

ITEM FOR FINANCE COMMITTEE

HEAD 106 – MISCELLANEOUS SERVICES

New Non-Recurrent Subhead “Contribution to the Tenth Replenishment of the Asian Development Fund”

Members are invited to approve the creation of a new non-recurrent subhead with a commitment of \$260.18 million for making a contribution to the tenth replenishment of the Asian Development Fund.

PROBLEM

Hong Kong has to decide whether to make a voluntary contribution to the tenth replenishment of the Asian Development Fund (ADF XI) of the Asian Development Bank (ADB) according to a consensus burden sharing formula.

PROPOSAL

2. We propose that Hong Kong should make a contribution of US\$33.14 million (or HK\$260.18 million) to ADF XI over a nine-year period from 2013-14 to 2021-22.

JUSTIFICATION

3. Hong Kong has been a donor of the Asian Development Fund (ADF) since 1983¹. With the approval of this Committee, we have made contributions

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¹ Hong Kong has contributed to seven previous replenishments totaling US\$82.11 million, including – US\$1 million each in 1983 (ADF IV) and 1987 (ADF V), US\$3 million in 1992 (ADF VI), US\$15.39 million in 1997 (ADF VII), US\$16.28 million in 2001 (ADF VIII), US\$19.19 million in 2005 (ADF IX), and US\$26.25 million in 2009 (ADF X). Unlike the token donations in ADF IV to VI, the amount contributed by Hong Kong in ADF VII to X matched that derived from the consensus burden sharing formula agreed amongst the donors. The outstanding commitment of US\$18.64 million (or HK\$147.52 million) for ADF IX and ADF X will continue to be disbursed by instalments until the middle of 2014-15 and 2017-18 respectively as scheduled.

according to a consensus burden sharing formula² in the last four replenishments since ADF VII in 1997. According to this formula, Hong Kong's burden sharing ratio is 0.57% of the target size of contribution by donors.

Reasons for contribution

4. We consider that Hong Kong should continue to contribute to ADF in its tenth replenishment for the reasons set out in paragraphs 5 to 10 below.

Expectation of Hong Kong's commitment

5. Hong Kong joined the ADB in 1969 and has benefited from ADB's operations in the region. During the period from 1972 to 1980, Hong Kong obtained five loans totalling US\$101.5 million from the ADB. These loans were used to finance the construction of public housing projects (Shatin Urban Development (Housing) Project (Wo Che Estate and Sha Kok Estate) and the second Shatin Urban Development Project (part of the development of Shatin New Town and the construction of Mei Lam Estate)), a sewage treatment plant (Shatin Sewage Treatment Plant Stage 1), a polyclinic (Shatin Hospital Polyclinic Project) and one other infrastructure project (Lok On Pai Sea Water Desalting Plant). All loans were repaid in full by 1987.

6. As Hong Kong is a member of ADB, firms in Hong Kong are able to bid for ADB-sponsored projects. According to the ADB, as of end 2011, Hong Kong firms have been awarded procurement contracts for goods, works and consultancy services on ADB-sponsored projects worth US\$878.39 million in total.

7. Given that Hong Kong's per capita Gross National Income (GNI), at US\$35,160 in 2011, is now one of the highest in the region, there is general expectation for Hong Kong – together with other regional members which have “graduated” from the ADB assistance programmes³ – to contribute to ADB's poverty reduction efforts in the region.

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² Although contribution to the ADF is on a voluntary basis, donors have generally made reference to a burden sharing formula, which is based on the donor's shareholding in ADB adjusted for its per capita GNI. The formula provides a useful reference for donors to determine their contributions to the ADF.

³ Graduation from ADB assistance will be triggered when the GNI per capita of a member exceeds the threshold (US\$6,725 in 2008). Hong Kong “graduated” from regular ADB assistance in 1999.

Hong Kong's commitment to the ADB

8. The ADB is one of the few multilateral financial institutions in which Hong Kong is a full member. As a responsible member, Hong Kong has a strong moral obligation, along with other member economies from within and outside the region, to fully support the activities of the ADB as far as possible. Our continued contribution to the ADF is an important practical demonstration of Hong Kong's support to the ADB. We note that, despite the considerable economic progress in the Asia and Pacific region over the past three decades, poverty continues to affect the lives of millions in the less developed countries in the region. These people are deprived of even the most basic amenities, social services and education. The ADB, mainly through the ADF, has played a key role in supporting efforts to reduce poverty in the Asia-Pacific region. Hong Kong's continuing funding support for the ADF will be a clear demonstration of our contribution towards poverty reduction efforts in the region.

9. A majority of regional donors, including Japan, Australia, China, Malaysia, Singapore and Thailand, have agreed to either increase or maintain their burden share at the same level as the previous replenishment (i.e. ADF X)⁴. Even though Korea is unable to fully maintain its burden share, it has agreed to increase its contribution by 32% in terms of won. That said, most of the non-regional donors, in particular the United States and some European countries, have decided to contribute less than the amount required to maintain their burden share in ADF X, citing such reasons as fiscal constraints, or expectation for regional donors to take up a greater role in financing the ADF.

10. There is a general expectation that Hong Kong, being a regional donor, will at least maintain its burden share in ADF XI as in the case of its regional peers. Any diminution from the burden-shared contribution is likely to be met with adverse reactions within the ADB and among the international community, as it will be taken to be a sign of Hong Kong backtracking on its commitment to support poverty reduction in the region and not shouldering the moral obligation that comes with its membership at the ADB. This would risk damaging Hong Kong's image as well as our reputation as an international financial centre.

Amount of contribution

11. As agreed among ADF donors in April 2012, ADF XI will have a replenishment size of US\$12.40 billion. Part of the funding will come from donor contributions (a target size of US\$5.81 billion) and the remainder from ADB's

/internal

⁴ Japan is the largest donor with a burden sharing ratio of 35% of total donor contributions.

Encl. 1 internal pool of resources. A total of 30 economies⁵, with details on individual donor contributions at Enclosure 1, have pledged their contributions to ADF XI.

12. Applying Hong Kong's burden sharing ratio of 0.57% as mentioned in paragraph 3 above to the target total donor contributions of US\$5.81 billion, Hong Kong's share translates into an amount of US\$33.14 million. The increase in Hong Kong's contribution relative to its last contribution of US\$26.25 million for ADF X is a result of the burden sharing of an enlarged size of ADF operations due to increased demand for assistance and inflation.

FINANCIAL IMPLICATIONS

13. Adopting the exchange rate of US\$1 = HK\$7.85⁶ and allowing 0.01% for contingency, a commitment of HK\$260.18 million is required to meet Hong Kong's contribution of US\$33.14 million to ADF XI.

Encl. 2 14. Subject to Members' approval of the proposed contribution to ADF XI, we will adopt the nine-year standard encashment schedule, as in ADF X, for Hong Kong's contribution. The schedule is set out at Enclosure 2. We will make sufficient provision in the Estimates of the relevant years to meet the cash flow requirements.

15. There will be very moderate additional administrative costs⁷ involved in Hong Kong's contribution to ADF XI, and they will be absorbed by the operating departments.

PUBLIC CONSULTATION

16. We consulted the Legislative Council Panel on Financial Affairs on the proposal on 7 January 2013. Members were supportive of the proposed contribution according to the consensus burden sharing formula on the consideration that Hong Kong should shoulder its international obligation to assist in poverty reduction efforts in the region.

/BACKGROUND

⁵ Not including Hong Kong. Hong Kong has indicated its intention to contribute to the replenishment subject to seeking approval of the domestic legislature, and with the amount to be confirmed. There are at present 31 donors including Hong Kong.

⁶ This is the upper bound of the Convertibility Zone (between 7.75 and 7.85) under the Linked Exchange Rate system.

⁷ Administrative costs are staff costs involved in the process.

BACKGROUND

Encl. 3 17. The ADF, established in 1973, is a concessional financing window of the ADB available to the most needy members in the Asia-Pacific region to support poverty reduction and improve the quality of life. ADF operations include various infrastructure projects for road improvement, power distribution, water supply and sanitation, etc., as well as development programmes in education, health, agriculture and finance sectors, in the poorest economies in the region. The total ADF assistance for these economies amounted to US\$46.93 billion since its inception to the end of 2011. At present, 28 ADB developing member jurisdictions, with details at Enclosure 3, have access to ADF resources. Among them, Bangladesh, Vietnam, Pakistan and Afghanistan are the largest beneficiaries of the ADF for the period from 2001 to 2010.

18. Contributions to ADF by ADB members are on a voluntary basis and the ADF is typically replenished once every four years.

19. On 4 December 2012, the Executive Council endorsed that, subject to the funding approval of this Committee, Hong Kong should contribute US\$33.14 million (or HK\$260.18 million) to ADF XI over a nine-year period.

Financial Services and the Treasury Bureau
January 2013

Overview of Donor Contributions and Burden Sharing of ADF XI

Donor	ADF XI contribution ¹ (US\$ mn)	ADF XI burden share ¹ (%)	ADF X burden share (%)	Difference in burden share (% point)
Non-regional (19)				
Austria	43.2	0.74	0.91	-0.17
Belgium	34.8	0.60	0.72	-0.12
Canada	193.4	3.33	4.50	-1.17
Denmark	24.9	0.43	0.43	0.00
Finland	29.2	0.50	0.73	-0.23
France	128.8	2.22	3.48	-1.26
Germany	194.2	3.34	4.82	-1.48
Ireland	27.0	0.46	0.90	-0.44
Italy	91.8	1.58	3.00	-1.42
Luxembourg	11.3	0.20	0.10	+0.10
Netherlands	81.0	1.39	2.34	-0.95
Norway	44.9	0.77	0.97	-0.20
Portugal	0.5	0.01	0.60	-0.59
Spain	66.9	1.15	2.80	-1.65
Sweden	79.7	1.37	1.37	0.00
Switzerland	53.1	0.91	1.04	-0.13
Turkey	5.8	0.10	0.14	-0.04
UK	314.6	5.41	5.07	+0.34
US	359.6	6.19	10.01	-3.82
Sub-total	1,784.8	30.70	43.92	-13.22
Regional (12)				
Australia	523.3	9.00 ²	6.49	+2.51
Brunei Darussalam	6.3	0.11	0.12	-0.01
China, People's Republic of	45.0	0.77	0.76	+0.01
Hong Kong, China	-³	-³	0.57	-
Japan	2,034.9	35.00	35.00	0.00
Kazakhstan	5.2	0.09	N/A	+0.09
Korea, Republic of	167.9	2.89	3.35	-0.46
Malaysia	9.6	0.16	0.13	+0.03
New Zealand	32.6	0.56	0.70	-0.14
Singapore	8.7	0.15	0.12	+0.03
Chinese Taipei	23.0	0.40	0.47	-0.07
Thailand	4.9	0.08	0.08	0.00
Sub-total	2,861.4	49.22	47.79	+1.99
Total actual contribution (A)	4,646.1	79.91	91.71	
Target size (basis for burden sharing) (B)	5,813.9	100.00	100.00	
Funding gap (C)=(B)-(A)	1,167.8⁴	20.09	8.29	

¹ Source: ADF XI Donors' Report

² Australia has indicated that it intends to confirm an additional contribution of 2% burden share by 30 June 2013. The supplemental payment will count towards Australia's final burden share in ADF XI.

³ Hong Kong has indicated its intention to contribute to the replenishment subject to seeking approval of the domestic legislature, with the amount to be confirmed.

⁴ It is expected that part of the funding gap will be filled by additional contributions to be made by some existing or new donors.

* Figures in the table may not add up due to rounding.

ADF XI Encashment Schedule

Payment Date	Encashment Drawdown Rate (%)	Estimated Encashment ¹ (US\$)	Subtotal Estimates (in Each Financial Year)		
			(US\$)	(HK\$ equivalent) ²	(rounded up to nearest thousand HK\$)
FY 2013/2014					
Jul-13	5.10	1,690,000			
Feb-14	4.50	1,491,500	3,181,500	24,977,272.48	24,978,000
FY 2014/2015					
Jul-14	4.50	1,491,500			
Feb-15	6.30	2,088,000	3,579,500	28,101,884.91	28,102,000
FY 2015/2016					
Jul-15	6.30	2,088,000			
Feb-16	8.30	2,750,500	4,838,500	37,986,023.22	37,987,000
FY 2016/2017					
Jul-16	8.30	2,750,500			
Feb-17	7.55	2,502,000	5,252,500	41,236,248.21	41,237,000
FY 2017/2018					
Jul-17	7.55	2,502,000			
Feb-18	7.35	2,435,500	4,937,500	38,763,250.94	38,764,000
FY 2018/2019					
Jul-18	7.35	2,435,500			
Feb-19	6.50	2,154,000	4,589,500	36,031,177.76	36,032,000
FY 2019/2020					
Jul-19	6.50	2,154,000			
Feb-20	4.45	1,474,500	3,628,500	28,486,573.37	28,487,000
FY 2020/2021					
Jul-20	4.45	1,474,500			
Feb-21	2.50	828,690	2,303,190	18,081,849.50	18,082,000
FY 2021/2022					
Jul-21	2.50	828,690	828,690	6,505,867.02	6,506,000
Total	100.00	33,139,380	33,139,380	260,170,147.41	260,175,000 say 260,180,000

¹ Source: ADB estimates

² Converted into Hong Kong dollars using the exchange rate of US\$1 = HK\$7.85, being the upper bound of the Convertibility Zone (between 7.75 and 7.85) under the Linked Exchange Rate system, plus 0.01% contingency.

ADF Recipient Jurisdictions

	Per Capita GNI (US\$; 2010)	ADF Loan and Grant Approvals (US\$ million; 2001-10)
1. Afghanistan	410	2,037.3
2. Armenia #	3,200	223.9
3. Bangladesh #	700	3,241.1
4. Bhutan	1,870	215.6
5. Cambodia	750	930.2
6. Georgia #	2,680	423.8
7. Kiribati	2,010	12.0
8. Kyrgyz Republic	840	555.6
9. Lao PDR	1,010	592.7
10. Maldives	6,150	85.6
11. Marshall Islands #	3,640	24.5
12. Federated States of Micronesia #	2,730	27.2
13. Mongolia #	1,870	463.0
14. Nauru	-	-
15. Nepal	490	1,376.2
16. Pakistan #	1,050	3,019.4
17. Palau #	6,560	3.4
18. Papua New Guinea #	1,300	328.0
19. Samoa	3,020	91.0
20. Solomon Islands	1,030	51.3
21. Sri Lanka #	2,260	1,105.3
22. Tajikistan	810	538.1
23. Timor Leste #	2,730	62.0
24. Tonga	3,340	31.3
25. Tuvalu	4,600	7.1
26. Uzbekistan #	1,300	482.6
27. Vanuatu	2,630	-
28. Vietnam #	1,160	3,180.0

Data source: World Bank and Asian Development Bank

Remarks:

- (1) “#” denotes recipients which have access to both ADF and ADB’s ordinary capital resources. Other ADF recipients have access to ADF only.
- (2) Some jurisdictions have no access to ADF but are eligible for ADB’s ordinary capital resources loans. These are Azerbaijan, Cook Islands, People’s Republic of China, Fiji, India, Indonesia, Kazakhstan, Malaysia, Philippines, Thailand, and Turkmenistan. Several of these jurisdictions are donors of ADF.
- (3) Some jurisdictions have outstanding ADF loans, although currently they are not eligible or otherwise have no access to ADF. These are Azerbaijan, Cook Islands, Indonesia, Kazakhstan, Myanmar, and the Philippines. ADB is currently considering granting ADF access to Myanmar.
- (4) ADF eligibility is based on both per capita GNI and creditworthiness. The per capita GNI cutoff for ADF eligibility was US\$1,175 in 2010. Creditworthiness measures the member’s debt repayment capacity and is assessed by ADB’s internal credit rating system.