

For information on
27 June 2012

Legislative Council
Panel on Home Affairs and Panel on Development
Joint Subcommittee to Monitor the Implementation of the
West Kowloon Cultural District Project

Financial Arrangements for
the West Kowloon Cultural District Project

PURPOSE

Further to LC Paper No. CB(2)2530/10-11(03) issued for discussion on 26 August 2011, this paper informs Members of the current financial situation and arrangements for the West Kowloon Cultural District (WKCD) project.

BACKGROUND

2. The Finance Committee of the Legislative Council approved a one-off upfront endowment of \$21.6 billion (in 2008 Net Present Value) on 4 July 2008 for covering the capital costs for implementing the WKCD project. The retail/dining/entertainment (RDE) part of the WKCD development will be vested in the WKCDA to provide a source of recurrent income through rental proceeds to meet the operating costs of the arts and cultural facilities and related facilities.

3. The other communal and government facilities and related engineering works supporting the whole WKCD development will be undertaken by the Government and funding approval for such works will be sought separately.

FINANCIAL INFORMATION AVAILABLE

4. The following financial information has been provided to the Legislative Council -

- a) The original Consultative Committee (CC) case estimates (PWSC(2008-09)31 dated 18 June 2008)
- b) Financial assumption changes (LC Paper No. CB(2)2530/10-11(03) dated 26 August 2011)
- c) Construction cost index changes (LC Paper No. CB(2)2530/10-11(03) dated 26 August 2011)

5. The three selected Conceptual Plan Consultants (CPC) have undertaken their own financial assessments based on their proposed conceptual plans. All CPCs (namely Foster+Partners, Rocco Design Architects Limited and Office for Metropolitan Architecture) confirmed that their plans were within budget according to their own financial assumptions, projected RDE income and estimated construction cost trend. Their estimated capital cost ranged from HKD28 billion to HKD29.6 billion, and taking into account the projected RDE income, their projected surplus on total project NPV¹ ranged from HKD2.9 billion to HKD8 billion.

6. Apparently, the outcome of the estimates was very much dependent on the cost and RDE revenue projections given by the CPCs. All three submissions indicated high RDE revenues to cover the capital cost deficits. It was recognized that the eventual cost level and RDE revenue would be subject to change and that the cost trend needed to be closely monitored due to the volatility of construction activities in the coming years.

¹ Total surplus on total project NPV = (sum of RDE operating income and one-off endowment) – (sum of capital cost and venue operating deficit)

LATEST UPDATE ON FINANANCIAL SITUATION

7. The WKCDA has been managing its finance prudently and is mindful of the investment objectives to meet project cash flow requirements, to preserve capital, to maintain a diversified portfolio investment risk and maturity profile, and to optimize investment yield. It also targets yield to cover inflation costs and maintain its purchasing power. As at 31 March 2012, the asset allocation of the WKCDA's investment was 49% long term placement with Hong Kong Monetary Authority, along with 51% internally managed deposits and bonds, including 17% RMB deposits, 14% USD deposits, 18% HKD deposits and 2% RMB bonds. The investment yield since inception was 1.4% in 2008-2009; 1.1% in 2009-2010; 3.4% in 2010-2011 and 4.1% in 2011-2012. The investment environment is however highly volatile and the associated risks have to be well managed.

8. The building cost has also been subject to high volatility, which will likely continue due to various infrastructure demands and macro-economic factors worldwide and in the region. Further tender price increases have been recorded since our last report –

- a) ASD tender price index trend
(from 1249 in the third quarter of 2010 to 1369 in the third quarter of 2011, or 9.6% increase over the past year)
- b) RLB tender price index trend
(from 1750 in the third quarter of 2010 to 1925 in the third quarter of 2011, or 10% increase over the past year)

9. According to the WKCD completion programme, the building design for Xiqu Centre will be available at the end of this year. The first construction tender is expected to be

issued by the third quarter of 2013, followed by super structure tender by the first quarter of 2014. The design details (with detailed cost plan) will be finalized with the selected designers in consultation with stakeholders. RDE related venues will be developed in parallel. The income generated will have an important impact on the finance of the project and should be carefully gauged.

10. The WKCDA is in close liaison with the Government on the funding and apportionment of the infrastructure costs. As the infrastructure and hotel/office/residential (HOR) uses will share a common basement structure, the costs of the basement need to be apportioned.

11. As previously reported, green initiatives to be adopted by the WKCDA will also have cost implications. In particular, the WKCDA plans to develop a District Cooling System that serves both the WKCDA and HOR premises, and will discuss with the Government the cost apportionment in this respect. There will be additional construction costs on individual buildings (compared to CC case) due to more stringent environmental design and accessibility requirements. There will also be cost implications arising from low-carbon (and longer term zero-carbon) initiatives. The actual cost implications of these initiatives can only be ascertained closer to the completion of detailed design.

WAY FORWARD ON FINANCIAL ARRANGEMENTS

12. The WKCDA is fully aware of the need for prudent financial management and planning to accomplish the vision of the WKCD. To meet the foreseeable financial challenges, the WKCDA will endeavor to seek the best return from the endowment according to our investment objectives, monitor

closely the tender price trend and update the expenditure position upon the issuance of building tender by mid-2013.

13. The WKCDA will actively look into alternative financing options and private sector involvement for some of the venues that may be better managed and operated by commercial service providers.

14. The WKCDA will also strive to adopt cost-effective designs and an optimal strategy to package and phase the design and construction of the WKCD project works (including the basement and infrastructure works), with due consideration of the target completion dates of the Core Art and Culture Facilities as well as the RDE facilities .

West Kowloon Cultural District Authority
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