14. The financial forecasts in the CP depend on the various assumptions adopted by the URA. (Please see paragraph 3 of the Annex.) Factors such as movements in the property market, interest rate changes, construction cost fluctuations and the actual implementation mode of individual projects would all have a significant bearing on the outturn of the financial projections and indeed the financial viability of the programme. Factors like interest rate and property market movements are in turn influenced by macro economic conditions. The Government would keep under close review the performance of the URA in delivering the urban renewal programme and its financial position in the annual CP and BP examination exercise.

SOCIO-ECONOMIC BENEFITS

15. The Government's financial support will improve the financial viability of urban renewal projects and facilitate the implementation of the programme, thus conferring distinct social and environmental benefits on the community, which is the ultimate objective of the urban renewal programme. With the compensation and rehousing arrangements, owners and tenants in older urban areas are given the chance of an improved living environment. Physically, obsolete and incompatible land uses will be rationalised and there will be better local transport networks and district facilities. The implementation of these projects would improve the quality of the living environment through the provision of public open space and Government/ Institution/ Community facilities in the built-up urban areas.

16. Economically, the urban renewal projects will create investment in the property development sector and increase job opportunities. The redeveloped sites with better district planning will also enhance the economic value of the land and properties in the locality. This may also encourage other property owners to embark on self-initiated rehabilitation efforts.

17. The above benefits will all be conducive to promoting Hong Kong's status as a world-class city, and achieving a quality and vibrant urban living environment in Hong Kong.

WAY FORWARD

18. Subject to Members' views, we intend to make a submission to the FC of the Legislative Council on 21 June 2002 to seek approval for a funding commitment of \$10 billion under the Capital Investment Fund as capital injection into the URA.

Planning and Lands Bureau
24 May 2002

Urban Renewal Authority First Corporate Plan and Financial Projections

Under the Urban Renewal Authority Ordinance (URAO), before the start of each financial year, the Urban Renewal Authority (URA) is required to submit to the Financial Secretary (FS) for approval a draft corporate plan (CP) setting out its proposed programme of projects for the next five years and a draft business plan (BP) setting out the projects to be implemented in the next year. In order to kick-start the urban renewal programme as early as possible to meet the community's expectation, FS gave approval to the URA in January 2002 for the implementation of three uncompleted projects of the Land Development Corporation (LDC) as "early launch" projects prior to the submission of its first draft CP and BP. Subsequently, the URA submitted its draft CP and draft BP covering the periods 1 April 2002 to 31 March 2007 and 1 April 2002 to 31 March 2003 respectively to FS for approval on 18 March 2002. The two draft plans were approved by FS on 28 March 2002.

2. The approved CP comprises 42 new projects, including all of the 25 uncompleted projects of the LDC and 17 projects identified in the Government's Urban Renewal Strategy. These projects will affect over 6 200 property interests and about 10 400 tenant households. They cover a total project area of around 13.5 hectares, with up to 18 000 flats to be built. In addition, about 13 400 m² of public open space and about 39 200 m² of floor space for use as Government/ Institution/ Community facilities will be provided. The implementation of these projects will improve the living conditions of the residents. It will also bring about improvement to the environment and much needed community facilities in the built-up urban areas to the overall benefit of the community.

3. The URA has made a number of assumptions in the financial projections in its CP. Subject to the various assumptions, the URA expects the 42 new projects in the CP to be financially viable as a whole. This is in line with our policy that the urban renewal programme should be self-financing in the long run. The major assumptions are as follows –

- (a) nominal premium will be payable in respect of urban renewal sites^Δ and land for the URA's rehousing purposes;

^Δ Except for one project which does not involve compensation for owners and rehousing.

- (b) a total of \$10 billion will be injected into the URA by the Government which would be drawn down in five equal tranches from 2002/03 to 2006/07;
- (c) a 50:50 joint venture approach with developers is adopted as a proxy*, whereby it is assumed that the developers would contribute half of the land value of the assembled site at the start of the development stage and share the development costs and profits with the URA equally;
- (d) no assumption of future inflation/deflation in the cashflow forecast. The acquisition costs of the 42 projects and gross development value (GDV) of these projects are based on valuation figures as at September 2001; and
- (e) the interest rates on bank loans and cash surplus are 6% per annum and 4% per annum respectively.

4. On the basis of the above assumptions, the URA estimates that the GDV of the 42 new projects will be about \$53.2 billion and the total development cost over the development period will amount to about \$37.9 billion, broken down as follows –

| | |
|--------------------------|-----------------------|
| Acquisition cost | \$17.7 billion |
| Rehousing cost | \$3.4 billion |
| <u>Construction cost</u> | <u>\$16.8 billion</u> |
| | \$37.9 billion |

In addition, a sum of \$0.4 billion is earmarked for work in the areas of rehabilitation, revitalisation and heritage preservation.

5. In addition to the Government's financial support, the URA would have to borrow from the market to finance its projects. At the peak of the development period of its first CP in 2009/10, this borrowing will amount to \$9.6 billion.

6. Under the scenario of the 50:50 joint venture approach as described in paragraph 3(c) above, the financial implications of the 42 projects to the URA would be as follows –

* There are three implementation modes for URA projects, namely sole development by the URA, joint venture with private developers and land sale after site assembly.

| | |
|--|-----------------------|
| <i>Revenue</i> | |
| 50% of land value | \$10.5 billion |
| 50% of GDV | <u>\$26.6 billion</u> |
| <i>Total revenue</i> | <i>\$37.1 billion</i> |
| <i>Cost</i> | |
| Full acquisition cost | \$17.7 billion |
| Full rehousing cost | \$3.4 billion |
| 50% of construction cost | \$8.4 billion |
| Rehabilitation, revitalisation and heritage preservation cost | \$0.4 billion |
| Overheads (Staff cost, accommodation etc.) | \$3.1 billion |
| <u>Corporate interest expenses</u> | <u>\$2.4 billion</u> |
| <i>Total cost</i> | <i>\$35.4 billion</i> |
| | |
| Total revenue | \$37.1 billion |
| <u>Less: Total costs</u> | <u>\$35.4 billion</u> |
| Surplus | \$1.7 billion |

7. Taking into account the deficit of \$1.7 billion inherited by the URA in the ten on-going projects of the LDC, the URA estimates that it will achieve a break even situation with a cash balance of \$10 billion and no liabilities in 2014/15, the end of the development period of the first CP projects.

Planning and Lands Bureau
24 May 2002