

**OFFICIAL REPORT OF PROCEEDINGS****Wednesday, 27 February 1980****The Council met at half past two o'clock****PRESENT**

HIS EXCELLENCY THE GOVERNOR (*PRESIDENT*)  
SIR CRAWFORD MURRAY MACLEHOSE, G.B.E., K.C.M.G., K.C.V.O.

THE HONOURABLE THE CHIEF SECRETARY  
SIR JACK CATER, K.B.E., J.P.

THE HONOURABLE THE FINANCIAL SECRETARY  
SIR CHARLES PHILIP HADDON-CAVE, K.B.E., C.M.G., J.P.

THE HONOURABLE THE ATTORNEY GENERAL  
MR. JOHN CALVERT GRIFFITHS, Q.C.

THE HONOURABLE THE SECRETARY FOR HOME AFFAIRS  
MR. LI FOOK-KOW, C.M.G., J.P.

THE HONOURABLE DAVID AKERS-JONES, C.M.G., J.P.  
SECRETARY FOR THE NEW TERRITORIES

THE HONOURABLE LEWIS MERVYN DAVIES, C.M.G., O.B.E., J.P.  
SECRETARY FOR SECURITY

THE HONOURABLE DAVID WYLIE McDONALD, C.M.G., J.P.  
DIRECTOR OF PUBLIC WORKS

THE HONOURABLE KENNETH WALLIS JOSEPH TOPLEY, C.M.G., J.P.  
DIRECTOR OF EDUCATION

THE HONOURABLE DAVID GREGORY JEAFFRESON, J.P.  
SECRETARY FOR ECONOMIC SERVICES

THE HONOURABLE ALAN JAMES SCOTT, J.P.  
SECRETARY FOR HOUSING

THE HONOURABLE THOMAS LEE CHUN-YON, C.B.E., J.P.  
DIRECTOR OF SOCIAL WELFARE

THE HONOURABLE DEREK JOHN CLAREMONT JONES, C.M.G., J.P.  
SECRETARY FOR THE ENVIRONMENT

DR. THE HONOURABLE THONG KAH-LEONG, J.P.  
DIRECTOR OF MEDICAL AND HEALTH SERVICES

THE HONOURABLE ERIC PETER HO, J.P.  
SECRETARY FOR SOCIAL SERVICES

THE HONOURABLE JOHN CHARLES CREASEY WALDEN, J.P.  
DIRECTOR OF HOME AFFAIRS

THE HONOURABLE JOHN MARTIN ROWLANDS, J.P.  
SECRETARY FOR THE CIVIL SERVICE

THE HONOURABLE JAMES NEIL HENDERSON, J.P.  
COMMISSIONER FOR LABOUR

THE HONOURABLE GERALD PAUL NAZARETH, O.B.E.  
LAW DRAFTSMAN

THE HONOURABLE WILLIAM DORWARD, O.B.E., J.P.  
DIRECTOR OF TRADE, INDUSTRY AND CUSTOMS

THE HONOURABLE OSWALD VICTOR CHEUNG, C.B.E., Q.C., J.P.

THE HONOURABLE ROGERIO HYNDMAN LOBO, C.B.E., J.P.

THE HONOURABLE LI FOOK-WO, C.B.E., J.P.

DR. THE HONOURABLE HARRY FANG SIN-YANG, C.B.E., J.P.

THE HONOURABLE LO TAK-SHING, O.B.E., J.P.

THE HONOURABLE FRANCIS YUAN-HAO TIEN, O.B.E., J.P.

THE HONOURABLE ALEX WU SHU-CHIH, O.B.E., J.P.

THE REVD. THE HONOURABLE JOYCE MARY BENNETT, O.B.E., J.P.

THE HONOURABLE CHEN SHOU-LUM, O.B.E., J.P.

THE HONOURABLE LYDIA DUNN, O.B.E., J.P.

DR. THE HONOURABLE HENRY HU HUNG-LICK, O.B.E., J.P.

THE HONOURABLE LEUNG TAT-SHING, O.B.E., J.P.

THE REVD. THE HONOURABLE PATRICK TERENCE MCGOVERN, O.B.E., S.J., J.P.

THE HONOURABLE PETER C. WONG, O.B.E., J.P.

THE HONOURABLE WONG LAM, O.B.E., J.P.

DR. THE HONOURABLE RAYSON LISUNG HUANG, C.B.E., J.P.

THE HONOURABLE CHARLES YEUNG SIU-CHO, J.P.

DR. THE HONOURABLE HO KAM-FAI

THE HONOURABLE DAVID KENNEDY NEWBIGGING, J.P.

THE HONOURABLE ANDREW SO KWOK-WING

THE HONOURABLE HU FA-KUANG, J.P.

THE HONOURABLE WONG PO-YAN, O.B.E.

**ABSENT**

THE HONOURABLE JOHN HENRY BREMRIDGE, O.B.E., J.P.

THE HONOURABLE ALLEN LEE PENG-FEI

**IN ATTENDANCE**

THE CLERK TO THE LEGISLATIVE COUNCIL

MRS. LORNA LEUNG TSUI LAI-MAN

**Papers**

The following papers were laid pursuant to Standing Order No. 14(2):—

Sessional papers 1979-80:

No. 37— Draft Estimates of Expenditure 1980-81 (published on 27.2.80).

No. 38— Draft Revenue Estimates 1980-81 (published on 27.2.80).

No. 39— Supporting Financial Statements and Statistical Appendices from the Estimates of Revenue and Draft Estimates of Expenditure 1980-81 (published on 27.2.80).

No. 40— Estimates of Revenue and Expenditure for the year ending 31 March 1981— Report of the Public Works Sub- Committee of Finance Committee 1979 (published on 27.2.80).

No. 41— Report of the Establishment Sub-Committee of Finance Committee for 1979-80 (published on 27.2.80).

**Government business****First reading of bill****APPROPRIATION BILL 1980**

*Bill read the first time and ordered to be set down for second reading pursuant to Standing Order 41(3).*

**Second reading of bill****APPROPRIATION BILL 1980**

THE FINANCIAL SECRETARY moved the second reading of:—‘A bill to apply a sum not exceeding \$18,441,723,000 to the service of the financial year ending on 31 March 1981’.

*Paragraphs*

MOTION	1
ACKNOWLEDGEMENTS	2

	<i>Paragraphs</i>
STRUCTURE OF SPEECH	3 - 4
PART I: THE ECONOMY IN THE 1970s	
(1) Growth Performance:	
(a) New series of estimates of expenditure on the G.D.P.	5 - 9
(b) Real output <i>versus</i> real income	10 - 14
(c) Shifts in key relationships	15
(2) Changes in the Economic Environment:	
(a) General	16
(b) The exchange rate	17 - 21
(c) Protectionism and diversification	22 - 28
(d) Socio-economic influences on the flexibility of the cost/price structure	29 - 35
(e) The China dimension	36 - 37
PART II: THE PUBLIC FINANCES IN THE 1970s	
(1) Introduction	38
(2) General Revenue Account for 1979-80:	
(a) Budgetary policy	39 - 40
(b) Revised estimates:	41
(i) Outturn	42 - 43
(ii) Revenue	44 - 46
(iii) Expenditure	47 - 51
(c) Financial position at 31 March 1980	52 - 54
(3) Assessment of Performance in the 1970s:	
(a) General principles	55
(b) Implications for management in the early 1980s	56 - 61
PART III: THE IMMEDIATE OUTLOOK FOR THE ECONOMY AND THE PUBLIC SECTOR	
(1) Present State of the Hong Kong Economy:	
(a) Outlook at the end of 1978	62 - 67
(b) Budgetary policy	68 - 73
(c) Preliminary estimate of G.D.P. in 1979	74 - 84
(d) Assessment of adjustment process	85 - 95
(2) Acceptable Expenditure Limits for 1980-81	96 - 101
(3) Forecast of Expenditure on the G.D.P. in 1980:	
(a) Introduction	102
(b) Gross domestic product by component:	
(i) Private consumption expenditure	103

	<i>Paragraphs</i>
(ii) Government consumption expenditure	104
(iii) Gross domestic fixed capital formation	105 - 108
(iv) Exports	109 - 113
(v) Imports	114
(vi) Net exports of services	115
(vii) Stocks	116
(c) Total expenditure on G.D.P.	117
(d) Prices and G.D.P. at current prices	118 - 120
(e) Implications of the forecast for the economy	121 - 129
PART IV: THE BUDGET FOR 1980-81	
(1) Introduction	130
(2) Draft Expenditure Estimates:	
(a) Total expenditure	131 - 133
(b) Recurrent	134 - 140
(c) Capital	141 - 146
(3) Revenue Estimates:	
(a) Total revenue	147 - 148
(b) Recurrent	149 - 153
(c) Capital	154 - 159
(4) Outturn and Assessment	160 - 164
(5) Pattern of Expenditure on Consolidated Account	165 - 167
(6) Fiscal Policy:	
(a) General	168 - 170
(b) Reserves of taxable capacity	171 - 174
(c) Revaluation of rateable values	175 - 179
(d) Reassessment of assessable values for property tax	180 - 185
(e) Tax reforms in hand	186 - 187
(f) Tax reform proposed for 1980-81: contrived cessations of business	188
(g) Tax concessions proposed for 1980-81:	189
(i) Personal taxation	190 - 197
(ii) Interest tax liability of credit unions	198 - 199
(iii) Estate duty	200 - 201
(iv) Stamp duty on conveyances of low value properties	202 - 204
(v) Implementation	205
(7) Assessment and Outturn:	
(a) Balance of fiscal system	206
(b) Outturn and state of reserves	207 - 212

	<i>Paragraphs</i>
(8) The Public Sector and the Economy:	213
(a) Growth and relative size of the public sector	214
(b) Balance of the public sector	215

**PART V: THE PUBLIC SECTOR AND THE ECONOMY  
IN THE 1980s**

(1) Outlook for the General Revenue Account in the Forecast Period, 1981-82 to 1983-84	216 - 219
(2) Likely Developments in the Economy	220 - 229

<b>CONCLUSION</b>	230
-------------------	-----

Appendices I: Paragraphs 17-44 of the printed version of the Budget Speech 1980	
II: Paragraphs 86-121 of the printed version of the Budget Speech 1980	
III: Paragraphs 128-134 of the printed version of the Budget Speech 1980	

**ANNEXES**

***REFERENCE  
IN SPEECH***

(1) The Hong Kong Economy 1970-79: Growth rates of selected aggregates and variables	f.n. (14)
(2) General Revenue Account 1970-71 to 1980-81	f.n. (35), f.n. (125), f.n. (142)
(3) Application of Cash Limits 1979-80	f.n. (47)
(4) Summary of Consolidated Account expenditure by main functions 1970-71 to 1980-81	f.n. (98) in Appendix II
(5) Summary of actual revenue by main sources 1970-71 to 1980-81	f.n. (113) in Appendix II
(6) Balance of the fiscal system 1970-71 to 1980-81	f.n. (116) in Appendix II
(7) Fiscal changes 1970-71 to 1979-80 (in terms of the requirements of fiscal policy)	para. 111 in Appendix II

	<i>Reference in Speech</i>
(8) Budgetary guidelines 1970-71 to 1980-81	f.n. (122) in Appendix II
(9) Forecast of expenditure on the Gross Domestic Product in 1980	f.n. (98)
(10) Financial Information System	—
(11) Expenditure in the Main Programme Areas	para. 133
(12) Summary of actual expenditure by main components 1970-71 to 1980-81	f.n. (127)
(13) Examples of salaries tax having regard to proposed increases in personal, child and dependent parent allowances	para. 197
(14) Effect on salaries tax of proposed increases in personal allowances	para. 197
(15) Income levels at which salaries tax payers enter the standard rate zone	para. 197

He said:—

### **MOTION**

Sir, I move that the Appropriation Bill 1980, which was published in an issue of the *Gazette Extraordinary* at 2 o'clock today, be read the second time.

### **ACKNOWLEDGEMENTS**

2 Laid on the table today, Sir, are the Draft Estimates of Expenditure for 1980-81, and the Revenue Estimates, together with the usual supporting documents<sup>(1)</sup>. For the ninth time, it gives me great pleasure publicly to acknowledge the assiduous efforts of all concerned in the preparation and production of these documents and the help I have received in preparing the budget and this speech<sup>(2)</sup>.

### **STRUCTURE OF SPEECH**

3 It would be a mistake to over-emphasize the fact that we are now moving from the decade of the 1970s into a new decade, the decade of the 1980s. But so profound were the changes wrought in the 1970s, not so much in

---

(1) For a list of all documents laid, see inside cover of the printed version of this speech.

(2) To a greater or lesser extent all departments have been involved, but particular mention must be made of the Finance Branch, Government Secretariat; the Economic Services and Monetary Affairs Branches, Government Secretariat; the Census and Statistics Department; the revenue departments; the translators from the Home Affairs Department; the Printing Department; and Economic Review Committee.

our geo-political circumstances—though there were changes there too—as in the size and structure of our economy, that we were faced with novel policy options and presented with many opportunities for responding, without taking undue risk, to the community's social needs and aspirations. Our ability to respond, of course, was due, in no small measure, to the foundations laid by our predecessors in the two previous decades, the 1950s and the 1960s. But the decade that has just ended possessed a dramatic—if at times somewhat turbulent—quality and we have entered the new decade on the crest of the most sustained period of fast growth we have ever recorded.

4 So, in this speech, I must take a long, hard look at the course of development of our economy and the management of the public finances in the 1970s (PARTS I and II), before indulging in what is today a particularly dangerous pastime, forecasting, but I cannot avoid trying to define, in reasonably precise terms, the immediate outlook for the economy (PART III). That will provide me with a hopefully reliable basis for explaining and defending the budget for the year ahead, 1980-81 (PART IV). I shall wind up the speech by trying to assess the outlook for the public sector in the new forecast period, 1981-82 to 1983-84, and by speculating on possible developments in the economy in the decade of the 1980s (PART V).

### ***PART I: THE ECONOMY IN THE 1970s***

#### *(1) Growth Performance*

##### *(a) New series of estimates of expenditure on the G.D.P.*

5 Before reviewing the economy in the 1970s using the national accounts framework, I must mention that there has been a major revision of our historical series of expenditure on the gross domestic product. An inevitable consequence of our continuing effort to improve and expand the coverage of our statistical services is that various series will, every now and then, have to be revised and even re-defined, but not for the purpose of obscuring the nature of problems facing us, despite charges to the contrary when we recently re-defined the money supply (M1 and M2) and bank loans and advances.

6 To those who choose to interpret the steady development of the Government's statistical services with a view to improving our understanding of the workings of the economy, as evidence of a tendency to increasing interventionism, I would say this: a better understanding of how the economy works, and of the course of its development over time, is more likely to discourage, than to encourage, the pursuit of interventionist policies, particularly in the context of this Government's commitment to the market—disciplined free enterprise economy.

7 By combining figures derived from the various economic surveys he has conducted in recent years, the Commissioner for Census and Statistics has



now put our series of estimates of expenditure on the G.D.P. on a firmer statistical base<sup>(3)</sup>. The new series represents an upward adjustment of about 10%, at any rate since 1973<sup>(4)</sup>. Although this revision is substantial, the dynamics of the economy as indicated by growth rates of G.D.P.<sup>(5)</sup> and of its major components remain largely unaltered.

8 On the basis of the new series, the average annual growth rate of G.D.P. in real terms over the ten years 1970 to 1979 was 9%. This is, in effect, a measure of the growth rate of the real *output* of the economy. Understandably,

(3) *An account of the revisions is given in The 1980-81 Budget: Estimates of Gross Domestic Product 1966-1978. The more important revisions are: first, the replacing of the token estimates of the net balance on invisible trade by concrete estimates derived from surveys aimed specifically at collecting data relating to the import and export of services; secondly, as estimates of consumption of domestically produced goods are now available from annual surveys of industrial production, they have been used to replace the old estimates, which were based on figures on local sales by manufacturing establishments in 1970 updated annually by such crude indicators as population growth; thirdly, as a result of the 1977 benchmark survey of wholesale and retail trades which provided information on changes in stocks held by distributors, the assumption used in preparing the old estimates of private consumption expenditure, namely, that all consumer goods imported and goods sold by local producers to distributors were consumed in the same year, is no longer necessary.*

(4) *G.D.P. at current prices:*

Year	Old series	New series	(2) as a % of	New series (per capita) (\$)
	(\$ mn) (1)	(\$ mn) (2)	(1)	
1970	18,670	19,214	102.9	4,853
1971	20,976	21,873	104.3	5,407
1972	24,156	25,854	107.0	6,282
1973	30,736	33,964	110.5	8,062
1974	35,252	38,786	110.0	8,979
1975	37,268	40,574	108.9	9,230
1976	47,266	51,973	110.0	11,695
1977	54,823	59,429	108.4	13,166
1978(*)	63,633	69,174	108.7	15,017
1979(*)	81,128	87,345	107.7	17,825

\*)

Notes: (\*) *Provisional estimates.*  
(\*\*) *Preliminary estimates.*

(5) *G.D.P. at constant prices:*

Year	Old series (1966 prices)		New series (1973 prices)	
	(\$ mn)	(%)	(\$ mn)	(%)
1970	15,211	5.7	25,344	6.2
1971	15,704	3.2	26,612	5.0
1972	16,838	7.2	29,190	9.7
1973	19,229	14.2	33,964	16.4
1974	19,657	2.2	34,574	1.8
1975	20,230	2.9	35,349	2.2
1976	23,608	16.7	42,005	18.8
1977	26,411	11.9	46,131	9.8
1978(*)	29,057	10.0	50,753	10.0
1979(**)	32,530	12.0	56,577	11.5

Notes: (\*) *Based on provisional estimates.*  
(\*\*) *Based on preliminary estimates.*

for an economy as externally oriented as ours, the level of economic activity in any year was highly responsive to changes in the world trading environment; and, as the decade of the 70s covered a period within which the world economy experienced its worst post-war recession, the growth rate of the Hong Kong economy varied widely as between individual years (although, somewhat fortuitously, having regard to the different causative factors at work, the rate has been steady at around 10% in the past three years)<sup>(6)</sup>.

9 The decade started with two years of relatively slow growth: the growth rate of G.D.P. in real terms in 1970 and 1971 was 6.2% and 5% respectively. Consistent with the expansion of world trade, the growth rate of G.D.P. accelerated in 1972 to 9.7% and, then, in 1973, to 16.4%. Subsequently, the recession brought the growth rate sharply down to 1.8% in 1974 and 2.2% in 1975. But the recovery from the recession was even sharper, thanks to a very strong export performance in 1976: the growth rate of G.D.P. in that year was 18.8%, falling back to around 10% in 1977 and in 1978. Then, as the incomes generated by the post-recession surge in exports influenced the growth rate of domestic demand, the economy moved into a state of marked internal and external disequilibrium<sup>(7)</sup>. However, in 1979, although the economy's growth momentum was sustained at 11.5%, there was a lessening of the degree of disequilibrium<sup>(8)</sup>.

(b) *Real output versus real income*

10 Hong Kong's flexible cost/price structure has enabled the economy to adjust rapidly to changing external circumstances, with consequential shifts

(6) *Growth rates in real terms:*

Year	G.D.P. (%)	World exports(***) (%)
1970	6.2	8.7
1971	5.0	6.0
1972	9.7	10.4
1973	16.4	12.0
1974	1.8	4.6
1975	2.2	-3.6
1976	18.8	11.4
1977	9.8	4.2
1978(*)	10.0	4.5
1979(**)	11.5	5.0

Notes: (\*) Based on provisional estimates.

(\*\*) Based on preliminary estimates.

(\*\*\*) Derived from U.N. Statistical Yearbook. The 1979 growth rate is a forecast only.

(7) Internal equilibrium involves the demand for, and the supply of, the output of the economy remaining roughly in balance without domestic prices changing any faster than is justified by changes in the world prices of Hong Kong's imports. External equilibrium involves the balance of payments remaining in balance without any need for the relationship between interest rates in Hong Kong and interest rates elsewhere to change or any need for the effective exchange rate of the Hong Kong dollar to change.

(8) See paras. 85-95 below.

in the terms of trade<sup>(9)</sup>. In an economy as externally oriented as ours, such shifts must be taken into account when assessing the economy's performance because, when the terms of trade shift in our favour, the growth rate of real income (or real product consumed) is in fact faster than the growth rate of real output (or real product produced); and *vice versa*, when the terms of trade are shifting against us.

11 In fact, over the last decade, there was a net shift in the terms of trade in our favour. So, whilst the growth rate of real output as measured by the average annual growth rate of G.D.P. in real terms was 9%, the average annual growth rate of real income was higher at 9.5%<sup>(10)</sup>.

12 Over the decade, the average annual growth rate of real output *per capita*, which is a measure of output per head of the population, was 6.5%, whilst the average annual growth rate of real income *per capita*, which is a measure of spending power per head of the population, was higher at 6.9%<sup>(11)</sup>.

(9) *The terms of trade measure the relative movements in import and export prices, which result in a varying volume of imports being exchangeable for a given volume exports.*

(10)	G.D.P. at constant prices (%)	Growth rates of:		Terms of trade	
		Real income (%)	Index (1973=100)	Shifts (***) (%)	
1970	6.2	8.2	95	1.7	
1971	5.0	8.7	98	2.7	
1972	9.7	11.4	101	3.7	
1973	16.4	15.5	100	-1.2	
1974	1.8	-2.5	92	-7.6	
1975	2.2	3.4	94	2.2	
1976	18.8	22.7	100	5.9	
1977	9.8	8.9	99	-1.5	
1978(*)	10.0	9.2	97	-1.3	
1979(**)	11.5	11.1	97	-0.2	

Notes: (\*) Based on provisional estimate.  
(\*\*) Based on preliminary estimate.  
(\*\*\*) A negative sign (-) denotes a deterioration.

(11) Growth rates of:	Real output per capita (%)	Real income per capita (%)
1970	3.7	5.6
1971	2.7	6.4
1972	7.8	9.5
1973	13.7	12.8
1974	-0.7	-4.9
1975	0.5	1.6
1976	17.5	21.3
1977	8.1	7.2
1978(*)	7.8	7.0
1979(**)	4.8	4.4

Notes: (\*) Based on provisional estimate.  
(\*\*) Based on preliminary estimate.

13 The growth rates of total output and of output *per capita* showed roughly the same pattern over the years up to 1978. But the effect of the very substantial immigration which started in the second half of 1978 was such that, in spite of the acceleration in the growth rate of total output from 10% in 1978 to 11.5% in 1979, in *per capita* terms there was actually a fall in the growth rate from 7.8% in 1978 to 4.8% in 1979.

14 There were, of course, several supply side factors contributing to the growth rate of real output *per capita* of 6.5% over the decade. The age structure of the population changed as the population matured<sup>(12)</sup>. As a consequence, although the labour force participation rate fell slightly, the average annual growth rate of employment at roughly 3.8% was greater than that of the population at 2.4%. As hours worked per worker fell at an average annual rate over the decade of roughly 1.9%, output per man-hour rose at a creditable rate of 8%<sup>(13)</sup>.

(c) *Shifts in key relationships*<sup>(14)</sup>

15 So, notwithstanding the rather erratic growth path of the G.D.P., which was the inevitable result of the world recession compounded by the need for the cost/price structure to adjust in order to maintain external competitiveness, the growth performance of the economy over the decade as a whole was remarkable. The economy will undoubtedly continue to encounter disequilibrating forces in the coming decade as a result of changing internal and external circumstances. So, if the Government's responses are to be appropriate, it is important that there is a proper understanding by all concerned of the economic forces at work and their changing emphasis. This can best be acquired by an examination of the significant shifts in the key relationships between the growth rates in real terms of the main economic aggregates and in the rates of change of the main economic variables in the decade that has just ended. Honourable Members will find the results of such an examination in paragraphs 17 to 44 of the printed version of this speech (Appendix I).

(12) *Age structure of population (%)*:

<i>Age group</i>	<i>1970</i>	<i>1975</i>	<i>1979</i>
<i>Up to 14</i>	37.1	31.5	26.5
<i>15 to 64</i>	58.5	63.3	67.5
<i>Over 64</i>	4.3	5.3	6.0
<i>Total</i>	<u>100.0</u>	<u>100.0</u>	<u>100.0</u>

(13) *Average annual growth rates, 1971 to 1979, of:*

	(%)
<i>G.D.P.</i>	9.9
<i>Employment</i>	3.8
<i>Hours worked per worker</i>	-1.9
<i>Output per man-hour</i>	7.9

(14) *The analysis in paras. 17-36 in Appendix I is based on the statistics in Annex (1).*

(2) *Changes in the Economic Environment*

(a) *General*

16 Of the several changes in the environment within which the economy has had to operate, those in four areas are of particular significance, namely, the exchange rate regime, protectionism and diversification, the flexibility of the cost/price structure and the China dimension.

(b) *The exchange rate*

17 The Hong Kong dollar was tied to sterling up to the middle of 1972 and then linked to the Bretton Woods system of fixed parities through the U.S. dollar until 26 November 1974, when we were forced to abandon that link and let the Hong Kong dollar float freely, more or less, against all other currencies.

18 Our experience suggests that, under a floating exchange rate regime, when excess demand is leading to a widening of the visible trade 'gap'<sup>(15)</sup>, the initial adjustment is through a depreciation of the exchange rate. But the impact of this on the level of demand is relatively slow, particularly in a situation where credit is freely available<sup>(16)</sup>. In this sort of situation, the effect on the economy appears, at least initially, to be for the dampening effect of the increase in prices to be offset by increases in money incomes accommodated by increases in the money supply<sup>(17)</sup>. That is to say, in this sort of situation, adjusting interest rates upwards appears to have little effect on the level of demand for loans, perhaps partly because, in an inflationary period, increases in the real costs of borrowing tend to lag, for one reason or another, well behind increases in interest rates in nominal terms.

19 Thus, in recent years, the economy has maintained a high growth rate of G.D.P. in real terms with full employment but, latterly, at a cost in terms of upward pressure on the internal price level and a depreciated exchange rate. To the extent that increases in interest rates have attracted capital inflows, or prevented capital outflows, the extent to which the exchange rate has had to depreciate has been reduced and the pressure on the internal price level has thereby been eased, but the process of bringing the growth rate of demand into line with output has been delayed.

20 In an economy like Hong Kong's which is highly dependent on imports, having few domestic substitutes, it is likely that the initial improvement in the balance of visible trade will have to arise more through an improvement in export performance, rather than through a decline in (total) imports. This will be particularly the case when the necessary downward adjustment in the growth rate of domestic demand is delayed by excessive credit creation.

---

(15) See f.n. (27) in Appendix I.

(16) See paragraph 35 in Appendix I.

(17) See f.n. (40) in Appendix I.

To the extent that prices in the rest of the world, and particularly in the economies of our major markets, happen to be increasing at the same time as the Hong Kong dollar is depreciating, exports may receive a further substantial stimulus.

21 Apart from an excessive growth rate of domestic demand, the timely efficiency of the adjustment mechanism may also be affected by capital inflows motivated by a wish to find a safe home for funds rather than by the relative attractiveness, in purely financial terms, of investment prospects in Hong Kong. To the extent that this happens when the exchange rate is depreciating<sup>(18)</sup>, it may restrict the extent of the depreciation and inhibit the achievement of internal and external equilibrium which the depreciation would otherwise bring about. It is difficult to be certain about when such situations have arisen, but it does appear that, in 1974, when Hong Kong switched from a fixed to a floating exchange rate regime, the exchange rate appreciated more as a result of capital inflows induced by political upheavals in South East Asia, than would have been justified by the balance of visible and invisible trade.

(c) *Protectionism and diversification*

22 Over the decade, the structure of the economy in terms of the relative importance of different sectors altered<sup>(19)</sup>. Within the manufacturing sector, the clothing and textiles industries remained predominant, but clothing replaced textiles as the largest individual industry. The relative shares of other industries within the manufacturing sector remained largely unchanged.

(18) *This would normally act as a disincentive to overseas investors unless the depreciation was viewed as temporary or unless the potential capital gain more than offsets the potential exchange rate loss.*

(19) *Contributions to the G.D.P. by industrial origin:*

	1970(*)	1979(**)
	(%)	(%)
<i>Primary Sectors:</i>	<u>2.2</u>	<u>1.4</u>
<i>Agriculture and fishing</i>	2.1	1.3
<i>Mining and quarrying</i>	0.1	0.1
<i>Secondary Sectors:</i>	<u>35.0</u>	<u>31.0</u>
<i>Manufacturing</i>	29.9	25.0
<i>Electricity, gas and water</i>	1.9	1.4
<i>Construction</i>	3.2	4.6
<i>Tertiary Sectors:</i>	<u>62.8</u>	<u>67.6</u>
<i>Wholesale and retail trade, and restaurants and hotels</i>	21.8	23.0
<i>Transport, storage and communications</i>	7.2	5.3
<i>Financing, insurance, real estate and business services</i>	14.3	21.0
<i>Community, social and personal services</i>	18.9	18.0
<i>Activities not adequately defined</i>	0.6	0.3

Notes: (\*) See Appendix 2 of The 1980-81 Budget: Estimates of Gross Domestic Product 1966-78.

(\*\*) Very rough estimates.

However, as the Advisory Committee on Diversification pointed out<sup>(20)</sup>, the broad picture is misleading in that, within industries, there were considerable changes and improvements in the range of products made. Many completely new and sophisticated product lines were introduced and many of the simpler product lines which had been the mainstay of the economy in previous decades were largely abandoned, partly because of the emergence of lower cost producers within this region and partly, at least as far as clothing and textiles were concerned, in response to the pressure to move up market induced by a progressive shift to various forms of protectionism.

23 This shift to protectionism in the 1970s, particularly in the second half of the decade, has probably limited the application of the adjustment mechanism. In a free trade situation, it was reasonable to assume that there was always an adjustment in the prices of Hong Kong's products that would improve their relative competitiveness sufficiently to generate the volume of sales necessary to offset a widening of the visible trade 'gap'. With our G.A.T.T. most-favoured-nation rights of access now more limited than in the past<sup>(21)</sup>, the downward adjustments of prices required, particularly for unrestrained items, might have to be much greater.

24 As well as structural changes within the manufacturing sector in the 1970s, there was a gradual shift in favour of tertiary sectors. Their increasing importance to Hong Kong's foreign exchange earnings<sup>(22)</sup> has made our economy less dependent than previously on a relatively limited range of manufactured goods. This should have made the economy less vulnerable to the vagaries of international trade, particularly changes in taste and increases in protectionism. The tertiary sectors are also characterized by having a relatively high value-added per employee and most of them are not land intensive.

25 There has been a particularly marked shift in favour of the financial and related business services sector<sup>(23)</sup>. This resulted from Hong Kong's long established financial and mercantile community, which had traditionally concentrated on servicing the domestic economy, this resulted from that community placing a greater emphasis on exporting its services. In addition, the new opportunities for offshore lending and other financial transactions, particularly within the region, attracted an increasing number of overseas financial institutions to Hong Kong<sup>(24)</sup>.

---

(20) *Report (1979), paragraph 424.*

(21) *By the end of the 1970s over 60% by value of Hong Kong's exports of clothing and textiles were subject to restraint, compared with only 10% at the beginning of the 1960s.*

(22) *As reflected in the increasing invisible trade balance: see f.n. (29) in Appendix I.*

(23) *For a detailed analysis of the development of this sector, see Report of the Advisory Committee on Diversification (1979), Chapter IV.*

(24) *Initially, they established themselves here by setting up independently or by buying into existing banks; later, as opportunities for buying in dwindled, by setting up as deposit-taking companies; and finally, when the 1965 moratorium on the issue of bank licences was relaxed in 1978, by seeking licences for branches. The number of licensed banks in Hong Kong is now 115 (operating through 1,020 offices) compared with 74 before the moratorium was eased; and of registered deposit-taking companies is 271.*

26 The expansion of the financial and related business services sector has been associated with a diversification of markets, with profound implications for the economy as a whole. The great increase in the volume of funds flowing into and out of Hong Kong dollars, unconstrained by exchange controls, and the greater number of banks with relatively easy access to funds from their head offices or other institutions overseas, have probably exacerbated the slackening of restraint on the money supply and credit creation which was a consequence of the shift from a fixed to a floating exchange rate regime<sup>(25)</sup>. There is now a greater awareness by Hong Kong residents of the range of financial investment opportunities available internationally as access to them has become easier. Similarly, the stock market here is receiving more serious attention from overseas and the gold market has become much more integrated with markets elsewhere as world wide trading in gold has become a 24-hour activity.

27 However, these developments, valuable though they have been, these developments have increased, and made more volatile, movements of funds across the exchanges. In short, Hong Kong's financial markets have become much more international with benefits in terms of the additional incomes and employment generated through the volume of business being transacted, but at a cost in terms of the extent *to* which, and the ease *with* which, the Government can deal with situations particular to Hong Kong.

28 These developments call into question the present system for determining interest rates. The interest rate agreement of the Exchange Banks' Association was concluded in 1964, primarily as a defensive commercial arrangement between banks to limit competition for deposits. Although the Government has no formal role in the operation of the interest rate agreement, there has always been some consultation between the Government and those responsible for the operation of the agreement. With the greater recognition, particularly in the past eighteen months or so, of the role of interest rates in the adjustment mechanism under a floating exchange rate regime, the extent — and the frequency — of such consultation has increased substantially. However, the interest rate agreement does not now have the same impact on the domestic market as in the past. As a result, we simply must give serious consideration to the possible need for a different and more comprehensive system for determining interest rates. This is a subject to which I shall return later<sup>(26)</sup>.

(d) *Socio-economic influences on the flexibility of the cost/price structure*

29 A decade such as the 1970s, in which the average annual growth rate of G.D.P. *per capita* in real terms was 6.5% and the growth rate or real income *per capita* was even higher, inevitably involved some socio-economic changes which affected the operation of the adjustment mechanism.

---

(25) *For the consequences of the floating rate regime for the management of the Government's Hong Kong dollar balances see B.S., 1979, paras. 241-257.*

(26) *See paragraph 228 below.*



30 As the Advisory Committee on Diversification was at pains to emphasize<sup>(27)</sup>, with both the Hong Kong economy and the world economy becoming more complex and business organizations larger, there is a greater need for an educated work force. Entrepreneurial flair must increasingly be combined with professional managerial skills; and the work force must have the skills to understand and operate more sophisticated machinery. Over the decade, the marked premium in terms of salary available to those *with* education, the expanded facilities available *for* education and the increased prosperity of parents, which has meant that they can more easily support their children over a longer period of education, have combined to increase the average educational attainment of our labour force substantially<sup>(28)</sup>. To the extent that a better educated labour force is more able to learn new jobs and new skills, this improvement enhances the economy's ability to respond to changing circumstances and improves the efficiency with which the adjustment mechanism operates.

31 However, to the extent that the skills required to use more sophisticated machinery are more specialized and industry specific, the efficiency of the adjustment mechanism is impaired. This is particularly the case where the skills required take time to acquire and are developed by experience. In such circumstances, employers, instead of rapidly releasing workers extra to their immediate requirements, are likely to retain them, even if they are under-employed, because of the cost and problems of finding new workers later on. Workers thus retained are denied to other employers and labour supply bottlenecks may develop even if there is not full employment overall.

32 Greater prosperity also brings with it changes in demand patterns. However, although particular developments can be discerned, overall trends are less clear. Higher incomes are likely to lead to a greater propensity to buy imported goods rather than domestically produced goods, but may also lead to a greater proportion of incomes being spent on services, which typically have a low import content<sup>(29)</sup>.

---

(27) *Report (1979), Chapter IX.*

(28) *Distribution of labour force by educational attainment:*

<i>Level of attainment</i>	<i>1971</i>	<i>1976</i>	<i>1978</i>
<i>No schooling/kindergarten</i>	<i>16.4</i>	<i>13.8</i>	<i>12.6</i>
<i>Primary</i>	<i>50.7</i>	<i>45.0</i>	<i>42.9</i>
<i>Secondary</i>	<i>29.8</i>	<i>37.5</i>	<i>39.7</i>
<i>Tertiary</i>	<i>3.1</i>	<i>3.7</i>	<i>4.8</i>
<i>Total</i>	<u><i>100.0</i></u>	<u><i>100.0</i></u>	<u><i>100.0</i></u>

Source: *Derived from f.n. (49), page 29 of the Advisory Committee's Report.*

(29) *Except in the case of overseas travel.*

33 As regards the implications of the greater prosperity enjoyed in the decade of the 1970s for the public finances: to the extent that enhanced prosperity has been taken in the form of additional leisure<sup>(30)</sup>, rather than additional earnings, there have been additional demands on the transport infrastructure and for leisure facilities. As people have sought to set themselves up in smaller, separate households with improved space standards per person, the urban areas have expanded requiring the provision of infrastructure and services on a greater scale and over a greater area. And because there is a limit to the extent to which people will put up with public squalor, while enjoying increased private affluence, there has been continual pressure for the quality of the publicly provided services and infrastructure to be improved.

34 The provision of this additional infrastructure has become increasingly costly. This is not a feature unique to Hong Kong, but is almost certainly exacerbated by our geographical constraints. The development of Hong Kong has meant increasingly intensive use of our scarcest resource, land. Infrastructural developments compete with other developments—commercial, industrial and residential—for the use of this scarce resource. Often, existing or other competing developments have forced us to adopt expensive solutions to the problems of providing an adequate infrastructure.

35 The decision to develop the new towns went some way to offsetting the impact of the finite and limited supply of land within the urban areas. However, given the strong attractions of the thriving and established urban areas, the influence of this decision will take some time to show through.

(e) *The China dimension*

36 The rapid development of Hong Kong's manufacturing sector followed upon the collapse of the *entrepot* trade in 1951. The export of manufactured goods qualifying for Hong Kong Certificates of Origin remains the main source of foreign exchange earnings, supplemented increasingly by the export of services. However, during the 1970s, Hong Kong's role as an entrepot for the region developed fast, and this was accompanied by a re-emergence of its role as an *entrepot* for China, particularly since 1978<sup>(31)</sup> and the growing use of Hong Kong by foreign firms as a base for seeking to do business with China. At the same time, of course, the importance of China as a source of

(30) See f.n. (13) above.

(31)

Year	Value of re-exports from China (\$ mn)	Share of Hong Kong's total re-exports (%)
1974	1,582	22.2
1975	1,743	25.0
1976	2,402	26.9
1977	2,492	25.3
1978	3,659	27.7
1979	5,663	28.3

imports<sup>(32)</sup> has remained virtually undiminished. Retained imports from China, moreover, represent even today about 2½ times the value of re-exports of China origin.

37 As regards the prices charged by China for its exports to Hong Kong, up to the early 1970s these were set at, or below, world prices and generally were more stable than world prices. Thus, Hong Kong benefitted, particularly as regards foodstuffs, from having a secure supply at relatively low and stable prices. However, more recently—indeed, since the floating of the Hong Kong dollar—there has been a tendency for the prices charged by China's trading organizations to move up to, and in line with, world prices. This is only to be expected given China's increasing emphasis on maximizing foreign exchange earnings in order to finance its 'four modernizations' programme, but it has become a new factor in our situation<sup>(33)</sup>.

## **PART II: THE PUBLIC FINANCES IN THE 1970s**

### (1) *Introduction*

38 Before reviewing the performance of the public sector, defined in terms of the Consolidated Account<sup>(34)</sup>, and evaluating the management of our public finances on General Revenue Account in the 1970s, I must bring honourable Members up to date on the state of the Government's accounts. I shall conclude this part of my speech by suggesting that our experience in the 1970s has certain implications for the management of the public finances in the decade before us.

(32) *Imports of goods by end use (1979):*

	All imports (\$ mn)	Imports from (2) as % China (\$ mn)	of (1)
Foodstuffs	9,968	4,520	45.3
Consumer goods	21,530	3,959	18.4
Fuels	4,676	1,401	30.0
Raw materials and semi-manufactures	37,507	4,899	13.1
Capital goods	12,157	350	2.9
Total	<u>85,837</u>	<u>15,129</u>	<u>17.6</u>

(33) *For an analysis of Hong Kong's economic relationship with China up to 1979, see the Report of the Advisory Committee on Diversification (1979), Chapter V, section (2); and see also f.n. (196) and paragraph 229 below.*

(34) *That is, expenditure by the Urban Council and the Housing Authority, expenditure financed by certain statutory funds (Development Loan Fund, Home Ownership Fund, Lotteries Fund and Student Loan Fund) and all expenditure charged to the General Revenue Account. So expenditure by institutions in the private or quasi-private sector is included to the extent of their subventions. The activities of Government departments which are partly financed by charges raised on a commercial basis are also included (e.g. Kowloon- Canton Railway, Airport, Waterworks). But not included is expenditure by those organizations, including even statutory organizations, in which the Government has only an equity position, such as the Mass Transit Railway Corporation.*

(2) *General Revenue Account for 1979-80*(a) *Budgetary policy*

39 The emphasis of budgetary policy this year, in both the wider and narrower sense, reflected our anxieties about the growth rate of total final demand in 1978 which exceeded the growth rate of G.D.P., resulting in a rapid growth rate of imports accompanied by a growth rate of domestic demand in excess of the growth rate of exports, implying a relative shift of resources away from the manufacturing sector. So budgetary policy in 1979-80 sought, *first*, to slow down the growth rate of public sector expenditure on Consolidated Account from 22% in 1978-79 to 7.5% in 1979-80 and, ideally, to reduce the relative size of the public sector so defined from its record high level; and, *secondly*, budgetary policy in 1979-80 sought at least to stabilize the share of the total output of the building and construction industry absorbed by the public sector (including the Mass Transit Railway Corporation for *this* purpose), the share having increased to 49% by 1978.

40 Within the public sector so defined, expenditure on General Revenue Account is usually around 90% of expenditure on Consolidated Account. For this reason, and because it is directly under the Government's control, it is the main instrument of budgetary policy.

(b) *Revised estimates*<sup>(35)</sup>

41 So, on General Revenue Account, after taking account of my revenue proposals<sup>(36)</sup>, I budgetted in 1979-80 for a surplus of \$1,455 million being the difference between estimated expenditure of \$12,433 million and estimated revenue of \$13,888 million. I believed the increase in expenditure budgetted for, which was 13% up on the revised estimate of \$11,027 million for 1978-79, to be the equivalent of 5% only in real terms. Given our anxieties about the economy, and given the expected 35% surge in expenditure in 1978-79, being the equivalent of 25% in real terms, I budgetted in 1979-80 for a surplus which was the equivalent of more than 10% of estimated revenue (and the budget conformed—in fact, was well within—all five guidelines<sup>(37)</sup>).

---

(35) See Annex (2).

(36) At a net cost to the revenue of \$6 million: see B.S., 1979, paras. 169-217.

(37)		\$ mn	%	Guideline
(1)	$\frac{\text{Recurrent revenue}}{\text{Total expenditure}}$	$\frac{11,476}{12,433}$	= 92	At least 88%
(2)	$\frac{\text{Recurrent expenditure}}{\text{Recurrent revenue}}$	$\frac{8,360}{11,476}$	= 73	No more than 80%
(3)	$\frac{\text{Surplus on recurrent account}}{\text{Capital expenditure}}$	$\frac{3,116}{4,073}$	= 77	At least 60%
(4)	$\frac{\text{Recurrent expenditure}}{\text{Total expenditure}}$	$\frac{8,360}{12,433}$	= 67	No more than 70%
(5)	$\frac{\text{Capital revenue}}{\text{Capital expenditure}}$	$\frac{2,412}{4,073}$	= 59	At least 20%

(i) *Outturn*

42 The revised estimates of revenue and expenditure for 1979-80 are \$16,550 million and \$14,232 million respectively. Thus the year's operations will result in a surplus of \$2,318 million<sup>(38)</sup>. This figure does not quite match up with the surplus derived from the Treasury's cash book of the 14 February, so I shall use a figure of \$2,500 million when considering our cumulative financial position at 1 April next.

43 The surplus, whether it be \$2,318 million or \$2,500 million, will be the highest on record in absolute terms, but only the fourth highest on record over the past ten years as a percentage of total revenue<sup>(39)</sup>. For the third year running this larger than budgeted for surplus—\$2,318 million rather than \$1,455 million—is due to a flush of revenue rather than a failure of expenditure<sup>(40)</sup> (*laughter*), but this outcome is entirely consistent with the constraining objective of budgetary policy in 1979-80. If it is any comfort to honourable

(38)	\$ mn		\$ mn	
	O/A.E.	R.E.	O/A.E.	R.E.
<i>Recurrent Account:</i>				
Revenue	11,476	13,214	—	—
Expenditure	8,360	9,081	+3,116	+4,130
<i>Capital Account:</i>				
Revenue	2,412	3,336	—	—
Expenditure	4,073	5,151	-1,661	-1,812
Overall surplus	—	—	+1,455	+2,318

Notes: O/A.E. = Original/Approved Estimates.  
R.E. = Revised Estimates.

(39)	Surplus (\$ mn)	% of total revenue
1970-71	622	21.3
1971-72	643	19.2
1972-73	1,139	24.4
1973-74	374	7.5
1974-75	- 378	6.3 (of total expenditure.)
1975-76	232	3.7
1976-77	917	12.2
1977-78	1,225	13.0
1978-79	1,486	11.9
1979-80 (R.E.)	2,318	14.0

(40)	Revenue (\$ mn)		Expenditure (\$ mn)	
	O.E.	Actual	A.E.	Actual
1977-78	8,172	9,383	8,119	8,158
1978-79	10,131	12,442	10,131	10,956
1979-80	13,888	16,550 (R.E.)	12,433	14,232 (R.E.)

Notes: O.E. = Original Estimates.  
A.E. = Approved Estimates.  
R.E. = Revised Estimates.

Members, the error is much less than in the previous two years<sup>(41)</sup> (*laughter*), but it reflects rather substantial differences between the approved estimates of revenue and expenditure and the revised estimates.

(ii) *Revenue*

44 At \$16,550 million, the revised estimate of revenue exceeds the original estimate of \$13,888 million by \$2,662 million, or by 19%.

45 *Recurrent* revenue at \$13,214 million is up by a net \$1,738 million<sup>(42)</sup>, or by 15%, on the original estimate: earnings and profits taxes are up by \$889 million, or by 18%, due to company profits, particularly in the property and banking sectors, being more buoyant than could reasonably be assumed by a reasonable man when the Revenue Estimates were prepared: interest earnings are up by a massive \$514 million, or by 104%<sup>(43)</sup>, for obvious reasons (that is to say larger fiscal reserves and high interest rates); and the yield from duties on dutiable commodities is up by \$97 million, or by 12%, as consumption this year has proved to be much less price elastic than I expected on the basis of our experience last year (which reminds me, Sir, of the humourist's complaint about inflation: don't worry about the prices of necessities, just let me buy my little luxuries).

46. *Capital* revenue at \$3,336 million is up by \$924 million, or by 38%, on the original estimate as premia from land transactions are up by \$886 million, or by 45%, and the yield from estate duty is up by \$55 million, or by 41%. There are two reasons for the substantial increase in revenue from land transactions: higher prices on the sale of 95 acres of land and the abolition of the instalment payment system on commercial/residential sites from 1 December 1979.

(iii) *Expenditure*

47 At \$14,232 million, the revised estimate of expenditure exceeds the approved estimate of \$12,433 million by \$1,799 million, or by 14.5%; and so, for the third year running, actual expenditure will exceed the approved estimate. Not only does this contrast with our experience in 1975-76 and in

(41)

	<i>Budget</i> (\$ mn)	<i>Surplus:</i> <i>Actual</i> (\$ mn)
1977-78	53	1,225
1978-79	Nil	1,486
1979-80	1,455	2,318 (R.E.)

(42) That is, + \$1,762 million — \$24 million = \$1,738 million. For a detailed analysis of the differences between the revised estimates of revenue and the original estimates, see the memorandum notes on the Revenue Estimates for 1980-81.

(43) To \$1,006 million, more than enough to finance the entire cost of the R.H.K.P.F. and the R.H.K.A.P.F.

the first post-recession year 1976-77<sup>(44)</sup>, but also, at 14.5%, the relative excess this year is likely to be nearly twice that in 1978-79, despite our declared intention, on budgetary policy grounds, to insist on a strict adherence to cash limits. That is to say, the intention was that the provision under the various heads of expenditure would be limiting, the cost of new or amended policy decisions and of a higher than expected rate of inflation being financed from savings. In this latter event, the implication was that there would be a cutback in the intended growth rate of expenditure in real terms<sup>(45)</sup>. But, realistically, I made two exceptions to this cash limit rule: civil service salary adjustments and the cost of measures to combat illegal immigration<sup>(46)</sup>. Having regard to these two exceptions, the Finance Branch did manage to ensure that cash limits *were* generally adhered to on recurrent account<sup>(47)</sup>, but circumstances prevented their being adhere to on capital account.

48. On *recurrent* account, at \$9,081 million, there is net over-spending of \$721 million, or nearly 9%, largely due to the Pay Trend Survey salary revision with effect from 1 April and the implementation of Report No. 2 of the Standing Commission on Civil Service Salaries with effect from 1 October, which required together (net) additional provision of \$409 million, bringing the total wage bill of the civil service to \$3,560 million for roughly 140,000 posts, or to 39% of total recurrent expenditure. For the same reason, additional provision of \$145 million is required for subventions (including the U.P.G.C.)<sup>(48)</sup>. The only head on which there was substantial over-spending —of \$96 million, or 27%—was Head 28 Defence: Miscellaneous Measures. The Hong Kong dollar equivalent of our 75% contribution to the recurrent cost of the garrison increased as the Hong Kong dollar/sterling exchange rate declined from \$8.50 to the pound, the rate assumed when the Estimates were prepared, to actual rates ranging from \$9.70 to \$11.40 to the pound.

(44)	<i>Shortfall/excess on Approved Estimates (\$ mn)</i>	<i>% of Approved Estimates</i>
1975-76	—585	8.8
1976-77	—620	8.6
1977-78	+ 39	0.5
1978-79	+ 825	8.1
1979-80 (R.E.)	+1,799	14.5

(45) *B.S., 1979, paras. 237 and 265.*

(46) *B.S., 1979, paragraph 246.*

(47) *See Annex (3).*

(48) *Not including the full cost of implementing the recommendations of Report No. 2 of the Standing Commission on Civil Service Salaries.*

49 On *capital* account, at \$5,151 million<sup>(49)</sup>, there is net over-spending of \$1,078 million, or nearly 27%, of which \$591 million is accounted for by Component (1): Public Works Programme (other than New Towns and Housing). About \$209 million of this excess, or the equivalent of 16% of the approved estimate of \$1,299 million for Component (1), reflects the fact that the cash limits concept could not be applied too rigorously when price increases exceeded expectations, that is to say, when the provision available against project subheads for on-going contracts was much less than that required when fluctuation clauses were invoked and when tender prices for new contracts exceeded the project estimates. In addition, an extra \$382 million is required for extraordinary items of expenditure unforeseen when the Estimates were prepared, such as camps for Vietnamese refugees, the purchase of Fairmount Gardens and additional expenditure on dangerous slopes.

50 At \$4,238 million, the revised estimate of expenditure on the two Public Works Programme components of the capital account, *plus* transfers to the

(49)	<i>Component</i>	<i>Approved Estimates 1979- 80 (\$ mn)</i>	<i>Revised Estimates 1979- 80 (\$ mn)</i>
(1)	<i>Public Works Programme (other than New Towns and Housing)</i>	1,299	1,890
(2)	<i>Public Works Programme (New Towns and Housing)</i>	1,300	1,348
(3)	<i>Land Acquisition</i>	(*)	(*)
(4)	<i>Transfers to D.L.F. for on-lending to the Housing Authority</i>	1,000	1,000
(5)	<i>Transfers to Home Ownership Fund</i>	—	—
(6)	<i>Subventions:</i>		
	<i>Education</i>	77	81
	<i>Medical</i>	29	23
	<i>Miscellaneous</i>	1	2
(7)	<i>University and Polytechnic Grants Committee</i>	85	136
(8)	<i>Departmental Special Expenditure</i>	184	207
(9)	<i>Defence Costs Agreement: Capital Works</i>	30	29
(10)	<i>Defence: Miscellaneous Measures</i>	34(**)	172(***)
(11)	<i>Other Transfers:</i>		
	<i>Emergency Relief Fund</i>	3	10
	<i>Student Loan Fund</i>	—	181
(12)	<i>Miscellaneous</i>	31	72(****)
	<i>Total capital expenditure</i>	4,073	5,151

Notes: (\*) Included in Components (1) and (2).

(\*\*) Re-provisioning of Victoria Barracks and R.A.F. Kai Tak and Lyemun and Sham Shui Po Barracks and other additional capital works for the Armed Forces outside the terms of the Defence Costs Agreement.

(\*\*\*) As for (\*\*) above, plus \$105 million being the cost of reinforcements of the garrison (treated as non-recurrent expenditure).

(\*\*\*\*) Includes \$32 million for expenses relating to Vietnamese refugees (treated as non-recurrent expenditure).



Development Loan Fund for on-lending to the Housing Authority, exceeds the approved estimate by \$639 million, or by 18%. This repeats our experience in 1978-79, when the approved estimate of these Components was exceeded by 44%. So the last two years are in marked contrast with the under-spending against approved estimates in 1975-76 and 1976-77(50).

51 The remaining \$439 million worth of additional provision required this year is for capital subventions (including U.P.G.C.), for the reinforcement of the garrison, expenditure on which is regarded as non-recurrent, the recently established Student Loan Fund and expenses connected with refugees which again are regarded as non-recurrent expenditure.

(c) *Financial position at 31 March 1980*

52 Assuming that the surplus on General Revenue Account in 1979-80 transferable to the General Revenue Balance(51) at 31 March next is \$2,500 million, our fiscal reserves at the beginning of the financial year 1980-81 will be about \$8,900 million(52). After allowing, say, \$3,200 million as cover for our formal contingent liabilities (which will be of the order of \$9,600 million by 31 March 1984, the last year of the new forecast period(53). After allowing \$3,200 million is covered from our formal contingent liabilities at 1 April

(50)	<i>Shortfall/Excess on Approved Estimates</i> (\$ mn)	<i>% of Approved Estimates</i>
1975-76	—354	22
1976-77	—474	30
1977-78	+ 73	5
1978-79	+886	44
1979-80 (R.E.)	+639	18

(51) *That is, the cash book balance exclusive of the adjustments made to annual revenue and expenditure on General Revenue Account for analytical purposes: see Annex (2).*

(52) *That is, General Revenue Balance at 1 April 1979=\$6,416 million+predicted surplus of \$2,500 million=\$8,916 million.*

(53)	<i>At 31 March:</i>		
	<i>1980</i> (\$ mn)	<i>1983 (peak)</i> (\$ mn)	<i>1984</i> (\$ mn)
<i>Guarantees of M.T.R.C. debt</i>	4,417	5,606	4,659
<i>Export Credit Insurance Corporation: outstanding amounts</i>	1,751	2,597	2,857
<i>Home Ownership Scheme: guarantees to banks</i>	100	989	1,210
<i>Asian Development Bank: uncalled capital</i>	243	463	463
<i>Gold coins</i>	147	194	234
<i>Buildng and Loan Agency: guaranteed notes</i>	165	165	165
<i>Demonetized currency notes</i>	10	10	10
<i>Total</i>	<u>6,833</u>	<u>10,024</u>	<u>9,598</u>

next we shall have 'free' reserves of around \$5,700 million to finance our seasonal deficits on General Revenue Account<sup>(54)</sup>, and any unexpected short-term difficulties and emergency situations which cannot be—and, indeed, *should* not be—dealt with by a revision of expenditure authorities or by fiscal measures. The level of our 'free' fiscal reserves is also such as to enable us to maintain a given level of expenditure<sup>(55)</sup>, without resorting to debt finance, as and when the revenue and expenditure estimates breach the relevant guidelines; and as and when the financing of capital expenditure becomes more dependent again on the surplus on recurrent account. In the first seven years of the decade, the ratio of capital revenue to the surplus on recurrent account averaged 39%; in the last three it has been double that at 77%<sup>(56)</sup>.

53 Thus our 'free' reserves at 1 April 1980 will be the equivalent of 31% of estimated expenditure next year of \$18,332 million<sup>(57)</sup> which is distinctly better than our guideline of 15% of estimated expenditure in the ensuing year and, in fact, the relative size of our 'free' reserves has doubled since 1977-78.

54. The available assets in the Development Loan Fund<sup>(58)</sup> and the Lotteries Fund<sup>(59)</sup> are not included in our fiscal reserves for they are committed to approved loan allocations. Nor are the net proceeds from the sale of our gold coins: when the accounts for the Year of the Monkey coin have been

---

(54) *These normally peak in October after which E.P.T. receipts begin to flow in.*

(55) *By a given level of expenditure, I mean a level necessary for policy reasons and appropriate in terms of the capacity of the economy.*

(56) *See, further, paragraph 61 below.*

(57) *Inclusive, for this purpose, of public debt repayments of \$304 million.*

(58) *Available assets in the Development Loan Fund at 1 April 1980 will be \$268 million against outstanding allocations of \$2,838 million of which \$2,398 million is for housing(\*); \$139 million for flatted factories; \$10 million for non-profit-making schools, and \$284 million for the Industrial Estates Corporation. As the available assets in the Fund are not sufficient to meet the anticipated calls to be made on the Fund during 1980-81, estimated at \$2,040 million, a sum of \$1,831 million has been entered in the commitment and provision columns under Head 87 Transfers to Funds Subhead 291 Payment to the Development Loan Fund.*

*Note: (\*) Housing Authority (\$2,328 million for public housing and \$16 million for the commercial elements of the Home Ownership Scheme); Housing Society (\$44 million for the Urban Improvement Scheme); Local Government Officers' Housing Schemes (\$2 million); and Hong Kong Building and Loan Agency Ltd. (\$8 million for guaranteed notes).*

(59) *Available assets in the Lotteries Fund at the same date will be \$66 million to which must be added estimated receipts during the year of \$47 million. Payments in 1980-81 against approved and new allocations are likely to be \$47 million, leaving a balance in the Fund of \$66 million at 31 March 1981. Outstanding allocations will amount to \$33 million. However, it is expected that the accumulating surplus in the Fund will be exhausted within the forecast period as a result of increased demand on the Fund's resources in connection with proposals in the White Paper entitled Social Welfare into the 1980s.*

finalized, the surplus in the Special Coin Suspense Account is expected to be about \$122 million<sup>(60)</sup>.

(3) *Assessment of Performance in the 1970s*

(a) *General principles*

55 During the 1970s the public finances were managed, more or less, on the basis of the following four sets of principles: *first*, that the growth rate of public expenditure, appropriately defined, should have regard to the growth rate of the economy and, allied to this, the relative size of the public sector should bear a certain relationship to the gross domestic product; *secondly*, that the changing pattern of expenditure on Consolidated Account should reflect the Government's view as to priorities; *thirdly*, that the fiscal system should be so designed as to achieve a certain balance between direct and indirect taxation and between direct and indirect taxation taken together and all other recurrent revenue, and that our tax system as such should meet certain defined requirements; and, *fourthly*, that the annual estimates of revenue and expenditure on General Revenue Account should observe certain guidelines with a view to ensuring that capital expenditure can be financed without recourse to debt (or, at worst, a limited recourse only) and to maintaining a certain relationship between our 'free' fiscal reserves and our budgetary commitments, enabling us to achieve a steady rate of implementation of the Government's programmes and policies. At paragraph 86-121 of the printed version of this speech (Appendix II) honourable Members will find a critical analysis of how successfully or otherwise we apply these four sets of principles over the decade.

(b) *Implications for management in the early 1980s*

56 This analysis which I trust they will study with care (*laughter*) has led me to the conclusion that for the proper management of the public finances in the 1980s I see no reason to depart from, or to amend, the four sets of principles which guided us in the past decade, but five points emerge from it.

57 *First*, the trend growth rate of public expenditure must not be allowed to exceed the trend growth rate of G.D.P. to such an extent and so persistently that the relative size of the public sector becomes excessive. By the end of the decade it was 18.7% and, whilst I do not regard this as an absolute limit, any further increase must be carefully watched.

---

(60) *As the state of the secondary market clearly indicates that none of the coins will be returned to the Treasury for redemption, this surplus will be progressively available for public purposes and, when the series is completed, the surplus in the Suspense Account should exceed \$400 million. So far, we have earmarked \$13 million for the Queen Elizabeth Stadium(\*) and \$25 million for the Jubilee Sports Centre at Sha Tin.*

Note: (\*) *Of the total cost of \$49.7 million, the balance of \$36.7 million is being financed as follows: General Revenue, \$21.4 million; Urban Council, \$5.3 million; Royal Visit Commemorative Fund, \$10.0 million.*

58 *Secondly*, it would not be sensible to try to fix upon, for all time, an ideal pattern of expenditure on Consolidated Account, because the Government's priorities must be readily adjusted in response to changing circumstances, and in response to the view taken, from time to time, as to the priorities best suited to the public interest. In the early years of the 1980s, however, it seems clear that the maintenance of law and order, the integrity of our land and sea borders, the transport infrastructure, land production and housing stand out as deserving especial priority<sup>(61)</sup>.

59 *Thirdly*, the tendency in the last four years of the past decade for the balance of the fiscal system to slip away even from the revised ratios introduced in 1977-78 must be corrected, and so must the present distribution of the burden between different classes of taxpayers, I repeat, between different classes of taxpayers.

60 *Fourthly*, as regards the management of the General Revenue Account, the tendency for the ratio of recurrent revenue to total expenditure to be on a *downward* trend in the past four years, coupled with the fact that the ratio of capital expenditure to total expenditure has been on an *upward* trend, means that the fiscal system will have to be made more productive of recurrent revenue. Although the growth rate of recurrent expenditure has been well contained, the level of capital expenditure has been lifted very substantially indeed in recent years, with the result that the ratio of recurrent revenue to total expenditure has been falling steadily<sup>(62)</sup>. The absence of an overall deficit simply reflects the present availability of capital revenue for the financing of the capital account, thus indicating a potential need to correct this by boosting recurrent revenue.

61 *Fifthly*, the divergent trends of the ratio of recurrent revenue to total expenditure and of capital expenditure to total expenditure also mean that care must be taken not to lose control of the level of capital expenditure. We simply must not get ourselves locked into a level of capital expenditure which is not sustainable. So Guideline (4) may no longer realistically define a balanced budget in terms of the desired relationship between recurrent and capital expenditure. In the last three years, capital revenue has been sufficient to finance two-thirds of capital expenditure and, as we shall see later on, it will finance an even higher proportion than this in 1980-81. But the management of the capital account in the next few years must not be based on the assumption that the ratio of capital revenue to the surplus on recurrent account will not return, at some time in the not too distant future, to a more normal level<sup>(63)</sup>.

---

(61) *For the pattern of expenditure on Consolidated Account in 1980-81, see paras. 165-167 below.*

(62) *This ratio has not yet breached the guideline of 88%, but is expected to do so in 1980-81. The only other year in which it was breached was in 1974-75 when the General Revenue Account was in overall deficit.*

(63) *As noted in paragraph 52 above, this ratio averaged 39% in the first seven years of the decade to 1976-77 and then jumped to 77% in the last three years. It will be as high as 161% in 1980-81.*

*PART III: THE IMMEDIATE OUTLOOK FOR THE ECONOMY AND THE PUBLIC SECTOR*

*(1) Present State of the Hong Kong Economy*

*(a) Outlook at the end of 1978*

62 The immediate outlook for our economy has to be assessed, not only in the context of the apparent outlook for the world economy, which I have tried to assess in paragraphs 128-134 of the printed version of this speech (Appendix III) but also in the context of an economy which has enjoyed four years of double digit growth. We entered 1979, the fourth year of rapid growth, against the following background: in 1978, the growth rate of total final demand exceeded the growth rate of G.D.P., resulting in a rapid growth rate of imports (particularly of consumer goods); within total final demand, the growth rate of domestic demand exceeded the growth rate of domestic exports of goods, implying a shift of resources away from the manufacturing sector; within domestic demand, the growth rate of public sector demand exceeded the growth rate of private sector demand and so the relative size of the public sector increased; the growth rate of demand by the public sector for the output of the building and construction industry far exceeded in 1978 the growth rate of demand by the private sector; the growth rate of private consumption expenditure was higher than might have been expected in 1978, given the growth rates of real income in 1977 and 1978<sup>(64)</sup>; the growth rate of imports far exceeded the growth rate of total exports and so the visible trade 'gap' widened from 8.1% in 1977 to 14.8% in 1978<sup>(65)</sup> and, during the year, during 1978, the exchange value of the Hong Kong dollar depreciated by 12.6% (having depreciated already by 6.8% in 1977<sup>(66)</sup>). Reflecting these imbalances there was an excess of demand for, over supply of, domestic resources of land, labour and capital with consequent pressures on prices and the money supply<sup>(67)</sup>.

63 So, in 1978, the growth rates and rates of change of the operative economic aggregates and variables were quite inconsistent with the attainment, let alone the maintenance, of economic stability. In other words, the economy was in a state of increasing disequilibrium. No economy can remain in such a state indefinitely and, sooner or later, counteracting forces will be generated

---

*(64) See f.n. (10) above.*

*(65) See f.n. (27) in Appendix I.*

*(66) The trade weighted exchange rate index (18 December 1971=100) fell from 106.1 at 31 December 1977 to 93.2 at 31 December 1978 (12.6%); the export weighted index fell from 111 to 101 (9.1%); and the import weighted index from 102 to 88 (14.3%). For changes in the daily average of the index, see f.n. (29) in Appendix I.*

*(67) See f.n. (33) and (40) in Appendix I.*

to effect an adjustment. The first stage of the adjustment process began in early 1977 with a depreciation of the exchange value of the Hong Kong dollar. However, the consequent effects on costs and prices did not begin to be fully felt until late in 1978.

64. This depreciation led to our exports becoming more competitive. Coinciding with a recovery of demand in our major markets in Europe, the depreciation made possible an acceleration in the growth rate of our domestic exports. This became particularly marked from the middle of 1978 onwards<sup>(68)</sup>.

65 Towards the end of the year, therefore, the shift in the distribution of resources away from the manufacturing sector appeared to have halted. Because the demand for Hong Kong's imports is price inelastic, the effect of depreciation on domestic prices took time to work through the system and dampen down demand. In addition, low interest rates, and hence a rapid expansion of bank loans and advances<sup>(69)</sup>, also helped to keep up the growth rate of domestic demand thus sucking in imports of consumer goods at a very rapid rate, although the growth rate of imports of raw materials and semi-manufactures also accelerated as demand for our domestic exports picked up<sup>(70)</sup>.

66 So, in the second half of 1978, the adjustment mechanism, working through the depreciation of the exchange rate, did begin to encourage a redistribution of resources in favour of the manufacturing sector and stimulated a higher growth rate of exports, but the growth rate of domestic demand

(68) *Quantum index of domestic exports (1973=100):*

	1977	1978	Increase (%)
Q1	114	118	3.5
Q2	134	147	9.7
Q3	148	166	12.2
Q4	148	171	15.5

(69) *Bank loans and advances in Hong Kong (old definition):*

End	1977 (\$ mn)	1978 (\$ mn)	Increase (%)
Q1	31,041	39,833	28
Q2	33,096	42,640	28
Q3	33,759	46,476	38
Q4	36,856	52,814	43

(70) *Growth rates of imports by end use in real terms:*

	1977/1976 (%)	1978/1977 (%)
Foodstuffs	5	6
Consumer goods	15	31
Fuels	8	5
Raw materials and semi-manufactures	3	26
Capital goods	13	17
All imports	8	22

remained very rapid. The growth rate of imports accelerated to 22% and the excess demand for, over supply of, domestic resources created a serious threat of domestically generated inflation.

67 In other words, as the growth rates and rates of change of the operative economic aggregates and variables had become *so* inconsistent with each other, *some* form of interventionism to achieve economic stability had become essential, at least in the sense that particular care had to be taken to ensure that budgetary policy—using that term in its generic sense—was compatible with the adjustment process. Although, sooner or later, the economy would have *had* to adjust to changing internal and external circumstances, any further delay due to budgetary policy having a frustrating effect on this process would only result in an unnecessary distortion of the structure of the economy and in painful consequences for individuals.

*(b) Budgetary policy*

68 Thus, the necessary emphasis of budgetary policy in 1979-80 was self-evident: the growth rate of total final demand had to be slowed down to bring it more into line with the growth rate of the economy's output and this had to be done in such a way as to facilitate a relative shift in favour of the manufacturing sector.

69 So, *to begin with*, the growth rate of public sector demand had to be slowed down; and this is what I budgetted for on Consolidated Account: a slow down from 22% in 1978<sup>(71)</sup> to 7.5% in 1979, speaking of course in real terms<sup>(72)</sup>. Ideally, also, the relative size of the public sector had to be reduced from its record high level.

70 *Secondly*, the slow down of public sector demand had to be arranged so as to ease the pressure of demand on the output of the building and construction industry; and this is what I budgetted for: a slow down in the growth rate of public sector demand<sup>(73)</sup> for the output of this industry from 31% in 1978 to 7% in 1979<sup>(74)</sup>.

71 *Thirdly*, as public sector demand is only one component of domestic demand, total final demand could only be slowed down sufficiently to prevent inflationary pressures developing further, and in such a way as to facilitate a relative shift of resources in favour of the manufacturing sector, if the growth rate of private domestic demand was also constrained. So steps were proposed, and have been implemented, to limit the extent to which the Government's Hong Kong dollar balances can be used as a base for domestic credit

---

(71) *Preliminary estimate.*

(72) *Forecast estimate.*

(73) *Including the M.T.R. project for this purpose.*

(74) *Preliminary and forecast estimates respectively.*

creation<sup>(75)</sup>; the instalment payment system for premia on large commercial/ residential sites was withdrawn, thus removing one source of credit which was previously available to developers; efforts have been made to maximize the amount of Crown land put on the market; and there has been a continuing emphasis on the role of the interest rate weapon.

72 Given that, under a floating rate regime, the adjustment mechanism can work through the exchange rate and through interest rates<sup>(76)</sup>, as I have previously argued, interest rates were brought into play too slowly in the late summer of 1978. It is true that the Best Lending Rate was increased four times between 1 May 1978 and 9 November 1978 (from 4½% to 8½%), having remained at 4½% since 14 April 1977, but these increases were neither sharp enough nor timely enough either to constrain the growth rate of domestic demand<sup>(77)</sup> or to protect the exchange rate from speculative money outflows. Thus, we were seized with a sense of urgency and the Best Lending Rate was increased twice and, by 19 February 1979, it was as high as 10½%.

73 As we shall see in a moment, in 1979 the economy *did* adjust in response to market forces, suitably aided and supplemented, but there were three unexpected developments. *First*, although this was a development of dubious desirability, there was the unexpectedly rapid increase in the supply of labour as a result of immigration. This has meant that our manufacturers could meet the increased demand for exports by increasing output. So the growth rate of exports was greatly in excess of the budget speech forecast of 7% in real terms. *Secondly*, the cumulative effect of rising incomes and an inflow of foreign firms establishing themselves here, partly to do business with China, meant that the demand for residential accommodation for purchase and renting was greater than expected. Thus, although the market for labour was in better balance, there was a worsening imbalance in the market for property. *Thirdly*, the rate of world inflation was higher than expected. So imported inflation began to push up domestic prices. This has had a dampening effect on private consumption expenditure, which slowed down, therefore, more sharply than I forecast.

---

(75) *Since 1 May 1979, the Exchange Fund's short-term deposits with banks in Hong Kong have been subject to a 100% liquid assets requirement, against the previous 25% requirement. In support of this provision, by 31 December 1979, 84% of the Fund's Hong Kong dollar balances were held on short-term deposits with banks, compared with 23% a year earlier. In addition, our Hong Kong dollar balances have actually fallen in recent months as opportunities have been taken to switch into foreign currencies.*

(76) *The former influences the competitiveness of exports and the cost of imports and the latter influences the growth rate of total final demand through the price of credit, although capital flows may offset this latter effect to some extent by influencing the growth rate of the money supply.*

(77) *Bank loans and advances in Hong Kong (old definition):*

<i>End</i>	<i>\$ mn</i>	<i>% increase</i>
<i>December 1977</i>	<i>36,856</i>	<i>—</i>
<i>June 1978</i>	<i>42,640</i>	<i>16</i>
<i>December 1978</i>	<i>52,814</i>	<i>24</i>



*(c) Preliminary estimate of G.D.P. in 1979*

74 I shall now review how the economy actually fared in 1979 against that background, using the preliminary estimate of expenditure on the gross domestic product<sup>(78)</sup>.

75 In last year's budget speech<sup>(79)</sup>, I forecast that the growth rate of *private consumption expenditure* would still be high, at 9% (in real terms, of course). Despite a surge in the size of our population<sup>(80)</sup>, the growth rate of private consumption expenditure was only 7.7% in 1979. This represents a fairly sharp deceleration when compared with the growth rates in 1977 and 1978 of 17.3% and 18.4% respectively.

76 Last year, I estimated that, consistent with our efforts to slow down the growth rate of public expenditure, the growth rate of *Government consumption expenditure* would slow down to 9%<sup>(81)</sup>. However, at 12.3%, the preliminary estimate of the growth rate in 1979 is higher than forecast and is about the same as in 1977 and 1978 at 12.5% and 12.8% respectively.

77. Last year, I forecast that the growth rate of expenditure on *gross domestic fixed capital formation* would be 9%<sup>(82)</sup>. The preliminary estimate for 1979 is as high as 23.7%. The difference is largely the result of higher than expected investment in plant and machinery: 46.3% instead of 8%. Much of this investment was in transport equipment (including aircraft), but manufacturers also expanded their capacity because they were able to acquire the labour they needed.

---

(78) *Various estimates of G.D.P. are published from the forecast released in the budget speech to the final estimate published in the Half-Yearly Economic Report for the following year. Thus, so far as the year 1980 is concerned:*

<i>Forecast</i>	<i>Budget Speech 1980</i>
<i>Revised forecast</i>	<i>Speech of the Financial Secretary at a public function around September 1980</i>
<i>Preliminary estimate</i>	<i>Budget Speech and Economic Background 1981</i>
<i>Revised preliminary estimate</i>	<i>Half-Yearly Economic Report 1981</i>
<i>Provisional estimate</i>	<i>Budget Speech and Economic Background 1982</i>
<i>Final estimate</i>	<i>Half-Yearly Economic Report 1982.</i>

*The latest estimates of expenditure on the G.D.P. (new series) are as follows:*

	<i>At current prices</i>		<i>At constant (1973) prices</i>	
	<i>(\$ mn)</i>	<i>(% increase)</i>	<i>(\$ mn)</i>	<i>(% increase)</i>
<i>1977(final)</i>	<i>59,429</i>	<i>14.3</i>	<i>46,131</i>	<i>9.8</i>
<i>1978(provisional)</i>	<i>69,174</i>	<i>16.4</i>	<i>50,753</i>	<i>10.0</i>
<i>1979(preliminary)</i>	<i>87,345</i>	<i>26.3</i>	<i>56,577</i>	<i>11.5</i>

(79) *B.S., 1979, paras. 114-115.*

(80) *Including Vietnamese refugees, the population at the end of June 1979 was 6.4% higher than at the end of June 1978.*

(81) *B.S., 1979, paragraph 113.*

(82) *B.S., 1979, paras. 48-49.*

78 As regards investment in building and construction, I forecast a growth rate of 10%. The preliminary estimate for 1979 is for a growth rate of only 4%, made up of a growth rate of 9.1% for private sector expenditure on building and construction, which is less than the forecast of 12%, and a decrease of 1.2% for public sector expenditure (including the M.T.R.C.), which is also less than the forecast of 8%.

79 The preliminary estimate of the growth rate of *total exports of goods*<sup>(83)</sup> for 1979 is 19.5%, made up of 16.6% for domestic exports and 28.8% for re-exports. For the reasons I described earlier<sup>(84)</sup>, these growth rates are significantly higher than my forecast growth rates of 8% for domestic exports, 7% for total exports and 12% for re-exports respectively. The upsurge in the re-export trade to 28.8%, the upsurge in the re-export trade, which began to get underway in late 1977, was sustained for the second year running. This provides confirmation that our role as an *entrepot* is now a significant factor in our developing and diversifying economy.

80 The preliminary estimate of the growth rate of imports for 1979 at 15.6% is also higher than my forecast of 10%<sup>(85)</sup>, but this is a reflection of the better than expected export performance: the growth rate of imports of consumer goods slowed down as forecast, but the growth rate of imports of raw materials and semi-manufactures slowed down less than I expected, whilst the growth rate of imports of capital goods actually accelerated<sup>(86)</sup>.

81 Last year, to complete the forecast, I put in a token figure for *exports less imports of services* which suggested that the surplus on the invisible trade account would be unchanged when compared with 1978 and would be insufficient to offset the deficit on the visible trade account. In the event, the new estimates now available on imports and exports of services suggest that, in 1979, the surplus on invisible trade was substantially larger than in 1978 and was almost large enough to offset the deficit on the visible trade account. There was also a depletion of *stocks* in 1979 instead of the limited amount of stock accumulation which I have forecast.

(83) *B.S.*, 1979, paras. 119-120.

(84) See paragraph 73 above.

(85) *B.S.*, 1979, paragraph 121.

(86) *Growth rates of imports in real terms:*

	<i>Foodstuffs</i>	<i>Consumer goods</i>	<i>Fuels</i>	<i>Raw material and semi-manufactures</i>	<i>Capital goods</i>
	(%)	(%)	(%)	(%)	(%)
1978/1977: Q3	7	35	2	36	24
Q4	11	39	8	32	27
1979/1978: Q1	3	24	—1	23	26
Q2	6	14	21	17	43
Q3	10	6	25	15	56
Q4	5	4	—14	13	20
1979/1978:	6	11	9	17	36

82 So, taking the various components of *expenditure on the G.D.P.* together, instead of my forecast of 7%, the preliminary estimate for 1979 is for a growth rate of G.D.P. in 1979 of 11.5%. This unexpectedly high growth rate was the result of a higher than expected growth rate of demand for our exports which we were able to meet as a result of a rapid expansion in the productive capacity of the economy. This, in turn, was the result of the unexpectedly high growth rate of the population, rather than additional productivity. This is reflected in the fact that the preliminary estimate of the growth rate of G.D.P. in *per capita* terms at 4.8% is in line with the forecast. As shifts in the terms of trade were insignificant in 1979, the growth rate of real income at 11.1% was roughly the same as that of G.D.P. At constant (1973) prices, the preliminary estimate of G.D.P. in 1979 is \$56,577 million.

83 At current prices, the preliminary estimate of G.D.P. for 1979 is \$87,345 million, or 26.4% higher than that in 1978. This exceeds my forecast of G.D.P. at current prices at 16% because, in addition to the higher than expected growth rate of G.D.P. in real terms, the rate of increase in prices was also higher than expected. The G.D.P. deflator increased by 13.3% compared with my forecast of 8% and consumer prices increased by 11.7% compared with my forecast of 9%.

84. So, for the fourth successive year, the growth rate of the economy was significantly higher than the trend growth rate of 9%. This is a remarkable record indeed, notwithstanding that the growth rate of G.D.P. *per capita* has been slowed down during the four post-recession years from 17.5% in 1976, to 8.1% in 1977, to 7.8% in 1978, to 4.8% in 1979, due to the effects of immigration on the growth rate of population in 1978 and particularly, of course, in 1979<sup>(87)</sup>.

(d) *Assessment of adjustment process*

85 Economic growth, Sir, in 1979 was not associated with economic instability to the same extent as in 1978. *First*, the growth rate of total final demand, at 13.4%, was more consistent with the growth rate of G.D.P., at 11.5%, than in 1978 when the growth rate of total final demand was 15.1% and the growth rate of G.D.P. was only 10%.

86 *Secondly*, within total final demand, the growth rate of domestic demand slowed down to 8.6%, while the growth rate of domestic exports of goods accelerated to 16.6%. This contrasts with the situation in 1977 and 1978, when the growth rates of domestic demand, at 14.4% and 16.3%

---

(87) *Growth rate of population (mid-year on mid-year):*

	%
1976	1.1
1977	1.6
1978	2.0
1979	6.4(=4,900,000 with an error range of + 144,000 to —58,000)

respectively, exceeded the growth rates of domestic exports, at 4.8% and 10.4% respectively. So economic growth in 1979 was again once more export-led.

87 But, *thirdly*, within domestic demand, the growth rate of public sector demand, at 9.6%, still exceeded that of private domestic demand, at 8.4%. However, compared with the situation in 1978 when the former, that is the growth rate of the public sector demand, was 20.6% and the latter, that is to say private sector demand, was 15.7%, the situation improved and this was consistent with one of the objectives of budgetary policy.

88 *Fourthly*, in so far as expenditure on building and construction is concerned, public sector expenditure actually decreased (in real terms, of course), by 1.2%, while private sector expenditure increased by 9.1%. Public sector expenditure here included the M.T.R.C. As a result, the proportion of the output of the building and construction industry taken up by the public sector fell from 49% in 1978 to 47% in 1979; and this is what I budgetted for.

89 *Fifthly*, the growth rate of private consumption expenditure slowed down from 18.4% in 1978 to only 7.7% in 1979, rather surprisingly, given the growth rates of real income in 1978 and 1979 of 9.2% and 11.1% respectively.

90 *Sixthly*, the growth rate of total exports, at 19.5% in real terms, exceeded the growth rate of imports, at 15.6%, a distinct improvement on the situation in 1978, when the growth rate of total exports, at 13.8%, was well below that of imports, at 21.5%.

91 So, *seventhly*, the visible trade 'gap' narrowed to 12.1% in 1979 from 14.8% in 1978 which, with the increase in the surplus on invisible trade account, contributed to a stabilizing of the exchange value of the Hong Kong dollar<sup>(88)</sup>.

92 *Finally*, there were signs that the imbalance between the demand for, and supply of, domestic resources was beginning to ease off. In the second half of 1979, the proportion of the labour force unemployed increased and the rate of increase in wage rates slowed down<sup>(89)</sup>. Resources were also

---

(88) See *f.n.* (38) in Appendix I.

(89) *Index of nominal average daily wage rates in manufacturing, including fringe benefits (July 1973 to June 1974=100):*

	<i>Index</i>	<i>Year on year increase (%)</i>
1978:		
<i>March</i>	148	13.8
<i>September</i>	159	16.1
1979:		
<i>March</i>	178	20.3
<i>September</i>	185	16.4

shifting back into the manufacturing sector, as manufacturing employment grew more rapidly than the employed labour force<sup>(90)</sup>.

93 But, despite the fact that the exchange rate effect on prices was less serious in 1979 than in 1978, the rate of increase in consumer prices accelerated from 8% in 1978 to 11.6% in 1979, instead of the 9% I forecast. The rate of increase in the G.D.P. deflator accelerated from 5.8% in 1978 to 13.3% in 1979, instead of the 8% forecast. (And, remember, the G.D.P. deflator is a measure of the general price level.) As regards the monetary aggregates<sup>(91)</sup>: although the growth rates of the money supply and of credit accelerated in 1979 and, therefore, domestically generated inflation was being accommodated, rather than contained, the difference between the growth rates of M2 and G.D.P. in money terms at 29.6% and 26.3% respectively was less than the difference in 1978 when the growth rates were 25.6% and 16.4% respectively.

94 So, Sir, with the important exceptions of inflation and the persistent imbalance between the demand for, and the supply of, both property and land, but to a lesser extent than heretofore in the case of labour, the anxieties with which we were seized as we entered 1979 are beginning to recede as we enter 1980. Inflation, of course, has an unsettling effect on people and an uneven impact, but we must recognize that the inflation we had to suffer in 1979 was, to a significant extent, imported. World inflation was unfortunately accelerating in 1979, partly as a result of the oil situation. We must also recognize that there is little we can do, which would be consistent with the need to maintain external competitiveness, to isolate ourselves from world inflation.

(90)	<i>Year on year increase (%):</i>	
	<i>Manufacturing employment</i>	<i>Employed labour force</i>
1978:		
<i>March</i>	1.3	5.4
<i>September</i>	4.3	7.1
1979:		
<i>March</i>	6.0	5.6
<i>September</i>	11.2	5.8
(91) <i>Growth rates of monetary aggregates (%):</i>		
	<i>1978/1977</i>	<i>1979/1978</i>
<i>M1:</i>		
<i>Old series</i>	23.2	24.6
<i>New series</i>	N.A.	3.7
<i>M2:</i>		
<i>Old series</i>	25.6	29.6
<i>New series</i>	N.A.	13.2
<i>M3:</i>		
<i>Bank loans and advances in Hong Kong:</i>		
<i>Old series</i>	43.3	39.5
<i>New series</i>	N.A.	34.0
<i>Total credit available to the economy</i>	N.A.	34.4

95 This is not so in the case of domestically generated inflation. But here, again, we must recognize that, in a market oriented economy like Hong Kong, prices increase because demand exceeds supply. Under normal circumstances, domestically generated inflation arising from an imbalance between the demand for, and the supply of, resources will tend to correct itself. I say, under normal circumstances, because complete dependence on market forces may involve a social cost which may be too large for the community to bear. When there is a possibility that this is so, deliberate steps may have to be taken to dampen down domestically generated inflation, either by slowing down demand or by increasing supply. But above all, the growth rate of total final demand must not be allowed to get out of line again with the growth rate of G.D.P. Among other things, this means that the public finances must continue to be managed prudently. That is to say, the growth rate of public sector demand must not be such as to frustrate the adjustment process by helping to generate a non-sustainable growth rate of imports and by preventing the cost/price structure from deflating by prematurely taking up any slack in the economy. So, as and when the growth rate of world trade slows down, our cost/price structure will have to deflate if we are to improve our relative competitiveness and avoid the re-emergence of economic instability.

(2) *Acceptable Expenditure Limits for 1980-81*

96 For the purpose of forecasting total expenditure on General Revenue Account for 1980-81 (and for the three years of the new forecast period, 1981-82 to 1983-84) departments were required to submit returns, at mid-1979 prices, which distinguished between, on the one hand, commitments in respect of maintaining present services and expanding them to meet demand at existing standards and, on the other hand, new services. All the figures were corrected by Finance Branch for errors and omissions and separately compiled forecasts for the two Public Works Programme components of the capital account were then added in.

97 I shall refrain from offering a detailed analysis of the results of this exercise. Suffice it to say that the exercise threw up total bids for 1980-81 on recurrent account of \$10,114 million and on capital account of \$7,302 million<sup>(92)</sup>, representing increases of 11% and 42% respectively on the revised estimates for 1979-80<sup>(93)</sup>.

(92) *For the three years of the new forecast period (at mid-1979 prices) the bids came to:*

	<i>Recurrent</i>	<i>Capital</i>	<i>Total</i>
	(\$ mn)	(\$ mn)	(\$ mn)
1981-82	11,324	7,209	18,533
1982-83	12,344	7,403	19,747
1983-84	13,256	7,719	20,975

(93) *Adjusted in accordance with the principles adopted for the preparation of the table at Annex (2).*

98 These figures were used as the basis for guidance to departments in preparing their estimates submissions, which amounted to \$10,397 million on recurrent account and \$7,410 million on capital account. After various adjustments made by Finance Branch, the final figures to emerge were \$10,702 million on recurrent account and \$7,327 million on capital account<sup>(94)</sup>.

99 I then had to consider whether these figures, together with estimate of other public sector expenditure included in the Consolidated Account<sup>(95)</sup> amounting to \$2,903 million were acceptable as cash inputs for the forecast of expenditure on the gross domestic product in 1980.

100 I eventually took the view that they were, for four reasons: *first* the satisfactory way the economy had been adjusting in the latter part on 1979, particularly on external trade account<sup>(96)</sup>; *secondly*, the build-up on our commitments on capital account which, incidentally, has forced me to abandon, temporarily, the absolute guideline figures for the various components of the capital account; *thirdly*, the fact that I believed the public sector would be in substantial surplus in 1980-81; and *finally*, the econometricians, after testing these and other hypothetical inputs, advised me that their implications for the economy were just about tolerable.

(94) *Recurrent account:*

	<i>\$mn</i>
<i>Departmental submissions</i>	10,397
<i>Less: Finance Branch reductions</i>	<u>545</u>
	9,852
<i>Add: Report No. 2 of the Standing Commission on Civil Service Salaries</i>	350
<i>New services</i>	150
<i>Additional commitments vote</i>	<u>350</u>
	<u>10,702</u>
 <i>Capital account:</i>	
<i>Departmental submissions</i>	7,410
<i>Less: Finance Branch reductions</i>	<u>534</u>
	6,876
<i>Add: Additional commitments vote</i>	<u>450</u>
	<u>7,326(*)</u>

Note: (\*) *This figure excludes \$414 million in respect of debt repayments (\$304 million transfers to the Home Ownership Fund for land premia (\$80 million), transfers to the Mass Transit Fund for equity (\$5 million) and expenditure on to Jubilee Sports Centre (\$25 million).*

(95) *By the Urban Council and the Housing Authority financed from their own resources; an expenditure charged to existing balances in, and income accruing to, the Development Loan Fund, the Lotteries Fund, the Home Ownership Fund and the Student Loan Fund.*

(96) *Movements in the relative size of the public sector in national accounts terms were similar see f.n. (22) in Appendix I.*

101 I must confess, however, to being rather worried on one score: when an upswing phase is as prolonged as four years and is likely to be further prolonged, it has to be accepted that the growth rate of public expenditure will tend to catch up with, and even exceed, the growth rate of the economy and, therefore, that the relative size of the public sector will tend to increase again after falling back in the early years of the recovery. Thus, after increasing to an average of 16.6% in the two recession years, 1974-75 and 1975-76, the relative size of the public sector fell back to an average of 14.7% in the following two years, but then increased to 17.4% in 1978-79 and to 18.7% in 1979-80<sup>(97)</sup>. The emphasis of budgetary policy in 1980-81 *should* really be to hold the public sector's share of resources at this level, but the pressures of our commitments on capital account forced me to accept Draft Estimates of Expenditure which will involve a further increase in the relative size of the public sector.

(3) *Forecast of Expenditure on the G.D.P. in 1980*<sup>(98)</sup>

(a) *Introduction*

102 Before presenting my forecast of expenditure on the G.D.P. in 1980 (in real terms, of course, at any rate to begin with), I must sound this warning: the world at present is so plagued with uncertainties that forecasting is a game which is more than usually hazardous for the players. So I am none too confident of the forecast, but there is some comfort in the thought that, inflationary pressures notwithstanding, our economy is in good shape, the labour force is fully employed, real incomes *per capita* have increased by 95% over the past decade and our 'free' fiscal reserves at 1 April will represent about 31% of estimated expenditure on General Revenue Account in 1980-81.

(b) *Gross domestic product by component*

(i) *Private consumption expenditure*

103 To begin with private consumption expenditure: my forecast is for a growth rate of 9% which is less than might be implied by the growth rate of real income in 1979<sup>(99)</sup> and the forecast growth rate for 1980. There are three possible reasons for this: *first*, a relatively high rate of increase in prices may, when allied with the uncertainties facing our economy, exert a constraining effect on consumption and provide a greater incentive to save, as it did in 1979, when the achieved growth rate<sup>(100)</sup> of private consumption expenditure, at 7.7%, was lower than might have been expected,

---

(97) See f.n. (29) in Appendix I.

(98) See Annex (9).

(99) See f.n. (10) above and f.n. (24) in Appendix I.

(100) The phrase 'achieved growth rate', when used throughout this section, means the growth rate implied in the preliminary estimates of expenditure on the G.D.P. in 1979.



given the growth rates of real income in 1978 and 1979 of 9.2% and 11.5% respectively. *Secondly*, there has been an increasing tendency for families to purchase their own flats; and, with a high rate of increase in the prices of flats and higher mortgage rates, a larger proportion of the incomes of some families will be tied up in monthly mortgage payments and so less will be available for other household expenditure. *Thirdly*, the spurt in the growth rate of private consumption expenditure from 2% in 1975 to 8.8% in 1976 to 18.4% in 1978 will continue to depress replacement demand as was probably the case in 1979.

(ii) *Government consumption expenditure*

104 The forecast of the growth rate of Government consumption expenditure is 12%, roughly the same as the growth rate achieved in 1979. This has been calculated, as usual, by converting the revised estimate of recurrent expenditure in 1979-80 by the public sector on Consolidated Account (less trading activities) and the corresponding cash input figure for 1980-81 into national accounts terms and then putting them on a calendar year basis. These figures were then appropriately deflated to arrive at a forecast for the growth rate of Government consumption expenditure in real terms, as I say, 12%.

(iii) *Gross domestic fixed capital formation*

105 My forecast for the growth rate of investment in *plant and machinery* in 1980 is 15%. This represents a slow down from the growth rate of over 40% achieved in 1979 which was the result, as I mentioned earlier, of a rapid growth rate of investment in transport equipment and office machinery<sup>(101)</sup>. Notwithstanding the fact that most of the transport equipment for the Modified Initial System of the M.T.R. has already arrived, I expect a rapid growth rate of investment in transport equipment in 1979-80, particularly because of the purchase of aircraft. However, I expect investment in industrial machinery to slow down in view of the many uncertainties surrounding world trade.

106. As for investment in *building and construction*: new building intentions of the private sector, as indicated by the floor area of buildings for which consents were given during 1979<sup>(102)</sup>, were rather below those for 1978. But this could have been the result of a realization that the building and construction industry was already operating against its capacity limits as

---

(101) *The growth rate of investment in industrial machinery was also rapid. This was reflected in the growth rate of imports of this category of capital goods of about 35% in real terms in 1979.*

(102) *Floor area of new building plans by the private sector with consents to commence work:*

	<i>Usable floor area (thousand square feet)</i>
1978	35,338
1979	33,174

reflected by a rapid increase in costs<sup>(103)</sup> and a shortfall of completions during 1979 compared with expectations at the beginning of the year<sup>(104)</sup>. The implication of the realization for 1980 is that the growth rate of expenditure by the private sector on building and construction will be determined by the rate of expansion of the industry's capacity and the permitted growth rate of expenditure by the public sector on building and construction. On this basis, I expect the growth rate of expenditure by the private sector on building and construction will be around 5%, compared with the achieved growth rate of 8% in 1979.

107 I expect the growth rate of expenditure by the public sector (including the M.T.R.C. for this purpose of course) on building and construction will be 15%, compared with virtually no growth in 1979.

108 So my forecast of the growth rate of total expenditure on building and construction is 10%. Combining this with my forecast of the growth rate of investment in plant and machinery of 15%, my forecast for the growth rate of gross domestic fixed capital formation is 12%, compared with the achieved growth rate of 23.7% in 1979.

(iv) *Exports*

109 Turning now to exports: economic prospects in the United States continue to be uncertain and the latest forecasts available to us suggest that the growth rate of real incomes in this market is likely to be negative

(103) *Labour and materials cost index (January 1969=100):*

	<i>Index</i>	<i>Year on year increase (%)</i>
<i>1978:</i>		
<i>March</i>	334	10.2
<i>June</i>	343	11.0
<i>September</i>	373	17.3
<i>December</i>	395	19.7
<i>1979:</i>		
<i>March</i>	440	31.7
<i>June</i>	482	40.5
<i>September</i>	522	39.9
<i>December (est.)</i>	545	38.0

*It should also be noted that, by the fourth quarter of 1978, the Tender Price Index compiled by the Public Works Department for public works contracts had increased by 18% over the fourth quarter of 1977; and, by the fourth quarter of 1979, it had increased by 38% over the fourth quarter of 1978.*

(104) *Completions of private accommodation in 1979(\*):*

<i>Type of accommodation</i>	<i>Forecast</i>	<i>Completions</i>	<i>Excess (+)/ Shortfall(-) (%)</i>
<i>Residential (units)</i>	30,335	27,742	—8.5
<i>Shops ('000 sq. ft.)</i>	1,671	1,379	—17.5
<i>Offices ('000 sq. ft.)</i>	1,722	1,929	+12.0
<i>Miscellaneous commercial ('000 sq. ft.)</i>	1,107	1,073	—3.1
<i>Flatted factories ('000 sq. ft.)</i>	15,825	13,753	—13.1
<i>Specialized factories ('000 sq. ft.) (**)</i>	1,892	1,046	—44.7
<i>Storage ('000 sq. ft.)</i>	2,759	2,531	—8.3

Notes: (\*) *Data from Rating and Valuation Department.*

(\*\*) *Affected by difficulties in forecasting completions at Tai Po Industrial Estate.*

in 1980<sup>(105)</sup>. However, in the second half of 1979, the growth rate of Hong Kong's domestic exports to this market picked up significantly; and, at the end of the year, order books still remained reasonably full. But one of the factors behind this recovery was that inventories were being replenished, having been run down in response to high interest rates and in anticipation of the much talked of imminent recession. Inventories are reported to be still below normal and there may be a tendency to re-build them in anticipation of further inflation, but it is difficult to be certain about this. Accordingly, I expect that the growth rate of Hong Kong's domestic exports to the United States will continue to be fairly rapid in the first half of 1980, but will slow down in the second half. Thus, my forecast for the growth rate of domestic exports to the United States for the year as a whole is 4%, compared with the achieved growth rate of 8% in 1979.

110 The reported prospects of the economies of our major markets in Europe in 1980 also suggest a slowing down in the growth rates of real incomes and consumption expenditure<sup>(105)</sup>. Consequently, I do not envisage a continuation of the very rapid growth rates of domestic exports to Germany and the United Kingdom of 22% and 28% respectively achieved in 1979. In any case, exchange rate movements in recent months will not improve our competitiveness in 1980 as they did in the second half of 1978, and in the first half of 1979, when orders for 1979 shipments were placed. However, as the manufacturing sector has been acquiring an increasing share of the employed labour force since the middle of 1978, and as the pressure of demand in the labour market started to ease in the second half of 1979, manufacturers should be able to meet increases in demand, to the extent that bilateral restraint agreements allow this to occur. Thus, my forecast for the growth rate of domestic exports to Germany is 10% and to the United Kingdom is 6%.

111 My forecast for the growth rate of domestic exports to the rest of the world is 9%, compared with the achieved growth rate of 20% in 1979.

112 To sum up, my forecast for the growth rate of domestic exports in 1980 is 7%, representing a slow down compared with the achieved growth rate of 16.6% in 1979.

113 To forecast the growth rate of re-exports is difficult, for it has been so erratic over the last decade<sup>(106)</sup>. But taking into account the expansion in

---

(105) See paragraph 133 and f.n. (135) in Appendix III.

(106) Growth rate of re-exports in real terms:

	%
1970	6
1971	16
1972	15
1973	32
1974	-8
1975	1
1976	27
1977	2
1978	21
1979	29

China's international trade and Hong Kong's role as an *entrepot* facilitating this expansion, I think the growth rate of re-exports will continue to be rapid at 14%, compared with the achieved growth rate of 29% in 1979. At 14% the forecast growth rate of re-exports is twice as rapid as the forecast growth rate of domestic exports<sup>(107)</sup>. Thus my forecast for the growth rate of total exports of goods in 1980 is 9%, compared with the achieved growth rate of 19.5% in 1979.

(v) *Imports*

114 The growth rate of imports that is consistent with the forecasts for the other G.D.P. components is 11%, which may be compared with the achieved growth rate of 15.6% in 1979.

(vi) *Net exports of services*

115 Although our *estimates* of the imports and exports of services have recently been put on to a firmer basis<sup>(108)</sup>, it is still difficult to *forecast* with any accuracy the net balance on invisible trade. Nevertheless, on the basis of the information to hand, I expect the growth rate of the net balance of invisible trade to be about 9%. This is lower than the achieved growth rate of 15% in 1979.

(vii) *Stocks*

116 Finally, I expect there will be a small replenishment of stocks in 1980 following the depletion which occurred in 1979.

(c) *Total expenditure on G.D.P.*

117 Combining these forecasts for the individual components of expenditure on the G.D.P., my forecast for the growth rate of G.D.P. in 1980 is 9%, compared with the achieved growth rate of 11.5% in 1979. At constant (1973) prices, total expenditure on the G.D.P. will be about \$61,800 million. In *per capita* terms, assuming the growth rate of the population to be about 4.1%<sup>(109)</sup>, the growth rate of G.D.P. *per capita* will be 5%, roughly the same as the achieved growth rate of 4.8% in 1979; and, as the forecast increases in import and export prices are such as to imply that the terms of trade will remain unchanged, the growth rate of real income *per capita* will also be about 5%.

---

(107) *Incidentally, the growth rate of re-exports in both 1977 and 1978 was also roughly twice that of domestic exports.*

(108) *The first survey of imports and exports of services was held last year to collect information in respect of 1978. Another survey will be conducted this year to collect information in respect of 1979; and so the preliminary estimate for 1979 of this component is bound to be substantially revised when the results of the 1979 survey become available towards the end of 1980.*

(109) *Mid-1980 on mid-1979 and made up of: 2.9% for net immigration and 1.2% for natural increase.*

*(d) Prices and G.D.P. at current prices*

118 Turning now to prices: the latest forecasts of world prices in 1980 are that the rapid rates of increase experienced in 1979<sup>(110)</sup> will continue. My forecast for the rate of increase in consumer prices in Hong Kong in 1980 is 10%, representing a slow down from the actual rate of increase of 11.6% in 1979.

119 *But*, the pressure of demand on the output of the building and construction industry will still be such in 1980 that building and construction costs will continue to increase rapidly<sup>(111)</sup> albeit, probably, at a rate below the rate of increase in 1979 over 1978 of almost 40%<sup>(112)</sup>. Together with my assumptions for the rates of increase in the prices of imports and exports at 10%, my forecast for the rate of increase in the general price level—in other words, in the G.D.P. deflator—is 11%. This, again, represents a slowing down from the actual rate of increase of 13.3% in 1979.

120 So my forecast of the growth rate of G.D.P. in money terms in 1980 is 21%. This implies that total expenditure on G.D.P. at current prices will be \$106,000 million. In *per capita* terms, G.D.P. at current prices will be almost \$21,000 representing a growth rate of 17%, compared with the achieved growth rate of 18.7% in 1979.

*(e) Implications of the forecast for the economy*

121 Before I turn, Sir, to the implications of this forecast, I must emphasize again that, as the world economy is passing through a particularly uncertain period, any view as to how the economy will fare must be subject to an unusually wide margin of error, and I would particularly stress that there is really no knowing what the state of the world oil market will be.

122 Be that as it may, the present forecast suggests that the movement towards internal and external equilibrium<sup>(113)</sup>, which began to become apparent in the second half of 1979, will not be reversed. *First*, the growth rate of total final demand, at 10% will only be marginally higher than that of G.D.P. at 9%. The growth rate of imports will also be rather higher, at 11%, but not significantly so<sup>(114)</sup>.

(110) For example, the rate of increase in consumer prices in O.E.C.D. countries was 11% in 1979 and is forecast to be only slightly less in 1980: see f.n. (137) in Appendix III.

(111) In the forecast exercise, the assumed rate of increase in building and construction costs is 25%.

(112) See f.n. (103) above.

(113) See f.n. (7) above.

(114)	Growth rate of:	1979	1980
		Preliminary	Forecast
		estimate	
		(%)	(%)
	Total final demand	13.4	10
	G.D.P.	11.5	9
	Imports of goods	15.6	11

123 *Secondly*, within total final demand, the growth rate of domestic demand, at 11%, will be higher than the growth rate of domestic exports of goods at 7%, and even higher than the growth rate of total exports at 9%<sup>(115)</sup>, implying some shift in the distribution of labour away from the manufacturing sector, but this must be viewed, I suggest, in the context of a sharp shift in favour of the manufacturing sector in 1979<sup>(116)</sup>.

124 *Thirdly*, within domestic demand, the growth rate of public sector demand at 13% will be higher than the growth rate of private sector demand at 11%<sup>(117)</sup>. So the public sector will still be commanding an increasing share of available resources in the economy. Nevertheless, the divergence between the two rates is not very large and, as resources shifted strongly back into the manufacturing sector in 1979, this is perhaps just acceptable.

125 But, *fourthly*, the pressure of demand for the output of the building and construction industry will still be considerable. With the industry already operating up to the limit of its present capacity, a forecast growth rate of expenditure on building and construction of 10% merely reflects—indeed, it merely *assumes*—an expansion of capacity, which will have to be achieved against a background of continuing rapid increases in building and construction costs<sup>(118)</sup>. In 1980, the public sector's share of the output of the building and construction industry will once again increase, probably to 49%, after easing *back* from 49% in 1978 to 47% in 1979<sup>(119)</sup>; but I think this can be

(115)		1979	1980
	<i>Growth rate of:</i>	<i>Preliminary estimate</i>	<i>Forecast</i>
		(%)	(%)
	<i>Domestic demand</i>	8.6	11
	<i>Domestic exports</i>	16.6	7
	<i>Total exports</i>	19.5	9

(116)	<i>Share of employed labour force engaged in the manufacturing sector:</i>	%
	<i>At September:</i>	
	1975	34.8 ( <i>recession year</i> )
	1976	42.6 ( <i>upswing began</i> )
	1977	40.5
	1978	39.5
	1979	41.5

(117)		1979	1980
	<i>Growth rate of:</i>	<i>Preliminary estimate</i>	<i>Forecast</i>
		(%)	(%)
	<i>Private domestic demand</i>	8.4	11
	<i>Public domestic demand</i>	9.6	13

(118) *See f.n. (103) above.*

(119)		1979	1980
	<i>Growth rate of:</i>	<i>Preliminary estimate</i>	<i>Forecast</i>
		(%)	(%)
	<i>Private expenditure on building and construction</i>	9.1	5
	<i>Public expenditure on building and construction</i>	- 1.2	15
	<i>Share of public sector</i>	47.0	49

accepted without running a serious risk of crowding out the private sector and/or diverting labour excessively away from manufacturing employment.

126 *Fifthly*, as I explained earlier, the growth rate of private consumption expenditure, at 9%, will be less than might be expected, given the achieved growth rate of real income in 1979 of 11.1%, and the forecast growth rate in 1980 of 9%<sup>(120)</sup>. This is useful in the context of the impact of the rapid growth rate of public sector demand.

127 *Sixthly*, the growth rate of imports of goods at 11% will be higher than that of total exports of goods at 9%<sup>(121)</sup>.

128 So, *seventhly*, the visible trade 'gap' will, in 1980, widen to about 14% from 12.1% in 1979<sup>(122)</sup>, but the visible trade deficit implied should be largely offset by the surplus on the invisible trade account. At 14%, the visible trade 'gap' is within the historical range of 10% to 16% in the 1970s<sup>(123)</sup>.

129 *Finally*, with the important exception of the building and construction industry, the demand for, and supply of, domestic resources in the economy will continue to move in the direction of a better balance as reflected by slower rates of increase of prices<sup>(124)</sup>. This will be, in part, the result of a further rapid increase in the supply of labour. This is a factor of dubious desirability for, no doubt, the rate of increase in wage rates will be slower than it might otherwise—indeed, *should* otherwise—be and there will be a lowering of the growth rate of productivity.

(120)	Growth rate of:	1979	1980
		Preliminary estimate (%)	Forecast (%)
	Private consumption expenditure	7.7	9
	Real income (Real income in previous year)	11.1 (9.2)	9 (11.1)

(121)	Growth rate of:	1979	1980
		Preliminary estimate (%)	Forecast (%)
	Imports of goods	15.6	11
	Total exports of goods	19.5	9

(122) *These figures include an adjustment to take account of imports of water and an estimate of imports of gold for industrial and commercial use. The unadjusted figures give a forecast of 13% in 1980, compared 11.5% in 1979.*

(123) *This range excludes the very small visible trade 'gaps' recorded in 1976 and 1977 when the effect of the post-recession upsurge in the growth rate of domestic exports in 1976 was still predominant: see f.n. (27) in Appendix I.*

(124)	Rate of increase in:	1979	1980
		Preliminary estimate (%)	Forecast (%)
	G.D.P. deflator	13.3	11
	Consumer prices	11.6	10

4.15 p.m.

HIS EXCELLENCY THE PRESIDENT:—Honourable Members, at this point both you and the Financial Secretary might like a very short break. Council will resume in ten minutes.

4.25 p.m.

HIS EXCELLENCY THE PRESIDENT:—Council will resume. The Financial Secretary.

THE FINANCIAL SECRETARY:—

#### *PART IV: THE BUDGET FOR 1980-81*

##### *(1) Introduction*

130 Honourable Members, Sir, would be delighted to hear that completes my review of the historical setting (*laughter*) and my prognostication of the immediate outlook in which the budget for the first year of the 1980s had to be prepared. I must now do what this motion is all about, bringing my attention to bear on the Appropriation Bill. That is to say I must now present the Draft Estimates of Expenditure, the Revenue Estimates and my revenue proposals for 1980-81 and thereafter. At the same time, I hope to be able to assure honourable Members that the Expenditure Estimates adequately provide for the Government's policies and programmes to be implemented at a very satisfactory rate, that our fiscal policies continue to have regard to our revenue needs and to our fiscal principles and that the budget is compatible with economic and monetary stability.

##### *(2) Draft Expenditure Estimates*

###### *(a) Total expenditure*

131 Actual expenditure in 1970-71 was only \$2,292 million. The revised estimate of expenditure in 1979-80 is \$14,232 million<sup>(125)</sup>.

132 The Draft Estimates for the first year of the new decade, 1980-81, provide for total expenditure of \$18,028 million<sup>(126)</sup>. This represents an

---

(125) See Annex (2).

(126) On an unadjusted basis, the provision sought (i.e. the provision shown in the Draft Estimates and, therefore, reflected in the Appropriation Bill) is \$18,442 million. All the adjustments are on capital account. Thus the unadjusted estimate of \$7,740 million may be reconciled with the adjusted estimate referred to in paragraph 142 below as follows: \$7,740 million—\$80 million being transfers to the Home Ownership Fund for land—\$5 million being transfers to the Mass Transit Fund for equity—\$25 million for the Jubilee Sports Centre (to be reimbursed from the Special Coin Suspense Account)—\$304 million for debt repayments=\$7,326 million.



increase of a startling \$3,796 million, or 27%, on the revised estimate for 1979-80. This increase, incidentally, is more than *total* expenditure in 1972-73.

133 As usual, I shall describe the Draft Estimates by components of expenditure assessing the breakdown, on both recurrent and capital account, by reference to our historical experience. The Government's intentions in the main programme areas for the coming year, and how they are provided for in the Draft Estimates, are spelled out in Annex (11) to the printed version of this speech.

(b) *Recurrent*<sup>(127)</sup>

134 The provision for expenditure on recurrent services is \$10,702 million, including \$350 million for additional commitments of an unavoidable nature arising during the year<sup>(128)</sup>. This represents an increase of \$1,621 million, or 18%, on the revised estimate for 1979-80 of \$9,081 million.

135 *Personal Emoluments* (including allowances, but not on-costs) at \$4,066 million account for 38% of recurrent expenditure compared with an historical ratio based on actual experience in the 1970s of 41%. Of this total provision, \$185 million is for posts applied for, but yet to be examined by Finance Branch and approved by Finance Committee, due allowance being made for likely recruitment in respect of such posts as are approved. The approved establishment of the civil service shown in the Draft Estimates is 141,136<sup>(129)</sup> which represents an increase of 7,714 posts, or 5.8%, on the approved establishment of 133,422 posts at 1 April 1979, and may be compared with the average annual growth rate over the ten years 1970-71 to 1979-80 of 5%.

136 The provision sought does not include an allowance for the cost of a revision of civil service salaries in 1980-81. Such a revision, if any, must await recommendations from the Standing Commission on Civil Service Salaries regarding the principles on which pay policy should, in future, be based.

(127)	Component	Draft Estimates		Average % over ten years (*)
		(\$ mn)	(%)	
(1)	<i>Personal Emoluments</i>	4,066	38.0	41
(2)	<i>Departmental Other Charges</i>	1,545	14.4	15
(3)	<i>Public Works Recurrent</i>	699	6.5	6.6
(4)	<i>Recurrent Subventions</i>	2,250	21.0	26
(5)	<i>U.P.G.C.</i>	457	4.3	
(6)	<i>Pensions</i>	367	3.4	3
(7)	<i>Defence</i>	440	4.1	4
(8)	<i>Public Debt</i>	37	0.4	0.4
(9)	<i>Miscellaneous</i>	841	7.9	4
	<i>Total Recurrent Expenditure</i>	<u>10,702</u>	<u>100.0</u>	<u>100</u>

Note: (\*) For details see Annex (12).

(128) Head 54 Miscellaneous Services Subhead 100 Additional commitments.

(129) Of which 130,000 are likely to be filled on 1 April 1980.

137 Provision for all other recurrent expenditure amounts to \$6,636 million, but I shall mention here four components only: *Departmental Other Charges*<sup>(130)</sup> at \$1,545 million account for 14.4% of recurrent expenditure, just below the historical ratio of 15%.

138 *Public Works Recurrent* expenditure<sup>(131)</sup> at \$699 million accounts for 6.5% of recurrent expenditure, the same as the historical ratio. As I have said before, I regard 7% as the minimum necessary to maintain our assets properly intact and to operate the services covered by this component.

139 *Recurrent Subventions* and *U.P.G.C.* at \$2,707 million will absorb 25.3% of recurrent expenditure, just below the historical ratio of 26%. This is partly due to the fact that no provision has been included in the Draft Estimates for grants to agencies subvented on a discretionary grant basis and the universities and the Polytechnic for salary revisions following upon Report No. 2 of the Standing Commission on Civil Service Salaries. At the time the Draft Estimates went to print, no applications for such grants had been received<sup>(132)</sup>. Overall, taking recurrent and capital subventions together, 17.4% of total expenditure on General Revenue Account will be disbursed by subvented organizations, less than the historical ratio of 20%, but the average ratio in the last two years has been 18.6% only because of the large increases in Government expenditure on capital account and not because the role of subvented organizations in the disbursement of public funds has declined (and, incidentally, contrary to the unsubstantiated belief of some commentators, the Finance Branch *is* concerned to see the value-for-money criterion observed by subvented organizations; and so is the Director of Audit).

140 The proportion of recurrent expenditure devoted to defence at \$440 million accounts for 4.1% of recurrent expenditure. This compares with an historical ratio, based on actual expenditure over the four years 1976-77 to 1979-80, of 4.6% when the present Defence Costs Agreement applied, and with 1.9% only over the first six years of the decade<sup>(133)</sup>.

---

(130) *That is, all recurrent expenditure other than personal emoluments, Public Works Recurrent, recurrent subventions, defence, pensions, interest and service charges on public debt and miscellaneous services.*

(131) *That is, all expenditure connected with the maintenance of Government assets and the operation of various services such as water supply, sewage works, quarries, street lighting, etc.*

(132) *But they have since been received and are now being processed. The cost in 1980-81 will have to be met from Head 54 Miscellaneous Services Subhead 100 Additional commitments.*

(133) *The Defence Costs Agreement as such provides for the Hong Kong Government's share of the total cost (recurrent and capital) of the agreed garrison of 4 1/3rd major units, as recalculated from time to time by reference to measures of inflation, to be 50% in 1976-77, 62½% in 1977-78 and 75% from 1978-79 onwards. The apportionment of the cost of reinforcements required from time to time is settled ad hoc outside the framework of the D.C.A. but, as the garrison is to be enlarged, the D.C.A. may have to be revised to provide a more flexible framework.*

(c) *Capital*<sup>(134)</sup>

141 A comparative analysis of the capital account by component is provided in f.n. (134) to the printed version of this speech and, even for the non-student of footnotes, bears close scrutiny (*laughter*). Sir, there are now twelve components of the capital account and the miscellaneous component includes, for the first time, \$450 million for additional commitments of an unavoidable nature arising during the year and recognizes the fact that the estimates for works are based on September 1979 prices<sup>(135)</sup>.

(134) Component	Draft Estimates	C.f. Revised
	1980-81 (\$ mn)	Estimates 1979-80 (\$ mn)
(1) <i>Public Works Programme (other than New Towns and Housing)</i>	1,817	1,890
(2) <i>Public Works Programme (New Towns and Housing)</i>	1,542	1,348
(3) <i>Land Acquisition</i>	441	(*)
(4) <i>Transfers to D.L.F. for on-lending to the Housing Authority</i>	1,831(**)	1,000
(5) <i>Transfers to Home Ownership Fund</i>	—	—
(6) <i>Subventions:</i>		
<i>Education</i>	91	81
<i>Medical</i>	56	23
<i>Miscellaneous</i>	4	2
(7) <i>University and Polytechnic Grants Committee</i>	287	136
(8) <i>Departmental Special Expenditure</i>	317	207
(9) <i>Defence Costs Agreement: Capital Works</i>	33	29
(10) <i>Defence: Miscellaneous Measures</i>	393(***)	172
(11) <i>Other Transfers:</i>		
<i>Emergency Relief Fund</i>	3	10
<i>Student Loan Fund</i>	36	181
(12) <i>Miscellaneous</i>	475(****)	72
<i>Total capital expenditure</i>	<u>7,326</u>	<u>5,151</u>

## Notes:

(\*) Until 1980-81 included in Components (1) and (2).

(\*\*) It is estimated that the Housing Authority will draw \$1,630 million from the Development Loan Fund for the construction of public housing for renting (interest free, repayable over 40 years), \$126 million for the construction of flatted factories and \$75 million for the construction of commercial facilities for estates built under the Home Ownership Scheme (both at 8% repayable over 20 years).

(\*\*\*) Includes \$180 million for reinforcement of the garrison (treated as non-recurrent expenditure), \$30 million for border defence works and \$183 million for the reprovisioning of Victoria Barracks and other capital works for the Armed Forces outside the terms of the D.C.A.

(\*\*\*\*) Includes \$450 million for expenditure unforeseen at the time the Draft Estimates were prepared, including cost increases (see Head 54 Miscellaneous Services Subhead 260 Additional commitments); \$12 million for expenses relating to Vietnamese refugees (treated as non-recurrent expenditure); and \$11 million for central computer facilities.

(135) Head 54 Miscellaneous Services Subhead 260 Additional commitments, the Controlling Officer for which is the Deputy Financial Secretary. On the basis of certain assumptions, it is expected that \$250 million may be required for extra costs on on-going and newly let contracts, leaving \$200 million for commitments unforeseen at the time the Draft Estimates were prepared (such as projects subsequently assigned a high priority, and there is a possibility that the Housing Authority may have to draw additional funds from the D.L.F. to ensure that the production target is met in 1981-82).

142 The provision for capital expenditure is \$7,326 million, an increase of \$2,175 million, or 42%, on the revised estimate for 1979-80. The estimate includes \$1,817 million for the Public Works Programme (other than New Towns and Housing), \$1,542 million for the Public Works Programme (New Towns and Housing), \$441 million for Land Acquisition and \$1,831 million for Transfers to the Development Loan Fund for on-lending to the Housing Authority. Taking these four components together for comparative purposes, the provision sought in 1980-81 is \$5,631 million compared with the revised estimate for this year of \$4,238 million, an increase of 33%. The provision for Subventions and the U.P.G.C. is \$438 million<sup>(136)</sup>, for the two defence components it is \$426 million and for the four other components it is \$831 million.

143 Now, Sir, in view of the Government's complete commitment to helping to solve the community's housing problem, and the misdirected claims that more could be done if only the Government was more imaginative and diligent, I should like to digress here to quantify in terms of both expenditure and production what it is we *are* doing: total capital expenditure on housing in 1979-80 is estimated to be \$1,746 million and, in 1980-81, it is estimated to rise to \$2,981 million; and these figures *exclude* the value of land used by the Housing Authority for the rented housing programme<sup>(137)</sup>.

(136) Reflecting the need to complete all approved building programmes for the universities and the Polytechnic before the new triennium beginning in 1982.

(137)	1979-80 Revised Estimates (\$ mn)	1980-81 Estimates (\$ mn)
(1) Rented Housing Programme(*):		
Drawings from Development Loan Fund(**)	932	1,630
Housing Authority's own resources(***)	171	66
Public Works Department	52	23
Asian Development Bank Loan(****)	29	27
Total (1)	1,184	1,746
(2) Home Ownership Scheme(*****)	514	1,194
Total (1)+(2)	1,698	2,940
(3) Temporary Housing Areas	48	41
Total (1)+(2)+(3)	1,746	2,981

Notes:

(\*) Not including the Housing Society.

(\*\*) For housing and ancillary facilities, but nothing for land, because land is granted to the Housing Authority at nil premium, although the full market value of the land is entered in the Authority's accounts as a Government contribution.

(\*\*\*) Difference between rent income and running expenses plus premia from commercial lettings.

(\*\*\*\*) See Memorandum Note on Head 63 Public Debt, paras. 4 and 8 on page 451 of the Estimates and the Memorandum Note on A.D.B. Loans on page 832 of the Estimates.

(\*\*\*\*\*) Not including the Home Ownership (Private Sector Participation) Scheme. But, for the Home Ownership Scheme itself, the expenditure figures include land and also \$53 million and \$75 million for 1979-80 and 1980-81 respectively being drawings by the Housing Authority from the D.L.F. for commercial facilities.

144 A four-year programme aimed at achieving a level of production of public housing for both rental and sale of about 35,000 flats a year was introduced last year<sup>(138)</sup>. This programme is rolled forward annually, and the 1980 version covering the next financial year and the three years of the new forecast period, 1981-82 to 1983-84, is set out in Annex (11) to the printed version of this speech. The annual target figure of 35,000 flats should be achieved for the first time in 1980-81 and be maintained at this level thereafter. The forecast of production in the four years, 1980-81 to 1983-84, at 142,116 flats exceeds production in the previous four years, 1976-77 to 1979-80, by 72,271 flats, or by 103%<sup>(139)</sup>. These production figures do not include 7,207 Housing Society flats and 2,274 Home Ownership (Private Sector Participation) Scheme flats expected to come on stream during the same four year period.

145 Land, of course, is another topical subject and it seems that more land is thought to be the solution to pretty well all our problems from housing to rents to inflation. None of these problems is quite as simple as that, but provision within the two Public Works Programme components of the capital account for land production (formation and servicing) is such that land production in 1980-81 is expected to be 853 acres, compared with 1,236 acres in 1979-80 and 238 acres in 1976-77<sup>(140)</sup>.

146 Over the three years of the new forecast period, 1981-82 to 1983-84, land production will be maintained at these high levels. It is difficult to be absolutely definitive about the actual gross areas likely to come on stream, but they should be in the order of 1,100 acres *per annum*<sup>(141)</sup>.

### (3) *Revenue Estimates*

#### (a) *Total revenue*

147 Actual revenue in 1970-71 was only \$2,914 million. The revised estimate of revenue in 1979-80 is \$16,550 million<sup>(142)</sup>.

148 The Revenue Estimates as printed anticipate that total revenue collections will be \$21,533 million in 1980-81 but, on an adjusted basis, this figure

(138) *B.S., 1979, paragraph 153.*

(139)		<i>Production (flats)</i>
	1976-77	9,620
	1977-78	13,020
	1978-79	14,130
	1979-80 (estimated)	33,075
		<u>69,845</u>

(140) Excluding 62 acres, 25 acres and 24 acres respectively for land formed for/by the Industrial Estates Corporation. *c.f.* figures in *f.n.* (106) in Appendix II.

(141) Excluding another 62 acres and 30 acres which will be formed in 1981-82 and 1982-83 respectively by the Industrial Estates Corporation at Yuen Long.

(142) See Annex (2).

becomes \$21,428 million<sup>(143)</sup>, which is an increase of \$4,878 million, or 29%, on the revised estimate for 1979-80.

(b) *Recurrent*

149 My estimate of recurrent revenue in 1980-81 is \$14,798 million, an increase of \$1,584 million, or 12%, on the revised estimate for 1979-80 of \$13,214 million.

150 *Earnings and profits taxes* account for \$6,920 million, or 47%, of recurrent revenue. This represents an increase of \$1,040 million, or 18%, on the revised estimate for 1979-80 of \$5,880 million, which was \$1,765 million, or 43%, up on actual collections in 1978-79 of \$4,115 million<sup>(144)</sup>, such has been the growth rate of money incomes in recent years, particularly in the banking and property sectors.

151 I have assumed that the yield from *stamp duties* will be \$750 million, which is \$50 million less than the revised estimate for 1979-80 (which, in turn, is equal to the original estimate, thanks to the higher turnover recorded on the stock exchanges in the last two months or so).

152 I have assumed that the yield from *bets and sweeps taxes* will be \$720 million (or 12.5% up on the revised estimate for 1979-80 which is slightly above the original estimate, despite fewer night race meetings). The contribution of bets and sweeps taxes to total recurrent revenue could now be, to my dismay, on a downward trend: from 1.5% in 1970-71 it reached a peak of 5% in 1978-79, but has since declined slightly. However, I shall refrain from further comment for the moment.

153 The estimated yield from *dutiable commodities* in 1980-81 is \$942 million (up by 6% on the revised estimate for 1979-80). Duties will contribute 6.4% to total recurrent revenue in 1980-81, which is almost the same as rates (although neither revenue head is contributing as much as it should but, again, I shall refrain from further comment for the moment).

(143) That is, \$21,533 million—\$80 million being payments for land premia from the Home Ownership Fund—\$25 million being reimbursement from the Special Coin Suspense Account for the Jubilee Sports Centre=\$21,428 million. All these adjustments are on capital account.

(144)

	1978-79	1979-80	1980-81
	Actual	Revised	Estimates
	(\$ mn)	(\$ mn)	(\$ mn)
<i>Profits tax</i>	2,651	4,040	4,625
<i>Salaries tax</i>	1,012	1,290	1,700
<i>Personal assessment</i>	114	105	111
<i>Interest tax</i>	100	170	190
<i>Property tax</i>	238	275	295
<i>Total</i>	<u>4,115</u>	<u>5,880</u>	<u>6,920</u>

(c) *Capital*

154 My estimate of capital revenue is \$6,630 million, which is an increase of \$3,294 million, or 99%, on the revised estimate for 1979-80.

155 Within this staggering estimate of \$6,630 million, land transactions are expected to bring in \$6,169 million<sup>(145)</sup> (as opposed to the revised estimate for 1979-80 of \$2,858 million), taxi concessions a modest \$275 million and estate duty a mere \$170 million.

156 Within the estimate for land transactions of \$6,169 million, *land sales*<sup>(146)</sup> are expected to yield \$5,168 million from the sale of 197 acres, compared with the revised estimate for 1979-80 of \$2,223 million from the sale of 95 acres<sup>(147)</sup>; *private treaty grants* are expected to yield \$525 million from the sale of 38 acres, compared with the revised estimate for 1979-80 of \$147 million from the sale of 298 acres<sup>(148)</sup>; and *modifications and regrants* are expected to yield \$476 million, which is slightly down on the revised estimate for 1979-80 of \$488 million.

157 In the last four years, 1976-77 to 1979-80, land sales have been 38 acres, 34 acres, 57 acres and 95 acres respectively. The fact that the land sales programme in 1980-81 envisages the sale of no less than 197 acres is a

(145) *The estimate of \$6,169 million is based on an assessment by the land authorities of the prices likely to be realized for the individual sites making up the land sales programme for 1980-81 and has regard to present payment terms. That is to say, it has been calculated with reference to December 1979 values and takes account of the change in the terms of sale for commercial/residential purposes which requires payment of the full premium in a single lump sum. The estimate also includes instalments of premia from the sale of commercial/residential and industrial land in previous years. For sales in the New Territories, a provisional assessment has been made of the number of lots to be sold by auction and by Letter B tender, the revenue from the latter being particularly difficult to assess as it depends on the age of the Letters B offered by successful tenderers.*

(146) *Land sales being defined so as to include land disposed of by tender in exchange for Letters B, and the lots themselves being either drawn from newly formed and serviced land or from areas released from other uses (e.g. open storage let on short-term tenancies).*

(147)	Industrial		Non-industrial		Total	
	1979-80	1980-81	1979-80	1980-81	1979-80	1980-81
	Acres		Acres		Acres	
Urban areas	7.4	27.9	28.4	69.8	35.8	97.7
New Territories	11.5	17.0	47.9	82.3	59.4	99.3
	<u>18.9</u>	<u>44.9</u>	<u>76.3</u>	<u>152.1</u>	<u>95.2</u>	<u>197.0</u>

(148) *Private treaty grants have fluctuated as follows in recent years:*

	Acres	
1976-77	310	(largely the Sha Tin race-course and the Kwai Chung Container Terminal)
1977-78	138	(Tai Po Industrial Estate)
1978-79	479	(largely Clearwater Bay Golf and Country Club and Tsing Yi dockyard)
1979-80	298	(largely for power stations)

reflection of the build up of expenditure on development works in the post-recession perRTL<sup>(149)</sup>. So, in 1980-81, 26 industrial lots and 77 non-industrial lots will be offered for sale, many of which will be very large lots; and in addition, two extremely valuable sites in the central districts of Hong Kong and Kowloon will be ready for sale for commercial development and they affect the revenue estimate.

158 I explained earlier the implications of the high levels of expenditure on development works achieved in the past four years for land production in the new forecast period, 1981-82 to 1983-84<sup>(150)</sup>. The outlook for land sales should, therefore, be mentioned here: the forecast is for 219 acres to be sold in 1981-82, 151 acres in 1982-83 and 193 acres in 1983-84<sup>(151)</sup>.

159 Together with private treaty grants and modifications and regrants, the revenue yields implied in these figures are such as to mean that the financing of the capital account in the forecast period will continue to be less dependent on the surplus on recurrent account than hitherto. But all this is rather heroic crystal ball gazing.

(4) *Outturn and Assessment*

160 The difference between the estimate of revenue shown in the Revenue Estimates *as printed* of \$21,533 million and the Draft Estimates of Expenditure *as printed* amounting to \$18,442 million is \$3,091 million. After allowing for the net effect of various accounting adjustments of \$309 million<sup>(152)</sup>, this difference becomes \$3,400 million and this is the surplus I am budgeting for on General Revenue Account in 1980-81<sup>(153)</sup>.

(149) *The gross figures for land production in paras. 145-146 and f.n. (106) in Appendix II are, of course, inclusive of large areas appropriated for public housing, Government, institutional and community use, open space and roads.*

(150) *See paragraph 146 above.*

(151)	Urban areas (acres)	New Territories (acres)
1981-82	110	109
1982-83	99	52
1983-84	124	69

(152) *See f.n.s. (126) and (143) above.*

(153) Revenue:	\$ mn	\$ mn
Recurrent	14,798	
Capital	<u>6,630</u>	<u>21,428</u>
Expenditure:		
Recurrent	10,702	—
Capital	<u>7,326</u>	<u>18,028</u>
Surplus on recurrent account	—	4,096
Deficit on capital account	—	696
Overall surplus	—	3,400



161 An analysis of the budget I have just presented in terms of our guidelines<sup>(154)</sup> dramatically illustrates one point I made earlier<sup>(155)</sup>, namely, that Guideline (4), which sets an upper limit to recurrent expenditure of no more than 70% of total expenditure, may have to be redefined. We need to ensure that we do not get ourselves locked into a level of expenditure on capital account which will not be sustainable as/when the level of capital revenue settles down and the financing of capital expenditure is again largely dependent on the surplus on recurrent account. Otherwise, we shall become unduly dependent on debt finance to finance the deficit on capital account and/or the growth rate of recurrent expenditure will have to be unduly restricted. Capital revenue is now at such a level that only 10% of capital expenditure has to be financed by the surplus on recurrent account (whereas Guideline (5) envisages that up to 80% may be).

162 At the same time, the ratio of the surplus on recurrent account to capital expenditure in 1980-81 at 56% will be less than the guideline of 60% (Guideline (3)); and, whilst recurrent expenditure will only absorb 72% of recurrent revenue (as opposed to the upper limit set by Guideline (2) of 80%<sup>(156)</sup>), recurrent revenue will only finance 82% of total expenditure instead of the minimum set by Guideline (1) of 88%.

(154)		\$ mn	%	Guideline
(1)	$\frac{\text{Recurrent revenue}}{\text{Total expenditure}}$	14,798	$\frac{14,798}{18,028} = 82$	At least 88%
(2)	$\frac{\text{Recurrent expenditure}}{\text{Recurrent revenue}}$	10,702	$\frac{10,702}{14,798} = 72$	No more than 80%
(3)	$\frac{\text{Surplus on recurrent account}}{\text{Capital expenditure}}$	4,096	$\frac{4,096}{7,326} = 56$	At least 60%
(4)	$\frac{\text{Recurrent expenditure}}{\text{Total expenditure}}$	10,702	$\frac{10,702}{18,028} = 59$	No more than 70%
(5)	$\frac{\text{Capital revenue}}{\text{Capital expenditure}}$	6,630	$\frac{6,630}{7,326} = 90$	At least 20%

(155) See paragraph 61 above.

(156) However, this is a reversal of the trend since 1977-78 (see Annex (8)) and is due to the fact that the growth rate of recurrent expenditure, after being equal to the growth rate of recurrent revenue in the first two post-recession years, was below it in the next two years but, in 1980-81, will be above it, viz:

	1976-77	1977-78	1978-79	1979-80	1980-81
	(%)	(%)	(%)	Revised Estimates	Draft Estimates
Recurrent expenditure	17.4	19.0	17.5	24.3	17.9
Recurrent revenue	17.3	19.0	24.5	30.2	12.0

163 So, within our presently buoyant financial situation, lie seeds of real trouble for the future and, during the coming year, I shall be considering whether our guidelines need to be revised to provide a new framework within which to discipline our thinking.

164 As regards the steady progression guideline of 10%, the (adjusted) provision in the Draft Estimates of Expenditure implies a growth rate in real terms of 12% compared with 7% in 1979-80 (revised estimates).

(5) *Pattern of Expenditure on Consolidated Account*

165 I said earlier, Sir, that there was no such thing as an ideal pattern of public sector expenditure for priorities must be readily adjusted to changing circumstances<sup>(157)</sup>, but it is useful to evaluate the proposed pattern of expenditure on Consolidated Account in 1980-81 in the context of our historical experience<sup>(158)</sup>.

166 General services will absorb 14.8% of total expenditure compared with an historical ratio based on actual experience in the 1970s of 16.7% (and, within this group, law and order will account for 11.7%, compared with 12.8%); economic services will absorb 8%, compared with a historical ratio of 8.5%; community services will absorb 22%, compared with a historical ratio of 24% (and, within this group, transport, roads, civil engineering and land will account for 12.8%, compared with a historical ratio of 10.7%); and social services will absorb 44.3%, compared with a historical ratio of 41.3% (and, within this group, housing will account for 18.6%, compared with a historical ratio of 9.8%)<sup>(158)</sup>.

167 Having regard to what I said earlier about priorities in the early years of the 1980s, I am not entirely satisfied that, in the Draft Estimates for 1980-81, there is sufficient emphasis on law and order and defence and our transport infrastructure; and, specifically, I would suggest that we should endeavour to allocate funds from the additional commitments vote in the capital account to enable an earlier than envisaged start to be made on the Hong Kong Island eastern corridor<sup>(159)</sup>.

(6) *Fiscal Policy*

(a) *General*

168 I pointed out earlier that we have already departed from the revised guideline ratios set in 1978 for the balance of the fiscal system<sup>(160)</sup>: instead

(157) See paragraph 58.

(158) The three residual groups will absorb 10.9% compared with the historical ratio of 9% (due to the larger additional commitments votes).

(159) Head 73 P.W.N.R.: Engineering Subhead 652.

(160) See paragraph 103 in Appendix II.

of the ratio of direct to indirect taxation being 55:45 and the ratio of direct and indirect taxation to all other recurrent revenue being 70:30, the ratios in 1979-80 were 61:39 and 73:27. There were three reasons for this: yields from earnings and profits taxes flushed; rates of indirect taxes and fees and charges lagged behind price increases; and there has been no revaluation of rateable values or upward adjustment of the rate percentage since 1977.

169 For the same reasons, on the basis of the Revenue Estimates as printed, the ratios will move further away to 63:37 and 74:26 in 1980-81. At the same time, the equity of the system as between different classes of taxpayers either will not improve or will further deteriorate. As regards *direct* taxes: although the estimated contribution of property tax to total recurrent revenue at 2% is only just below the contribution in 1979-80 (revised estimates) at 2.1%, this is simply because of additional yields from new properties<sup>(161)</sup>. The ratio of property tax to rates at 23:77 will be only slightly below that in 1979-80 (revised estimates) of 24:76, but will still be far too low<sup>(162)</sup>. As regards *indirect* taxes: rates will only contribute 6.6% to total recurrent revenue, compared with 6.8% in 1979-80 (revised estimates)<sup>(163)</sup>; and dutiable commodities will contribute only 6.4%, compared with 6.7% in 1979-80 (revised estimates)<sup>(164)</sup>. The contribution of bets and sweeps taxes seems to have peaked out inasmuch as, after reaching 5% in 1978-79, it fell to 4.8% in 1979-80 (revised estimates) and is estimated to be 4.9% in 1980-81.

170 Furthermore, although the contribution to total revenue of First Registration Tax on motor vehicles, together with annual licence fees for vehicles and drivers and duty on hydrocarbon oils, will be 6.4% in 1980-81, the same as in 1979-80 (revised estimates), it is well below the peak for the decade of 9.9% in 1970-71, and below the average contribution over the decade of 7.2%. But historical comparisons aside, I do not believe this adequately reflects what motorists and other road users ought to pay, given the size of our investment in road works in recent years, and presently in hand, and the importance of ensuring that available road space is used as effectively as possible, particularly as and when public transport services are improved and diversified. In saying that, I am not suggesting that fiscal weapons should play more than a marginal role in transport policy, whatever the price elasticity of demand by would-be car purchasers may be, and I do not think we should be unmindful of the influence that recent increases in the before-tax price of petrol and light diesel oil must be having on usage already.

---

(161) C.f. 3.7% in the peak year 1976-77 and 3% in 1977-78, when the new assessable values were established.

(162) C.f. 29:71 in 1976-77 and 25:75 in 1977-78, when the lists of rateable values based on the 1976 revaluation exercise became effective.

(163) C.f. 9% in the peak year 1970-71 and 8.9% in 1977-78, when the new lists of rateable values came into effect.

(164) C.f. 16% in 1970-71, the peak year for the decade.

*(b) Reserves of taxable capacity*

171 Even ignoring the possibility of increasing some tax rates, or widening the ambit of some of our revenue laws, without infringing, of course, any of the basic requirements of a tax system for Hong Kong<sup>(165)</sup>, it is apparent that we have considerable reserves of taxable capacity. In view of my concern about the falling trend of recurrent revenue to total expenditure<sup>(166)</sup>, I turned my attention to property tax, rates, dutiable commodities<sup>(167)</sup>, bets and sweeps taxes<sup>(168)</sup> and First Registration Tax on motor vehicles and annual licence fees for vehicles and drivers<sup>(169)</sup>. I also looked at the present state of play on the routine updating of cost-related and tax-loaded and royalty-loaded fees and charges<sup>(170)</sup> and the updating of charges raised for the services provided by our various public utility-type undertakings to restore the desired rate of return on capital employed<sup>(170)</sup>.

(165) See paras. 105-111 in Appendix II.

(166) See paragraph 60 above.

(167) Incidence of duties (examples only):

	Effective date of last duty change	Incidence immediately thereafter (%)	Present incidence (%)
<i>Liquor:</i>			
Brandy (V.S.O.P.)	3 December 1975	40	28
Whisky (Ordinary)	Ditto	58	28
Gin	Ditto	59	51
Beer: imported	Ditto	16	15
local	Ditto	18	16
<i>Chinese type spirit:</i>			
imported	Ditto	28	23
local	Ditto	26	22
<i>Tobacco:</i>			
<i>Cigarettes:</i>			
imported (U.K.)	1 March 1978	30	23
imported (U.S.)	Ditto	34	26
local	3 December 1975	37	26
<i>Hydrocarbon oils:</i>			
Motor spirit	25 February 1976	35	22
Diesel oil for road vehicles	Ditto	34	17

(168) A new rate of tax of 11% for exotic bets was introduced in 1975 (see C.S., 1975, paras. 41-42), but the rate for traditional bets has remained unchanged at 7½% since the beginning of time (i.e. 1931). As the average bet per punter per race-day has probably more than doubled in the past five years, and even having regard to the importance of discouraging illegal off-course bookmakers, there is obviously scope for increasing the yield from bets taxes by reducing the Jockey Club's commission (at present 9¼%) and, perhaps, even the proportion available for prize money (83¼%).

(169) Rates of F.R.T. were last raised on 1 March 1979 (see B.S., 1979, paras. 193-197), and so were licence fees for vehicles (see B.S., 1979, paras. 202-210). Fees for drivers' licences have remained unchanged since 1 March 1974.

(170) The Management Accounting Services Division of the Treasury monitors the extent to which various types of fees and charges (see f.n. (119) in Appendix II) lag behind costs, and the extent to which loadings are eroded over time. It is apparent that many fees and charges will have to be up-dated at an appropriate time (and, incidentally, the up-dating of these fees and charges must normally be determined by management and not 'political' considerations).

172 In pondering what to do, if anything, I tried to avoid being influenced by considerations of what might, or might not, be thought to be 'politically' tolerable at the present time and I also wished to avoid being criticized, after the event, for not increasing tax rates and rates of other charges once it had become general knowledge that I did not intend to do so. In the end, however, I decided not to propose any increases for the time being, for two reasons: generally, because our financial position does not indicate an *immediate* need to boost recurrent revenue, for the guideline which requires us to ensure that recurrent expenditure absorbs no more than 80% of recurrent revenue is still being met; and because I think that, in most cases, the elasticities are such that increases in rates of charge could be mildly inflationary and this possibility I wished to avoid at this time. Let what I have said be taken as a broad hint that there will be increases next year, leading to avoidance action through speculative purchases, I should add that there is no necessary reason why fiscal proposals have to be announced in the budget speech (*laughter*); and, of course, cost-related fees and charges and charges raised for the services of our public utilitytype undertakings cannot be allowed to lag behind full costs (appropriately defined) for very long.

173 In fact, we have just announced a revision of passenger charges for the K.C.R. effective from 1 April next which, incidentally, will nowhere near yield a satisfactory rate of return on that enterprise even in relation to present capital employed, let alone once we have finished investing nearly \$2,000 million in double tracking, electrification, new rolling stock and modernized facilities over the five years ending 1983-84. I should also mention just for record that revised sand prices are long overdue; and various airport charges are currently under review and may well be introduced later on this year.

174 Having said all that, there is one cost-related fee increase which I shall announce forthwith, effective from tomorrow: in recent years, there has been a significant increase in the number of requests for certified copies or extracts of documents which, under the provisions of the Business Registration Ordinance, any person may require the Commissioner of Inland Revenue to provide on payment of the prescribed fee. In 1978-79, the Business Registration Office issued over 92,000 certified copies or extracts of business registration documents and, currently, requests are being received at the rate of 2,000 per week. Certified copies or extracts are sought for a variety of reasons, but usually relate to a desire to ascertain the identity of the proprietors of a business with whom a transaction is intended. I am not satisfied that the Government is being adequately recompensed for the effort involved in providing these certified copies or extracts by the prescribed fee of \$15 and so I propose that the fee should be doubled to \$30, bringing in extra revenue of at least \$1.5 million a year.

(c) *Revaluation of rateable values*

175 Last year<sup>(171)</sup>, I said that serious consideration would need to be given during 1979 to the possibility of a revaluation of rateable values in 1980. Accordingly, without being finally committed, I instructed the Commissioner of Rating and Valuation to make the necessary preparations and, for this purpose, requisitions for particulars of tenements were despatched to ratepayers towards the end of 1979. Everything, in fact, was in train for a revaluation exercise during 1980 with a view to bringing new lists of rateable values into effect on 1 April 1981.

176 I now have to advise honourable Members that this revaluation has been indefinitely abandoned for three reasons: *first*, the Commissioner has had to divert experienced professional and technical staff to rent control work as a result of the recent decision to extend rent controls to all domestic accommodation as provided for in the Landlord and Tenant (Consolidation) (Amendment) Ordinance 1980<sup>(172)</sup>. *Secondly*, this is a more important reason, rateable values by law have to be related to unfettered market rents. As a result of the imposition of blanket rent controls, there is now unlikely to be sufficient usable data to provide a sound basis for updating rateable values of domestic premises. *Thirdly*, such controls tend, *per se*, to distort the market situation in that, although rents for first and fresh lettings are not restricted, the free rental market is subject to abnormal pressures as landlords attempt to mitigate the effects of being encumbered with controlled tenants.

177 The fact is that, until a sufficiently large free rental market for domestic accommodation is re-established and the gap between controlled rents and market rents is narrowed, there are poor prospects for a revaluation on the present historical basis. Indeed, we may possibly have to think of using capital values as an approach to the establishment of rateable values, as has been proposed in the United Kingdom. Naturally, the Commissioner of Rating and Valuation and I gave consideration to the possibility of revising rateable values for non-domestic premises alone, but we concluded that it would be manifestly unfair to penalize that sector which is not, and is not to be, brought under the umbrella of rent control.

178 The abandonment of the revaluation exercise for the time being has, of course, revenue implications for 1981-82. While the purpose of a revaluation of rateable values is to ensure that the rate burden is fairly distributed as between ratepayers, to the extent that rateable values are increased,

---

(171) *B.S., 1979, paragraph 230.*

(172) *The Commissioner has had to accept not only the burden of a greatly increased workload in dealing with a further 43,000 controlled tenancies, in addition to the 150,000 post-war domestic tenancies controlled under the 1973 amendment to the Ordinance, plus subtenancies, but also the added responsibility of monitoring certain of the criminal provisions of the new legislation. The Rating and Valuation Department, in addition to servicing the recently announced Review Committee on Rent Control, will have to provide an on-going monitoring service of the domestic rental markets.*

there is scope for raising extra (recurrent) revenue at a given percentage rate. As I said last year, given the time span between revaluation, any future revaluation may or may not have to be compensated for by a reduction in the percentage rate<sup>(173)</sup>.

179 But, meanwhile, the converse may apply if the revenue is to be protected; and so, accordingly, I now give due notice of my intention to consider an increase in the General Rate percentage for 1981-82. Rates are one of our major indirect taxes; they are certain in application and relatively inexpensive to administer and collect. Their relative significance cannot be allowed to diminish, with consequences for the balance of the fiscal system as between direct and indirect taxation, merely because of the effect of other non-fiscal legislation. I would remind honourable Members of what I said in 1975: 'Rates catch many who would otherwise contribute little or nothing to the revenue and this should be borne in mind by those who vociferously complain that the direct tax net is cast across too restricted a field'<sup>(174)</sup>. Not to be overlooked in addition, of course, are the revenue needs of the Urban Council which presently receives one-third of the revenue derived from the urban areas. As the Chairman recently indicated in the speech on 13 November last, the Council expected the revaluation of rateable values in 1981-82 and I quote 'to catch up with the swiftly rising cost of the Council's expanding services'.

*(d) Reassessment of assessable values for property tax*

180 Having decided to abandon the 1980 revaluation of rateable values, I then had to consider the fate of the review of assessable values for 1980-81 which was to have been undertaken at the same time by the Commissioner of Rating and Valuation on behalf of the Commissioner of Inland Revenue.

181 Simply stated, assessable values, like rateable values, are based on the free rental market concept, unless the rent is controlled under the Landlord and Tenant (Consolidation) Ordinance, when the controlled rent is substituted for the free market rent. This ensures that an owner is not taxed on a greater amount. For pre-war controlled premises, and the 150,000 or so post-war domestic premises which have been subject to controls since 1970 or 1973, the Commissioner of Rating and Valuation already has in his possession extensive information on rents. For the 43,000 post-war domestic premises recently brought under control, however, the controlled rents in many cases have yet to be lawfully established. Moreover, rents for domestic premises not previously subject to control increased substantially towards the end of 1979, as did rents for offices and retail shops.

---

(173) *Not to be overlooked, of course, are the revenue needs of the Urban Council which presently receives over one-third of the rates revenue derived from the urban areas. As the Chairman recently indicated (in a speech on 13 November 1979) the Council expected the revaluation of rateable values in 1981-82 'catch up with the swiftly rising cost of (their) expanding services.....'.*

(174) *B.S., 1975, paragraph 108.*

182 To ascertain proper assessable values for the purpose of property tax with a reasonable degree of certainty it would, therefore, be necessary to send out a further return to obtain information relative to 1 April 1980. This information would then have to be recorded and analysed and, for those premises newly brought under control, it would be desirable to delay fixing the assessable values until such time as the processing of initial applications to establish controlled rents is completed. Given these constraints, tight schedules on computer processing and doubts as to the availability of the necessary staff, reluctantly I have had to conclude that this exercise must be postponed.

183 I say 'postponed', and not 'abandoned'. I say 'postponed' because there are serious revenue implications in this decision. An additional sum of \$120 million was expected in 1980-81 as a result of the proposed review and, given the way rents have moved since that estimate was made, the eventual figure could have been somewhat higher<sup>(175)</sup>. But, as it will be some time before we can even consider moving over to an income (or rent passing) basis for the assessment of property values as recommended by the Third Inland Revenue Ordinance Review Committee<sup>(176)</sup>, there can be no question of the next review of assessable values not being undertaken for 1981-82. By that time, the Commissioner of Rating and Valuation should have sorted out most of the initial problems associated with the extended rent controls and solved his immediate staffing problems. Over the remainder of this year, therefore, planning will proceed with this end in view, and a fresh return will be sent to owners and occupiers early in 1981.

184 But, because of the quite unwarranted loss of revenue and the diminishing share of the direct tax burden being borne by property owners, other than corporations, I considered whether there were any other possibilities open to me to improve the yield from property tax, whilst remaining within the assessable value concept. The Commissioner of Inland Revenue and I looked closely at three possibilities: *first*, to uplift gross assessable values across-the-board by the use of a percentage inflator, thereby recognizing that there has been a general increase in rents; *secondly*, to reduce the 20% allowance for repairs and outgoings granted in all cases in arriving at net assessable values; and, *thirdly*, to increase the rate of tax chargeable on net assessable values, i.e. to supplement standard rate of tax at 15% with some higher rate for property tax purposes.

185 In each case, however, we were confronted with insurmountable conceptual and practical difficulties, and I concluded, therefore, that the basis of charge to property tax must remain unchanged until 1981-82 when, as I have said, it will be possible to introduce revised assessable values.

---

(175) *As it is, the estimate for 1980-81 is only \$20 million up on the revised estimate for 1979-80 reflecting the yield from new properties.*

(176) *Report (1976), paragraph 161.*



*(e) Tax reforms in hand*

186 Last year, I made reference to three questions which were the subject of recommendations or comment by the Third Inland Revenue Ordinance Review Committee: *first*, the idea of a system of ‘pooling’ of capital expenditure as a means of simplifying the calculation of depreciation allowances for the purposes of profits tax<sup>(177)</sup>; *secondly*, the case for granting relief to trustees who become subject to withholding tax on interest received and thereafter are obliged to deduct interest tax a second time from interest paid to beneficiaries of the trust fund<sup>(178)</sup>; *thirdly*, the existence of a possible *lacuna* in the Inland Revenue Ordinance whereby surpluses thrown up on the redemption or realization of certificates of deposit and similar entitlements to stated sums of money may escape liability to tax<sup>(179)</sup>.

187 I undertook to have amendments to the Ordinance drafted in respect of the first two questions. Despite the relatively simple concepts involved, the drafting of the necessary legislation has proved unusually difficult, but it is now nearing completion. As regards the taxation treatment of certificates of deposits and monetary instruments, I have concluded that, on grounds of equity and to protect the revenue, the Ordinance should be amended to place the interest tax or profits tax liability, as the case may be, of the surpluses realized on these instruments beyond doubt, and a bill is now in draft form. Incidentally, Sir, I have considered, yet again, the case for abolishing interest withholding tax altogether but have concluded, yet again, that this would not be justified on monetary or fiscal grounds.

*(f) Tax reform proposed for 1980-81: contrived cessations of business*

188 I have only one tax reform proposal this year but it is a mildly complicated one: the Commissioner of Inland Revenue has drawn my attention to a loophole in the transitional provisions which were enacted when the method of assessment of profits tax was changed in 1975-76 from a preceding year basis to an actual year basis. The loophole appears to have been the consequence of an anxiety on our part not to deprive persons genuinely going out of business of their rights to a form of terminal relief. It is now clear, however, that the generous approach adopted in 1975 is being exploited by some property developers and speculators who, through the use of contrived cessations of business, are succeeding in dropping out of charge to tax enormous profits on sales of properties at a considerable cost to revenue. Clearly, this state of affairs cannot be allowed to continue and, accordingly, an amending bill which will close this loophole is about to be published. As I am bound to be accused of closing the stable door after

---

(177) B.S., 1979, paras. 171-172 (in accordance with the fourth requirement of the tax system: see paragraph 108 in Appendix II and Annex (7)).

(178) B.S., 1979, paragraph 223 (in accordance with the fifth requirement: see paragraph 109 in Appendix II and Annex (7)).

(179) B.S., 1979, paragraph 224 (in accordance with the first, third and fifth requirements: see paras. 105, 107 and 109 in Appendix II).

the horse has bolted, I should make it clear that there is no time limit on those contrived cessations so that, without corrective legislation now, considerable sums of future revenue will remain at risk.

(g) *Tax concessions proposed for 1980-81*

189 Despite my concern, Sir, about the longer term outlook for General Revenue and the present imbalance in the fiscal system, I have four concessions to propose for 1980-81.

(i) *Personal taxation*

190 Personal taxation (that is to say salaries tax and personal assessment) engenders a good deal of comment each year and certainly no less than usual this year (*laughter*). It is alleged in some quarters that the level of personal taxation has had scant regard, over the years, to the effects of inflation and that, as a consequence, personal taxation now embraces a very much larger proportion of the economically active population. Certainly, it is true that the yield has been increasing, but this is due to the growth rate of incomes in recent years<sup>(180)</sup>, resulting also in an increase in the number of taxpayers (giving, incidentally, the Commissioner of Inland Revenue some not inconsiderable administrative problems). However, not only has the progression of effective rates of tax been stretched out by adjustments, from time to time, to the platforms and the system of allowances, but also the standard rate of 15% applicable to those in the gross income zone has remained unchanged for 14 years. Specifically, I would claim that the increases in personal allowances announced in my 1977 and 1979 budget speeches have mitigated the liability of personal taxpayers generally as well as of those who arguably have been brought to charge through the effects of inflation alone<sup>(181)</sup>.

---

(180) See *f.n. (4) above*.

(181) See *B.S., 1977, paras. 208-216 and B.S., 1979, paras. 173-177. Briefly:*

- (a) *with effect from 1976-77, supplementary personal allowances (\$2,500 single; \$5,000 married) effectively increased the levels of income at which persons are totally exempt by 25%; and further, through the adoption of a claw-back mechanism, provided relief for single taxpayers up to a maximum annual income of \$29,167 and relief for married taxpayers up to a maximum annual income of \$58,334;*
- (b) *with effect from 1976-77, child allowances were increased from \$3,000 to \$4,000 for the first child, from \$2,500 to \$3,000 for the second child and from \$1,500 to \$2,000 for the third child. The allowance for the fourth to the sixth child remained at \$1,000 each and for the seventh to the ninth child remained at \$500 each. Thus, for a three-child family, allowances were increased by 28.5% and, for a nine-child family, by 17.4%.*
- (c) *with effect from 1978-79, the claw-back mechanism was reduced from 15% to 10%, thereby extending relief for single taxpayers up to a maximum annual income of \$37,500 and for married taxpayers up to a maximum annual income of \$75,000;*
- (d) *with effect from 1978-79, a dependent parent allowance was reintroduced at the rate of \$4,000 for each dependent parent over 60 years of age (double the allowance given up to 1972-73), with no limit on the number of claimable dependent parents;*
- (e) *with effect from 1978-79, the 30% maximum graduated rate was abolished, thereby reducing the maximum rate at the margin to 25% (but subject still to an overall maximum rate of 15% on gross assessable income less outgoings and expenses).*

191 Unresearched, strident claims to the contrary, personal taxation in Hong Kong at any income level is, in *no* sense, punitive. I say this notwithstanding views which have been expressed that the entry points into the tax net (the so-called thresholds) are now too low and that, further, taxpayers in the middle-income groups are increasingly subject to economic pressures. These pressures are, in fact, associated with and, indeed, are a consequence of, growing affluence.

192 Nevertheless, this being the Year of the Monkey (*laughter*), I have four proposals to make in regard to personal taxation, proposals which are so generous as to merit no further argument (*laughter*): *first*, I propose an increase in the level of personal allowances from \$10,000 to \$12,500 for single persons and from \$20,000 to \$25,000 for married persons.

193 *Secondly*, honourable Members will recall that last year, I reduced the percentage claw-back applicable to the supplementary personal allowances from 15% to 10%. I now propose to zero-rate the claw-back so that, save for those persons on high incomes to whom the standard rate of tax applies, taxpayers at all levels will enjoy the full benefit of the supplementary personal allowances, which will remain at \$2,500 for a single person and \$5,000 for a married person. Effectively, therefore, this proposal, combined with the proposed increases in personal allowances, will mean that all single persons on annual incomes of \$15,000 or less will be totally exempt, and married persons on annual incomes of \$30,000 or less will also be totally exempt.

194 *Thirdly*, I propose an increase in child allowances, from \$4,000 to \$5,000 for the first child, from \$3,000 to \$4,000 for the second child, from \$2,000 to \$3,000 for the third child, from \$1,000 to \$2,000 for the fourth, fifth and sixth child and, finally, from \$500 to \$1,000 for the seventh, eighth and ninth child if you have them (*laughter*).

195 *Fourthly*, I propose an increase in the dependent parent allowance from \$4,000 to \$5,000. I make this proposal without further comment. The criteria, I might add though, for the granting of this allowance will remain unchanged<sup>(182)</sup>.

196 The implementation of these four proposals will be effective for final salaries tax assessment for 1979-80 (and for personal assessment also) and provisional salaries tax for 1980-81. The cost to the revenue will be considerable. In 1980-81, after allowing for the two instalment system for salaries tax, the cost will be \$331 million in respect of increased personal allowances and \$38 million and \$14 million in respect of the increased child allowances and the increased dependent parent allowance. The cost of these proposals in respect of taxpayers opting for personal assessment

---

(182) See *B.S.*, 1979, *Annex (10)*.

is estimated to be \$43 million in 1980-81. The total cost to the revenue in 1980-81 will, therefore, be \$426 million<sup>(183)</sup>.

197 The effect of these proposals will be to exempt 15,000 persons previously liable to salaries tax and a further 45,000, who would have become chargeable in 1980-81, will remain out of the tax net. Additionally, 265,000 salaries taxpayers will benefit by way of reduced liability and a further 50,000 will benefit under personal assessment. Examples of the effects of the new allowances on persons at various income levels and in various personal circumstances appear at Annex (13) to the printed version of this speech; a table showing the present and future effective rates of tax at different income levels for persons in various personal circumstances is at Annex (14); and I have set out at Annex (15), the levels at which persons in various personal circumstances will become liable to the full standard rate in future. Forlornly, I would ask that these annexes be examined with care and not ignored: for instance, the effect of these proposals will be to reduce the tax payable by a married man on an annual income of \$60,000 with two children and two dependent parents from \$2,025 at present (or 3.4% of his annual income) to \$600 (or 1% of his annual income). As I say, I do hope that these annexes are studied by public at large and the press in particular (*laughter*).

(ii) *Interest tax liability of credit unions*

198 The tax liability of credit unions has also recently given rise to a good deal of comment. The objects of a credit union are, *first*, to promote thrift among its members; *secondly*, to receive the savings of its members either as payment on shares or as deposits; and, *thirdly*, to make loans to its members, and I quote 'exclusively for provident or productive purposes'<sup>(184)</sup>.

199 A decision was handed down by the Board of Review in 1979 that a credit union is a club and not a business. Thus, credit unions are not liable to profits tax. They are, however, liable to tax on the interest earned on investments or on loans made to members. As regards outside investment income, I see no compelling argument to justify exemption from interest withholding tax; credit unions are neither charitable institutions nor trusts of a public character. As regards interest on loans made to members, however, I am persuaded that exemption from tax would be consistent with the statutory objects of credit unions, and I propose, therefore, that the Inland Revenue Ordinance should be amended to grant exemption as from the year of assessment 1980-81 at a cost to the revenue of \$100,000 (*laughter*).

(iii) *Estate duty*

200 Honourable Members, Sir, will recall that last year I referred to a loophole in the controlled companies provisions of the Estate Duty

---

(183) *The cost in a 'full' (i.e. an ordinary) year will be around \$264 million at present levels of chargeable incomes.*

(184) *Section 3(2) of the Credit Unions Ordinance (Cap. 119).*

Ordinance<sup>(185)</sup>, which had the effect of undermining the original intention of those provisions and, therefore, of enabling the wealthier members of the community, should they be so inclined, to avoid their legal obligations. I undertook to plug that loophole and so this Council enacted the Estate Duty (Amendment) (No. 2) Ordinance 1979 which came into force on 4 July 1979.

201 This year, however, I am concerned with estates which currently attract duty at the lower end of the scale. The exemption limit was last raised to \$400,000 in 1977 and, having regard in particular to prevailing property prices, I consider that it is again time to lift the ceiling at which duty becomes payable. I propose, therefore, to raise the exemption limit to \$600,000 for the estates of persons dying after the enactment of the necessary legislation. The cost to the revenue of this proposal will be about \$5 million in 1980-81.

(iv) *Stamp duty on conveyances of low value properties*

202 In 1977, new platforms were introduced for the concessionary rates of duty on conveyances of low value properties provided for under Head 19(1) of the Schedule to the Stamp Ordinance. Thus, the fixed concessionary rate of \$20 was levied on properties up to \$100,000, as compared with \$75,000 previously; and the concessionary *ad valorem* rate of duty of 1% was levied on properties valued at between \$100,000 and \$175,000, as compared with \$75,000 and \$150,000 previously. The full *ad valorem* rate of duty of 2¾% became payable on properties above \$175,000, as compared with \$150,000 previously.

203 In recognition of the much higher level of prices of domestic flats, I propose that the limit for the concessionary *ad valorem* rate of duty of 1% should be raised by \$75,000 to \$250,000 at a cost to the revenue of no less than \$67 million in 1980-81. In recent years, about 40,000 purchasers of flats a year have benefitted from these concessionary rates, and a further 18,000 purchasers a year will benefit as a result of this higher limit for the 1% rate (and, remember, it is in fact the *purchaser* who, in practice, pays the duty on the assignment).

204 The new platform will have to be extended also to Head 53(1) voluntary dispositions *inter vivos*.

(v) *Implementation*

205 As Your Excellency this morning signed the necessary Orders under the Public Revenue Protection Ordinance, the increased fee for certified copies or extracts of business registration documents and the higher limit of \$250,000 up to which the concessionary *ad valorem* rate of stamp duty of 1% will apply will be effective from the opening of business tomorrow morning. Bills to amend the Inland Revenue Ordinance to provide for my proposals in

---

(185) *B.S., 1979, paras. 178-182.*

respect of personal taxation and the Estate Duty Ordinance to raise the exemption limit for small estates will be introduced into this Council as soon as possible.

(7) *Assessment and Outturn*

(a) *Balance of fiscal system*

206 These four concessions<sup>(186)</sup>, together with the increased fee for certified copies or extracts of business registration documents, will have the effect of slightly improving the ratio of direct to indirect taxation compared with the ratio based on the Revenue Estimates as printed: the ratio will become 62:38, compared with 63:37; but the ratio of direct and indirect taxation taken together to all other recurrent revenue will remain at 73:27.

(b) *Outturn and state of reserves*

207 The net cost to the revenue of these five proposals will amount to \$496 million in 1980-81<sup>(187)</sup> and thus my estimate of revenue for 1980-81 becomes \$20,932 million. So, effectively, I am budgeting for a surplus of \$2,904 million. This represents 14% of estimated revenue and is in line with our actual experience in each of the four post-recession years, 1976-77 to 1979-80<sup>(188)</sup>.

208 Should this budgetted for surplus materialize—and I would stress again that the estimate of revenue from land sales is heroic, and incidentally, the way in which the estimate is made up is explained in crystal clear details in a number of foot notes—should this budgetted for surpens materialize, our ‘free’ fiscal reserves at 31 March 1981 should be of the order of \$8,600 million<sup>(189)</sup>. Obviously, therefore, at that date we shall be well in excess of the guideline of 15% of likely expenditure in 1981-82; and, indeed, even more so than at 1 April 1980 when our ‘free’ reserves will stand at about 31% of estimated expenditure in 1980-81<sup>(190)</sup>.

(186) *Classified in terms of our tax requirements (see paras. 105-111 in Appendix II):*

<i>Proposal</i>	<i>Requirement</i>
<i>Personal taxation</i>	<i>Fifth</i>
<i>Credit unions</i>	<i>Fifth and sixth</i>
<i>Estate duty</i>	<i>Fifth</i>
<i>Stamp duty on conveyances of low value properties</i>	<i>Fifth</i>
<i>and the reform of the law to deal with contrived cessations of business comes under the fourth requirement.</i>	

(187) *And \$334 million in a ‘full’ year.*

(188)	<i>Actual revenue</i>	<i>Actual surplus</i>	(2) <i>as % of</i>
	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>(1)</i>
<i>1976-77</i>	<i>7,494</i>	<i>917</i>	<i>12</i>
<i>1977-78</i>	<i>9,383</i>	<i>1,225</i>	<i>13</i>
<i>1978-79</i>	<i>12,442</i>	<i>1,486</i>	<i>12</i>
<i>1979-80 (R.E.)</i>	<i>16,550</i>	<i>2,318</i>	<i>14</i>

(189) *That is, \$5,700 million being our ‘free’ fiscal reserves at 1 April 1980 (see paragraph 52 above) + \$2,904 million = say, \$8,600 million.*

(190) *See paragraph 53 above.*

209 Thus we shall have a most comforting degree of security in these most uncertain times as we entered the uncharted waters of the 1980s. That is the *first* point to bear in mind when considering the present state of our 'free' fiscal reserves (for which, of course, I do *not* apologize, given the average annual growth rate of expenditure on General Revenue Account for the four years 1977-78 to 1980-81 of 29% in money terms and 15% in real terms).

210 The *second* is this: without prejudicing our ability to maintain a given level of expenditure in the face of any difficulties we may encounter in the forecast years, we shall be well placed to finance additional expenditure over and above that provided for in the Draft Estimates for 1980-81 should further unexpected and unavoidable commitments be thrust upon us or should we decide, in exceptional circumstances, to increase the level of expenditure on certain works programmes (and here I stress *works* programmes for the rapid build-up of our reserves in recent years has been due to the fact that an unusually large proportion of capital expenditure has been financed by capital revenue).

211 The *third* point to bear in mind is that it is from our 'free' fiscal reserves that we shall have to draw funds to finance any scheme to provide for housing loans for civil servants as and when the parties concerned can reach agreement on the details of such a scheme; to set up an enlargement of, or to extend the concept of, the Home Ownership Scheme; and to increase our equity position in, for example, the Mass Transit Railway Corporation should that be necessary to enable the Corporation to raise additional debt finance for any further extension of the railway that may be decided upon.

212 Furthermore, I would remind honourable Members, and this is my *fourth* point regarding the reserves, I would remind honourable Members that in the 1980s, the demands on our economic and social infrastructure will become acute and progressively more expensive to meet; and, also, there are, on the stocks, several very large public works projects, the financing of which will probably require a blend of debt finance and of grants from General Revenue (against a pricing policy designed to ensure that a positive cash flow is ultimately generated sufficient to repay the debt and earn a return on the capital employed).

(8) *The Public Sector and the Economy*

213 Finally, I must assess the likely impact of the public sector, defined in terms of the Consolidated Account, on the maintenance of economic stability in 1980-81.

(a) *Growth and relative size of the public sector*

214 The average annual growth rate of expenditure on Consolidated Account in real terms over the ten years, 1970-71 to 1979-80, was 11.2% which exceeded the growth rate of G.D.P. in real terms at 9% over the same period. After accelerating from 4.5% in 1976-77 to 18.5% in 1977-78 and to 21.7%

in 1978-79, the growth rate of expenditure was slowed down to 10.7% in 1979-80. I am allowing it to accelerate again to 13.4% in 1980-81, which is well in excess of the forecast growth rate of G.D.P. in 1980 of 9%. Thus the relative size of the public sector will further increase from its historical high of 18.7% in 1979-80 to 19.7% in 1980-81<sup>(191)</sup>. This reflects a very high level of expenditure on Consolidated Account and, whilst it may be just acceptable on macro-economic grounds, it does underline the importance of all concerned ensuring that the value-for-money criterion is conscientiously observed at all times. The fact is that the greater the volume of public sector transactions, the greater the scope for public funds to be disbursed inefficiently and for assets to be underutilized.

(b) *Balance of the public sector*

215 I have already explained why I thought an outcome along these lines for 1980-81 would be just about acceptable and one of the reasons I gave was that I thought the public sector on both General Revenue Account and Consolidated Account would be in surplus<sup>(192)</sup>. This is the case: on General Revenue Account the estimated surplus is \$2,904 million and on Consolidated Account it is \$2,649 million<sup>(193)</sup>. To ensure that the surplus on General Revenue Account has its full constraining effect on domestic demand by the private sector, and hence on total domestic demand, the consequent increase in the government's Hong Kong dollar balances will be either placed by the Exchange Fund short term (that is, on demand, at call or at short notice) thus attracting the 100% liquid assets requirement<sup>(194)</sup>, or switched into foreign currencies when suitable opportunities occur.

(191)

$$\frac{\text{Consolidated Account expenditure at current prices}}{\text{G.D.P. at current prices}} = \frac{20,931}{106,000} \times 100 = 19.7\%$$

\$ mn

(192) See paragraph 100 above (and also paragraph 124 above).

(193)

	\$ mn	\$ mn
<i>Revenue:</i>		
<i>Recurrent</i>	15,843	—
<i>Capital</i>	7,737	23,580
<i>Expenditure:</i>		
<i>Recurrent</i>	12,022	—
<i>Capital</i>	<u>8,909</u>	<u>20,931</u>
<i>Surplus</i>	—	2,649(*)

Note: (\*) The difference of \$255 million between this surplus and the surplus on General Revenue Account of \$2,904 million is made up as follows:

	\$ mn
<i>Urban Council</i>	-206
<i>Housing Authority</i>	—
<i>Development Loan Fund</i>	+ 31
<i>Lotteries Fund</i>	—
<i>Home Ownership Fund</i>	-78
<i>Student Loan Fund</i>	<u>-2</u>
	<u>-255</u>

(194) But the present ceiling of \$7,000 million on borrowings by the Exchange Fund will have to be increased shortly.



*PART V: THE PUBLIC SECTOR AND THE ECONOMY IN THE 1980s**(1) Outlook for the General Revenue Account in the Forecast Period, 1981-82 to 1983-84*

216 That concludes, Sir, my presentation of the Draft Estimates of Expenditure for 1980-81 and the Revenue Estimates as amended by my revenue proposals. Despite my reservations about the distortions caused by the much higher level of capital expenditure, for three reasons I believe we are well placed to meet our commitments on General Revenue Account in the new three years forecast period, 1981-82 to 1983-84: *first*, the deficit on capital account is presently very small; *secondly*, we have substantial reserves of taxable capacity; and, *thirdly*, our 'free' fiscal reserves are well in excess of the guideline.

217 These commitments on General Revenue Account in the forecast period are, of course, considerable. To maintain the services envisaged in the Draft Estimates, and to expand them to meet demand at existing standards, recurrent expenditure *at 1980 prices* will increase from \$10,700 million in 1980-81 to over \$14,000 million by 1983-84, an average annual growth rate of more than 9%. If total expenditure is allowed to grow annually at the guideline rate of 10% (in real terms, of course, i.e. *at 1980 prices*), if total expansion is allowed to grow annually of the guideline rate of 10% then it could be as high as \$24,000 million *at 1980 prices* by 1983-84. If, in the forecast period, capital expenditure remains at its present (i.e. 1980-81) plateau of, say, \$7,500 million *at 1980 prices*, made up of, say, \$3,700 million for the two Public Works Programme components, \$500 million for land transactions, \$1,800 million for transfers to the Development Loan Fund for on-lending to the Housing Authority and \$1,500 million for the other eight components of the capital account, there might be room for additional expenditure of \$2,500 million on new services and capital works by 1983-84 *at 1980 prices*. Now as at 1 April 1984, I estimate that there will still be outstanding, *at 1980 prices*, about \$2,000 million worth of expenditure on projects presently in Category A of the Public Works Programme, and this figure becomes \$16,000 million if projects already in Category B are added in. So, whereas I remain doubtful of the continuing validity, in the 1980s, of Guideline (4), which sets a limit to recurrent expenditure as a proportion of total expenditure, clearly we face the prospect of having to make as much room as possible available for capital expenditure. Thus, if there is room for about \$2,500 million worth of additional expenditure by 1983-84<sup>(195)</sup> *at 1980 prices*, the way in which it is distributed between recurrent services and capital works will present us with some difficult decisions, and these decisions will be made even more difficult if, in the process of building up to a level of expenditure of the order of \$24,000 million *at 1980 prices* in 1983-84 we are,

---

(195) That is, \$24,000 million—\$14,000 million—\$7,500 million=\$2,500 million.

meanwhile, relatively short of recurrent revenue (as we may well be in the first two years of the forecast period). However, so far as I can see at the moment, total expenditure of this order could be contemplated, provided the growth rate of the economy does not deviate significantly from the trend growth rate experienced in the 1970s.

218 All this is *not* to say that such levels of expenditure on General Revenue Account, let alone on Consolidated Account, *will* be feasible in terms of what the economy can bear (and the events of the last few days have not made me more optimistic about the near-term prospects for the world economy). If the relative size of the public sector is enlarged too quickly, the growth rate of the economy and the maintenance of internal and external equilibrium will be prejudiced. This will be so, regardless of the acceptable secular trend of the relative size of the public sector and regardless of whether the economy is on an upswing or on a downswing.

219 Furthermore, all our planning to date has been based on the assumption of an average annual growth rate of the population of around 2%, made up of 1.2% by natural increase and the balance by net immigration. Should immigration continue at its present high rate, the growth rate of the population over the forecast period would be at least 4% and, as the productivity of immigrants is not initially as high as that of the existing labour force, the growth rate of real G.D.P. *per capita* would be less than it would otherwise be. At the same time, there would be an inevitable decline in the growth rate of the social wage received by the less well-off section of the community, as a result of public expenditure, and an inevitable strain on our infrastructural facilities<sup>(196)</sup>. All this would add to pressures for even higher levels of public expenditure, which might well be quite unacceptable.

(2) *Likely Developments in the Economy*

220 While it is difficult, as a consequence, to predict the state of our public finances over the forecast period, even within the disciplines set by our budgetary guidelines, modified or otherwise, the growth path of our economy in the 1980s is likely to be characterized by unusual uncertainties (and I have no doubt it will continue to be as full of surprises as in the 1970s).

221 But, despite all the uncertainties, five likely developments can be fairly easily discerned: *first*, the struggle against protectionism since the late 1950s has been remarkably successful in that derogations from our G.A.T.T. most-favoured-nation rights of access to our major markets have been virtually limited to our exports of textiles and clothing, but there are signs that the major industrialized countries may be moving towards an extension of protectionism to other products and towards a discriminatory application of restrictions as far as different suppliers are concerned. The extent to which the present line can be held will depend considerably on the willingness of

---

(196) *The provision of which is becoming increasingly costly anyway: see paragraph 34 above.*

the developing countries, and the so-called newly industrialized countries in particular, to liberalize access to *their* markets. With the end of the Tokyo round of multilateral trade negotiations, the major industrialized countries have probably reached the limit of the extent to which they can liberalize trade among themselves. It may be that they will increasingly use the protectionism now practised by many of the developing countries as an excuse for further limiting the access rights of all others to their markets.

222 Thus, *secondly*, the case for the Hong Kong economy to be more broadly based emerges, as has been recognized by the Advisory Committee on Diversification. The advice of Executive Council has just been sought on several of the eight main subject areas of the Advisory Committee's report; and we shall be seeking advice on the remainder by the end of next month. Those recommendations which are acceptable will be implemented as soon as possible thereafter. So we can expect the structure and product-pattern of our manufacturing industries to change over the coming decade, largely as a consequence of market forces, but assisted by the implementation of the Advisory Committee's recommendations. The change will not be dramatic. The scope for change is limited by our relative shortage of land<sup>(197)</sup>. It will need to be stimulated by an even greater stress on technical education, an area in which I would hope to see a greater involvement of public funds. But, as I pointed out earlier<sup>(198)</sup>, although the future growth momentum of our economy will depend in part on a greater technical capability and a greater degree of sophistication, one adverse consequence will be a reduction in the much-valued mobility of our labour force.

223 *Thirdly*, the financial services sector will continue to develop as a source of foreign exchange earnings in its own right and, as the Advisory Committee on Diversification recognized, Hong Kong will almost certainly remain the major international centre for, and in, the region. But this means we shall have to become more concerned with the ground rules within which the constituent markets operate: currently, the Secretary for Monetary Affairs and I are examining some of the provisions of the Banking Ordinance and the Deposit-taking Companies Ordinance in the light of present day needs and circumstances, including the internationalization of our banking industry. In accordance with the Advisory Committee's recommendation<sup>(199)</sup> and subject

---

(197) *The main effect of this constraint has been to keep the range of products manufactured in Hong Kong fairly narrow and to result in a concentration on light industry. This has not been entirely disadvantageous as a high degree of specialization can make for cost- efficiency. Where the production of components or supporting services for these industries involves land-intensive processes, they have generally had to be imported from overseas. So, the opportunities that now exist for Hong Kong firms to establish joint ventures in Guangdong may alleviate supply constraints of this sort. Supplies of components and services from sources which are both nearby, and partly under the control of Hong Kong firms, may improve both the competitiveness of Hong Kong's exports and the flexibility with which our manufacturers can respond to changing market conditions.*

(198) *See paragraph 31 above.*

(199) *Report (1979), paragraph 348.*

to the advice of Executive Council, the Secretary for Economic Services will be bringing forward, in due course, a bill for the prudential supervision of the insurance industry; and a substantial revision of the Companies Ordinance is also in hand. More immediately, I shall be seeking the advice of Executive Council on the question of disclosure of shareholdings by directors, on fringe dealings in gold, on a gold futures market, on a bill to unify the stock exchanges, and, on a bill to collect statistics for monetary policy purposes<sup>(200)</sup>. The fact is, on this last point, the fact is that our efforts, to develop a comprehensive understanding of the relationships between the monetary and other economic aggregates are being hampered by the inadequacy of the monetary statistics presently available to us. The statistics we now use are collected for prudential purposes. They are not necessarily suitable for analytical purposes. For example, available statistics for loans and advances in Hong Kong relate to loans to customers where the credit received lies in Hong Kong, but a significant proportion of these loans is in fact for use outside Hong Kong and so has no direct impact on our economy.

224 *Fourthly*, the increasing importance of Hong Kong as a regional, and international, financial centre is likely to increase the volume of capital flows across our exchanges, particularly when times are turbulent. Thus, the exchange rate of the Hong Kong dollar will be even more vulnerable to movements not necessarily either reflecting events within Hong Kong or in the interests of the economy as a whole. To the extent that our present floating exchange rate regime leads, from time to time, to an expansion of credit disproportionate to the economy's ability to absorb it, awkward questions of monetary management arise (and the Hong Kong Government is not the only government which finds them awkward although, so far, we have managed to avoid dangerous experiments).

225 In this connection, I have recently been considering the position of the Exchange Banks' Association. I believe that an association comprising all the licensed banks in Hong Kong has a very important part to play in our monetary system, but I am not certain that the present arrangements are totally satisfactory. Specifically, there is no requirement for every licensed bank to belong to the Association, and the existing committee is too small to be fully representative of what is now a very diverse banking industry. I am, therefore, considering a proposal to incorporate the Exchange Banks' Association by statute, and to require, by one means or another, every bank licensed under the Banking Ordinance to be a member of the Association. At the same time, the membership of the committee of the Association would have to be enlarged to make it more broadly-based.

226 I should be distressed if these thoughts about the position of the Exchange Banks' Association were taken as any form of criticism of the chairman and members of the present committee, or their predecessors.

---

(200) See paragraph 44 in Appendix I.

Indeed, I have every reason to be most appreciative of the support they have given the Government in recent years, which support has placed them, on occasions, in a rather difficult position.

227 I would also welcome the establishment of a convenient channel for communication between the Government and deposit-taking companies in the 1980s: at present, some companies are grouped in two associations, but there is no single association representing all companies. It is not for me to dictate on this matter, but I can see some positive advantages in an umbrella association comprising all the companies on the deposit-taking companies register<sup>(201)</sup>.

228 This brings me, conveniently, back to the question of the determination of interest rates: at present the interest rate agreement of the Exchange Banks' Association sets the maximum levels of certain deposit rates which may be offered by members of the Association. Changes in these levels are decided by the interest rate agreement working committee of the Association, in consultation with the Government. It is at least questionable whether the terms of the present interest rate agreement, together with the absence of any form of control over the deposit rates that may be offered by deposit-taking companies, are suited to present day needs and circumstances. I make this point in the Hong Kong context, that is to say, where the Government does not directly influence the level of interest rates in the money markets<sup>(202)</sup>. I doubt whether present arrangements are sufficiently comprehensive for the increasingly complex market place of the 1980s. If all this is thought to amount to a hint that I consider the Government should exert a direct influence over money market interest rates, let me hasten to *insist* that one thing I am *not* thinking of is the possible issue of treasury bills or similar Government paper.

229 *Fifthly*, the expansion of China's international trade in order to help finance the 'four modernizations' programme seems likely further to benefit Hong Kong in terms of the demands that will be made upon our financial and mercantile services<sup>(203)</sup>. The provision of any necessary facilities in Hong Kong to cope with these demands will constitute a further diversification of our economy and should make it less vulnerable to downturns in particular trades. Thus, wherever feasible, infrastructural developments in Hong Kong should be compatible with the trade flows to, and from, China through Hong Kong.

---

(201) *Both the Exchange Banks' Association and a deposit-taking companies association would have, of course, roles which would be complementary to, and not competitive with, the Banking Advisory Committee and the Deposit-taking Companies Advisory Committee.*

(202) *Taking these to cover transactions between banks, between deposit-taking companies, and between banks and deposit-taking companies.*

(203) *It is inevitable that, in meeting these demands (and the demands of our fast growing entrepot trade generally), the volume of loans and advances in Hong Kong recorded in our monetary statistics will increase and, whilst they will be loans and advances used in Hong Kong (contrast the point made at the end of paragraph 43 in Appendix I), their impact on the Hong Kong economy can only be beneficial.*

*CONCLUSION*

230 On that brief glimpse into the future, I now move, Sir, that the debate on this motion be adjourned.

*Debate adjourned pursuant to Standing Order 54(2).*

**Adjournment and next sitting**

HIS EXCELLENCY THE PRESIDENT:—In accordance with Standing Orders I now adjourn the Council until 2.30 p.m. on Wednesday 12 March.

*Adjourned accordingly at seven minutes to six o'clock.*

*APPENDIX I**Paragraphs 17-44 of the printed version of the Budget Speech 1980**(ii) Total final demand<sup>(15)</sup> and the G.D.P.*

17 Looking first at aggregate demand and supply: in the long run, the growth rate of demand for the output of the economy has to be broadly consistent with the growth rate of the ability of the economy to produce that output. So, the average annual growth rate of total final demand over the ten years 1970 to 1979 was 9.5%, which is roughly equal to that of G.D.P. at 9% but, because of this difference, the growth rate of imports was slightly higher, at 10%. But, for individual years within the decade, the growth rates of total final demand and of G.D.P. were, more often than not, out of line with each other. Although circumstances in particular years differed, it seems that, after a year in which there is a strong export-led upswing in the economy, there is a tendency for the growth rate of total final demand to exceed that of G.D.P. in the subsequent two years. Incidentally, the discrepancy between the growth rates of total final demand and of G.D.P. in individual years was wider prior to the floating of the Hong Kong dollar in November 1974 than in subsequent years, the exception being 1978<sup>(16)</sup>.

---

(15) *That is, private consumption expenditure + Government consumption expenditure + gross domestic fixed capital formation + increase in stocks + exports of goods + net exports of services. Net exports of services has to be used instead of exports of services because separate statistics of imports and of exports of services are not available prior to 1978. The resultant distortion is believed to be small, particularly as some invisible trade involves parallel transactions, although not necessarily of the same order of magnitude (e.g. the import of shipping services and the servicing of ships passing through Hong Kong, which constitute the export of a service).*

(16) *See also paragraph 62, B.S. 1980.*

(iii) *Domestic demand<sup>(17)</sup> and domestic exports of goods*

18 Turning now to the relationship between the growth rates of several components of total final demand: the average annual growth rate of domestic demand over the decade was 10.2%, whereas the growth rate of domestic exports of goods was (only) 8.4%<sup>(18)</sup>. Statistically, this difference is largely a reflection of a high growth rate of fixed investment at 13.3%.

19 Shifts in the relationship between the growth rates of domestic demand and of domestic exports of goods were reflected in differences in the growth rates of the employed labour force and of employment in manufacturing. Thus, in the first post-recession year, when the growth rate of domestic exports of goods at 29.5% was significantly higher than that of domestic demand at 15.2%, the growth rate of employment in manufacturing was 24%, whilst that of the employed labour force was 1.6%<sup>(19)</sup>. In 1977 and 1978, when the growth rates of domestic demand at 14.4% and 16.3% respectively were higher than the growth rates of domestic exports of goods at 4.8% and 10.4%, the growth rate of employment in manufacturing, taken over these two years, was only 1.6%, while that of the employed labour force was 9.5%. In 1979, when the growth rate of domestic exports of goods at 16.6% was higher than that of domestic demand at 8.6%, the growth rate of employment in manufacturing was 11.2%, while that of the employed labour force was 5.8%. All this illustrates the mobility of our labour force and helps to explain why there was virtual full employment in the four post-recession years, despite marked changes in the growth rates of the several components of total final demand.

(iv) *Public sector demand<sup>(20)</sup> versus private sector demand<sup>(21)</sup>*

20 Within domestic demand, the average annual growth rate of demand by the public sector over the decade was 12%. This is significantly higher than the growth rate of demand by the private sector at 10%.

21 Thus, the public sector was commanding an increasing share of available resources. In 1970, the relative share of the public sector, as measured by

(17) *That is, private consumption expenditure + Government consumption expenditure + gross domestic fixed capital formation + increase in stocks.*

(18) *Ideally, the relationship analysed should be between the growth rate of domestic demand for domestically produced goods and the growth rate of domestic exports of goods plus exports of services, but statistics are not available.*

(19) *For convenience, statistics of the employed labour force and employment in manufacturing in September of each year were used as the basis for these calculations.*

(20) *That is, in national accounts terms, Government consumption expenditure + gross domestic fixed capital formation by the Government and the Mass Transit Railway Corporation.*

(21) *That is, private consumption expenditure + gross domestic fixed capital formation by the private sector + increase in stocks.*

the ratio of public sector demand to the G.D.P. at current prices was 8%<sup>(22)</sup>. It drifted up to 8.7% in 1973 and then jumped to 10.4% as the economy moved into recession in 1974. When the economy recovered in 1976, it declined a little to 9.5%, but increased again to 11.1% in 1977 and to 12.7% in 1978, despite the fact that the upswing phase was sustained.

22 Despite our efforts in 1979-80 to slow down the growth rate of public expenditure (on General Revenue Account), the extraordinary demands on capital account, which could not have been foreseen when the budget was prepared, have resulted in the relative share of the public sector increasing further to 13.5%. It would have increased even further, but for the faster than expected growth rate of the economy.

(v) *Demand for the output of the building and construction industry*

23 Focussing in particular on demand for the output of the building and construction industry, the average annual growth rate of demand by the public sector over the decade was 15.9%, very much higher than that by the private sector at 10.8%<sup>(23)</sup>. So the public sector's share of the output of the building and construction industry increased sharply over the decade. It was only 26% in 1970, but it reached 49% in 1978, easing back, however, to 47% in 1979. The public sector's demand for the output of the building and construction industry is now such that the Government's capital works programmes have a significant effect on the prices charged by the industry and these prices, and the prices the industry pays for its labour, will influence prices in the rest of the economy.

(vi) *Private consumption expenditure and real income*

24 As regards the largest component of domestic demand, namely, private consumption expenditure, the average annual growth rate over the decade was 9.6%, which was roughly equal to the growth rate of real income at

---

(22)	<i>Public sector demand at current prices (\$ mn)</i>	<i>G.D.P. at current prices (\$ mn)</i>	<i>(1) as % of (2)</i>
	<i>(1)</i>	<i>(2)</i>	
1970	1,540	19,214	8.0
1971	1,799	21,873	8.2
1972	2,220	25,854	8.6
1973	2,969	33,964	8.7
1974	4,052	38,786	10.4
1975	4,249	40,574	10.5
1976	4,942	51,973	9.5
1977	6,605	59,429	11.1
1978	8,797	69,174	12.7
1979	11,800	87,345	13.5

(23) *The extent to which the growth rate of public sector demand on building and construction is higher than the growth rate of private sector demand depends very much on the choice of period because there were wide variations in the growth rates. Taking, for example, the 9-year period 1971 to 1979, the average annual growth rate of public sector demand on building and construction was 21%, while that of private sector demand was 9%.*



9.5%, suggesting that the average propensity to consume of the population remained constant over time. In general, the growth rate of private consumption expenditure was slower than the growth rate of real income when the economy was in the early phase of an upswing and was faster when the economy was in the mature phase<sup>(24)</sup>.

(vii) *Imports and total exports of goods*

25 As regards the external sector, the average annual growth rate of imports (in real terms, of course) over the decade was 10%, slightly faster than that of total exports of goods at 9.4%, but this difference is immaterial<sup>(25)</sup>.

26 Over the decade there appears to have been a relationship between the growth rate of imports and the growth rate of total exports of goods, such that the one has not exceeded the other for more than two years at a time<sup>(26)</sup>. This is indication of the speed with which the economy adjusts to imbalance in the visible trade account.

27 Under the fixed exchange rate regime, the growth rate of imports was faster than that of total exports in each of the two years 1970 and 1971 and *vice versa* for the following three years. By contrast, under the floating exchange rate regime, a shift of this sort has occurred in every year except 1978. Notwithstanding the fact that the economic circumstances facing Hong Kong before and after the floating of the Hong Kong dollar were different, this suggests that the adjustment mechanism, at least in terms of the external balance, has been more efficient under the floating exchange rate regime.

---

(24) *The average annual growth rate of private consumption expenditure displayed a pattern in the 1970s which suggested that, in a particular year, it bore a statistical relationship with the growth rate of real income in that year and in the previous year, the current year having a relatively greater influence. For example, in the three years 1974 to 1976, the average annual growth rate of private consumption expenditure was only 3.2%, compared with 7.3% for real income. In the subsequent three years 1977 to 1979, the growth rate of private consumption expenditure was 14.4%, compared with 9.7% for real income. But, occasionally, there were deviations from the pattern as consumer behaviour was affected by a wealth effect arising from significant variations in the value of such assets as property, and stocks and shares.*

(25) *The reason is that the growth rates of imports and total exports of goods differed greatly for individual years and so comparisons over time are affected by the choice of the period.*

(26) *Growth rates in real terms of:*

	<i>Total exports of goods (%)</i>	<i>Imports of goods (%)</i>
<i>1970</i>	<i>8.4</i>	<i>13.6</i>
<i>1971</i>	<i>6.5</i>	<i>13.6</i>
<i>1972</i>	<i>6.8</i>	<i>3.5</i>
<i>1973</i>	<i>12.3</i>	<i>10.7</i>
<i>1974</i>	<i>-6.3</i>	<i>-10.3</i>
<i>1975</i>	<i>3.2</i>	<i>3.8</i>
<i>1976</i>	<i>28.0</i>	<i>24.8</i>
<i>1977</i>	<i>5.1</i>	<i>7.9</i>
<i>1978</i>	<i>13.8</i>	<i>21.5</i>
<i>1979</i>	<i>19.5</i>	<i>15.6</i>

(viii) *External trade account and the exchange rate*

28 Shifts in recent years in the visible trade 'gap'<sup>(27)</sup> also reflected the influence of the floating of the Hong Kong dollar although, when the shift in the terms of trade was sharply adverse<sup>(28)</sup>, as was the case in 1974, the visible trade 'gap' could widen despite the fact that the growth rate in real terms of total exports was more rapid than that of imports.

29 Furthermore, exchange rate movements since the floating of the Hong Kong dollar in 1974 (or since the break with sterling in 1972, for that matter) were remarkably in line with the external trade account, the incidence of actual payments notwithstanding, particularly when our new estimates of the invisible trade balance are combined with the visible trade balance to produce an overall visible and invisible trade balance<sup>(29)</sup>. In the last two years, when the exchange rate depreciated, the external trade account was in deficit, but

(27) *Visible trade 'gap', that is, the proportion of the value of imports of goods not covered by the value of total exports of goods:*

<i>Year</i>	<i>Adjusted(*)</i> (%)	<i>Unadjusted</i> (%)
1970	13.6	13.5
1971	15.4	15.3
1972	11.0	10.9
1973	10.5	10.4
1974	12.0	12.0
1975	11.0	10.9
1976	4.5	4.0
1977	8.1	7.9
1978	14.8	14.5
1979	12.1	11.5

Note: (\*) *The data for the value of imports used in the calculation has been adjusted to take account of imports of water and an estimate of imports of gold for industrial and commercial use.*

(28) *See f.n. (10), B.S. 1980.*

<i>(29)</i>	<i>Visible trade balance(*)</i> (\$ mn)	<i>Invisible trade balance</i> (\$ mn)	<i>Visible and invisible balance</i> (\$ mn)	<i>Movements of the Hong Kong dollar(***)</i> (%)
1970	-2,397	3,427	1,030	N.A.
1971	-3,123	3,367	244	N.A.
1972	-2,388	3,818	1,430	N.A.
1973	-3,050	4,316	1,266	2.0
1974	-4,106	4,817	711	3.6
1975	-3,699	4,619	920	1.7
1976	-1,963	6,355	4,392	3.8
1977	-3,963	6,059	2,096	2.2
1978	-9,356	7,298	-2,058	-10.7
1979	-10,503	10,018(**)	-485	-8.4

Notes: (\*) *Adjusted for imports of water and of gold for industrial and commercial use.*

(\*\*) *Preliminary estimate.*

(\*\*\*) *Calculated by comparing the daily average of the trade weighted exchange rate index for a particular year with that of the previous year. A negative sign (—) denotes depreciation.*

much less so in 1979 than in 1978. In the previous five years, 1973 to 1977, when the exchange rate appreciated, the account was in surplus, as it was also in the first three years of the decade when the Hong Kong dollar was tied to sterling.

(ix) *Pressure of demand on domestic resources and inflation*

30 Corresponding to these shifts in the external balance, there were shifts in the internal balance, that is to say, in the balance between the demand for, and supply of, domestic resources of land, labour and capital<sup>(30)</sup>, with consequences for prices, particularly the prices of goods and services which are largely determined by domestic demand and supply, such as real estate. Together with changes in the rate of increase of world prices of imported goods and services, over which we have no control, such shifts in the internal balance were the main influence on the internal price level over the decade. The other influence was the exchange value of the Hong Kong dollar.

31 At the beginning of the decade, the growth rate of total final demand was higher than that of G.D.P. This reflected a rapid growth rate of private consumption expenditure, presumably reacting to the rapid growth rate of incomes generated by the rapid expansion in world trade and, therefore, in Hong Kong's domestic exports in the late 1960s. Resources were fully employed, as indicated by an unemployment rate of only just over 4% in 1971, notwithstanding the fact that the growth rate of domestic exports slowed down rather sharply and the growth rate of world trade declined<sup>(31)</sup>. During 1970 and 1971, wage rates were increasing rapidly<sup>(32)</sup> for the pressure of

(30) *A convenient, but rather imprecise, indicator of the shifts in the balance between demand for, and supply of, domestic resources is provided by changes in the ratio of total final demand to the G.D.P. The measure is imprecise because, inter alia, the growth rate of re-exports, which fluctuated rather widely during the decade, has a disproportionately large influence on the ratio. Nevertheless, such a measure does show the direction in which the balance (or imbalance) between the demand for, and supply of, resources was shifting:*

*Ratio of total final demand to G.D.P. (both at constant prices):*

	<i>Unadjusted</i>	<i>Adjusted to exclude</i>
	<i>(%)</i>	<i>re-exports</i>
		<i>(%)</i>
1970	188.1	173.6
1971	195.3	179.3
1972	189.9	172.8
1973	185.5	166.3
1974	175.4	159.7
1975	176.5	160.6
1976	180.3	163.9
1977	179.0	163.1
1978	187.2	169.0
1979	190.4	169.4

(31) *The growth rate of domestic exports slowed down from 9.5% in 1970 to 4.3% in 1971 as the growth rate of world exports slowed down from 8.7% in 1970 to 6.0% in 1971.*

(32) *Wage rates of manufacturing workers, for example, increased during the two twelve months periods ending September 1970 and September 1971 by 18% and 16% respectively.*

demand was such that the cost/price structure as measured by the G.D.P. deflator<sup>(33)</sup> was inflating. As the slow down in the growth rate of world trade was felt, this pressure eased off. At the same time, however, the rate of increase in consumer prices was relatively low<sup>(33)</sup>, reflecting the fact that domestically generated inflation was higher than imported inflation.

32 In 1973 and 1974, the world economy moved into recession leading to a lessening of the pressure of demand on domestic resources, because the demand for Hong Kong's exports slackened. However, rapidly rising world prices led to imported inflation replacing domestically generated inflation. Thus, the rate of increase in consumer prices was significantly higher than that of the G.D.P. deflator<sup>(33)</sup>, because import prices were increasing significantly faster than export prices.

33 As the world economy began to recover from the recession, demand for Hong Kong's exports picked up and, with it, the demand for domestic resources, as evidenced by the rapid fall in the unemployment rate<sup>(34)</sup>. So, again, the domestic cost/price structure started to inflate. This was reflected in a rate of increase in the G.D.P. deflator higher than that of consumer prices in 1975 and 1976. But these rates of increase were low compared with those of the early 1970s. The fact that the Hong Kong dollar was floating, and was appreciating<sup>(35)</sup>, contributed to this relative price stability.

34 The pressure of demand on domestic resources was sustained in 1977. Although the growth rate of domestic exports slowed down dramatically, the growth rate of total final demand was still sufficient to induce a further

---

(33) Rates of increase in:

	<i>G.D.P. deflator</i>	<i>Consumer prices</i>
	(%)	(%)
1970	11.1	7.1
1971	8.4	3.4
1972	7.8	6.1
1973	12.9	18.2
1974	12.2	14.4
1975	2.3	1.2
1976	7.8	4.0
1977	4.1	5.5
1978	5.8	5.8
1979	13.3	11.6

(34) Unemployment rate:

	(%)
September 1975	9.1
March 1976	5.6
September 1976	4.6
March 1977	4.5
September 1977	4.1
March 1978	3.0
September 1978	2.7
March 1979	2.3
September 1979	3.4

(35) See f.n. (29) above.

small fall in the unemployment rate. So, in that year, the rate of increase in consumer prices was higher than that of the G.D.P. deflator. Again, both these rates of increase were low because the Hong Kong dollar was still appreciating.

35 In 1978, however, the rapid growth rate of domestic demand, coupled with a recovery in the growth rate of domestic exports in the second half of the year, were such that the pressure of demand on domestic resources increased further and the unemployment rate declined more steeply. This pressure of excess demand resulted in the exchange value of the Hong Kong dollar depreciating and caused the rate of increase in import prices to accelerate; thus the adjustment mechanism began to correct the imbalance. But, to some extent, the operation of the adjustment mechanism was being frustrated by the very rapid growth rate of credit creation<sup>(36)</sup>. So, towards the end of the year, notwithstanding the fact that the rate at which prices increased for the year as a whole was still comparatively low, there was a very real threat of a serious inflationary situation developing, both domestically generated and imported.

36 This threat became a reality in the first half of 1979 largely for three reasons: a higher than expected rate of world inflation<sup>(37)</sup>; a depreciating Hong Kong dollar<sup>(38)</sup>; and a worsening imbalance between the supply of, and demand for, property. The unemployment rate remained at its historically low level of under 3%. The rates of increase in both the G.D.P. deflator and consumer prices accelerated to levels well above the trend rates of increase for the decade as a whole of 8.5% and 7.6% respectively<sup>(39)</sup>. But I shall have more to say later on about the state of our economy as we move from the last year of the decade of the 1970s into the first year of the 1980s.

---

(36) See paragraph 65, B.S. 1980.

(37) World inflation was fed into the Hong Kong economy via import prices and export prices, the latter rising in response to buoyant demand generally for Hong Kong products, and particularly in Germany, the U.K. and Japan.

(38) Trade weighted exchange rate of the Hong Kong dollar (18 December 1971=100):

End	1977	1978	1979
January	115.4	107.0	95.6
February	115.0	105.2	94.8
March	114.5	103.8	92.6
April	114.0	104.6	92.9
May	113.1	104.0	92.0
June	112.3	101.6	90.2
July	112.2	98.6	88.0
August	112.8	96.7	90.1
September	111.8	95.3	90.6
October	108.6	90.7	92.8
November	108.6	95.1	93.3
December	106.6	93.2	92.7

(39) Derived from the annual increases in the table in f.n. (33) above. See also Annex (1).

(x) *Monetary aggregates*

37 Over the decade, the relationship between the growth rate of the money supply and the rate of increase in prices shifted. Before the floating of the Hong Kong dollar in November 1974, the adjustment mechanism operated through changes in the money supply. Whenever the growth rate of the money supply exceeded that of G.D.P. in money terms, the rate of increase in prices as measured by the G.D.P. deflator was higher than that of consumer prices. In other words, the domestic cost/price structure inflated at a rate more rapid than the rate of imported inflation<sup>(40)</sup>. By contrast, when the growth rate of the money supply was slower than that of G.D.P. in money terms, price increases were imported rather than domestically generated.

38 Since the floating of the Hong Kong dollar, the role of the money supply in the adjustment mechanism has become obscured. Certainly, the relationship between the growth rate of the money supply, the growth rate of G.D.P. in money terms and the rate of increase in prices appears to have changed, although this did not become clear until 1976. Since then, the average annual growth rate of M2 at 25.4% has been substantially above that of G.D.P. at 18.9%.

39 There are four apparent reasons for this divergence of the two growth rates: *first*, the loss of the automatic control on the growth rate of the money supply consequent on the floating of the Hong Kong dollar.

40 *Secondly*, the growth rate of domestic demand in 1977 and 1978 at 14.4% and 16.3% respectively was a more important determinant of the growth rate of G.D.P. than the growth rate of total exports of goods at 5.1% and 13.8% respectively. So, as domestic activities rely more heavily on local bank credit than do export activities, outstanding bank loans and advances in Hong Kong as a proportion of the money supply increased from 63% at the end of 1977, to 72% at the end of 1978, and then to 77% at the end of 1979, compared with 61% only at the end of 1976. At the end of 1977, the net holdings of foreign currency assets by the banks were

(40)	Growth rate of:		Ratio between rate of increase in G.D.P. deflator and rate of increase in consumer prices
	M2(*) (%)	G.D.P. in money terms (%)	
1970	20.8	18.1	1.6
1971	24.4	13.8	2.5
1972	28.9	18.2	1.3
1973	6.6	31.4	0.7
1974	16.6	14.2	0.8
1975	16.9	4.6	1.9
1976	21.0	28.1	2.0
1977	20.7	14.3	0.7
1978	25.6	16.4	1.0
1979	29.8	26.3	1.1

Note: (\*) Old series.

equivalent to 30% of the money supply, compared with 22% at the end of 1978 and 23% at the end of 1979<sup>(41)</sup>.

41 *Thirdly*, at the same time, the demand for credit grew along with rising land prices and construction costs, a recovery of turnover and prices on the stock market<sup>(42)</sup>, and a delay in adjusting interest rates upwards in response to interest rates elsewhere and having regard to macro-economic considerations. Thus, the growth rate of bank loans and advances in Hong Kong was 43% in 1978 and 40% in 1979, compared with 18% only in 1976<sup>(43)</sup>.

42 *Fourthly*, the rapid expansion in recent years in the number of deposit-taking companies, and their growing importance as a source of funds for banks, has meant that the growth rate of the money supply, as measured by M2 on its old definition, has been artificially inflated, thus distorting it as a measure of the true situation. And, incidentally, it was this, rather than a childish wish to obscure an embarrassing set of statistics, that caused us to introduce the new definition of M2<sup>(44)</sup> consequent upon the introduction of minimum liquidity requirements for deposit-taking companies.

(41) *Determinants of the money supply (M2) (old series):*

	<i>End 1976</i>	<i>End 1978</i>	<i>End 1979</i>
	(\$ mn)	(\$ mn)	(\$ mn)
<i>Bank loans and advances in Hong Kong</i>	29,480	52,814	73,690
<i>Banks' net holdings of foreign currency assets</i>	15,009	16,167	21,945
<i>Notes and coins in circulation</i>	5,177	7,775	8,784
<i>Banks' net holdings of other assets</i>	- 1,253	- 3,350	- 9,116
<i>Total</i>	<u>48,413</u>	<u>73,406</u>	<u>95,303</u>

(42) *The Hang Seng Index increased from 404 at the end of 1977 to a high of 708 at 4 September 1978 and, after falling to a low of 494 at 2 January 1979, it increased to 879 at the end of 1979. It is worth noting that the growth rate of M2 in 1972, at 29%, exceeded the growth rate of G.D.P. in money terms, at 18% (the Hang Seng Index having risen from 341 at the end of 1971 to 843 at the end of 1972). However, the growth rate of M2 in 1973, at 7%, was less than the growth rate of G.D.P. in money terms at 31% (the Hang Seng Index having fallen to 434 at the end of 1973, after peaking at 1,775 at 9 March 1973).*

(43) *These growth rates are based on aggregates of bank loans and advances using the old definition. Rough estimates of the growth rate of bank loans and advances in Hong Kong to customers other than D.T.Cs. are as follows:*

	(%)
<i>1976</i>	16
<i>1977</i>	23
<i>1978</i>	41
<i>1979</i>	34 (actual)

(44) *The calculations of the money supply on the narrower definitions (M1 and M2) and of bank loans and advances in Hong Kong, have been revised back to December 1978 to eliminate growing distortions caused by transactions between licensed banks and registered deposit-taking companies. The new definitions are as follows:*

*M1—Legal tender notes and coins in the hands of the non-bank and non-deposit-taking company public; plus demand deposits (other than from banks and deposit-taking companies) with licensed banks.*

*M2—M1 plus savings and time deposits (other than from banks and deposit-taking companies) with licensed banks.*

*M3—M2 plus deposits from the non-bank and non-deposit-taking company public with registered deposit-taking companies.*

*Bank loans and advances in Hong Kong—Loans and advances to customers in Hong Kong (other than banks and deposit-taking companies) by licensed banks.*

43 Although I have been able to suggest some reasons for the present relationship between the growth rate of the money supply and that of G.D.P. in money terms, our efforts to develop a comprehensive understanding of the relationships between the monetary and other economic aggregates are being hampered by the inadequacy of the monetary statistics presently available to us. The statistics we now use are collected for prudential purposes by the Commissioner of Banking and the Commissioner of Deposit-taking Companies. This means that they are not necessarily suitable for the purpose of economic analysis. For example, available statistics for loans and advances in Hong Kong relate to loans to customers where the credit risk lies in Hong Kong, but a significant proportion of these loans is in fact for use outside Hong Kong and so has no direct impact on our economy<sup>(45)</sup>.

44 To remedy this situation, I shall shortly be seeking Executive Council's advice on a bill designed to empower the Secretary for Monetary Affairs to collect monetary statistics required to fill the gaps in our knowledge. This proposal has already received the support of the Banking Advisory Committee and the Deposit-taking Companies Advisory Committee and is in line with a recommendation of the Advisory Committee on Diversification<sup>(46)</sup>.

## APPENDIX II

### *Paragraphs 86-121 of the printed version of the Budget Speech 1980*

#### *(b) The public sector and the economy*

##### *(i) Growth*

86 As I said earlier, in Government accounting terms, the public sector in Hong Kong may be defined with reference to the Consolidated Account, that is to say, all expenditure financed from public funds, irrespective of who incurred the expenditure<sup>(94)</sup>. It is the growth rate, in real terms, of public sector expenditure so defined that must be kept in line with the growth rate of the economy as measured by the growth rate of G.D.P. in real terms. The Government, therefore, exercises a considerable degree of influence over the growth rate of public sector demand in national accounts terms (which includes the M.T.R.C.).

87 Over the ten years 1970-71 to 1979-80, the average annual growth rate of expenditure on Consolidated Account in real terms was 11.2% and of

---

(45) *A recent survey of all banks in Hong Kong shows that at the end of 1979, about 10% of their loans in Hong Kong to customers other than deposit-taking companies could be identified as for use overseas. This component increased in the second half of 1979 at a rate significantly faster than that of loans identified as for use in Hong Kong.*

(46) *Report (1979), paragraph 343.*

(94) *See f.n. (34), B.S. 1980.*



G.D.P. it was 9%<sup>(95)</sup>. The growth rate of expenditure accelerated from 2.3% in 1970-71 to 20.7% in 1972-73, with the growth rate of G.D.P. averaging 5.6% in the first two years and then accelerating to 9.7% in 1972. The growth rate of expenditure then stabilized at rather more than 14% in each of the following two years, 1973-74 and 1974-75, with the growth rate of G.D.P. accelerating further to 16.4% in 1973, and then falling away sharply to 1.8% and 2.2% in the recession years 1974 and 1975.

88 The growth rate of expenditure on Consolidated Account was reduced to 0.6% in 1975-76, recovering to 4.5% in 1976-77. It then accelerated to 18.5% and 21.7% in the next two years, but was eased back to 10.7% in 1979-80. After the recession years, the growth rate of G.D.P. moved away fast to 18.8% in 1976 and averaged 10.4% in the following three post-recession years.

89 By way of a slight digression, I should mention here that, in recent years, I developed the concept of a steady progression guideline for expenditure in real terms on General Revenue Account, which, remember, is usually around 90% of expenditure on Consolidated Account. I believed we could allow the relative size of the public sector *as a whole* (i.e. on Consolidated Account) to increase over time in response to the enlargement of the economy without running any serious risk of crowding out the private sector. I set this guideline rate at 10%, that is to say, a little above the trend growth rate of G.D.P. This rate also seemed to be consistent with what was practicable having regard to the many constraints on public sector type expenditure, such as the decision-making process itself, planning disputes, recruitment of staff, land resumptions and so on; and it seemed to be consistent also with the need to secure value for money.

90 I recognized, of course, that this essentially *target* rate might well have to be lower in some years, but it could be higher in others. However, taking one year with another, the aim was to achieve a growth rate of 10%. Over

(95)

	<i>Growth rates in real terms:</i>	
	<i>C.A. expenditure</i>	<i>G.D.P.</i>
	(%)	(%)
<i>1970-71/1970</i>	<i>2.3</i>	<i>6.2</i>
<i>1971-72/1971</i>	<i>7.1</i>	<i>5.0</i>
<i>1972-73/1972</i>	<i>20.7</i>	<i>9.7</i>
<i>1973-74/1973</i>	<i>14.2</i>	<i>16.4</i>
<i>1974-75/1974</i>	<i>14.3</i>	<i>1.8</i>
<i>1975-76/1975</i>	<i>0.6</i>	<i>2.2</i>
<i>1976-77/1976</i>	<i>4.5</i>	<i>18.8</i>
<i>1977-78/1977</i>	<i>18.5</i>	<i>9.8</i>
<i>1978-79/1978</i>	<i>21.7</i>	<i>10.0</i>
<i>1979-80/1979</i>	<i>10.7</i>	<i>11.5</i>

the ten years, 1970-71 to 1979-80<sup>(96)</sup>, the average annual growth rate was, in fact, 10.7%. Only in the first two years of the decade, 1970-71 and 1971-72, in the recession year, 1975-76, in the first post-recession year, 1976-77 (when we had difficulty gearing up again after the recession) and in the year in which inflationary pressure beset us, 1979-80, was the growth rate below the target (*albeit* well below it in 1975-76 and 1976-77). In 1972-73, the growth rate jumped to 20%, eased back to 15.2% and 12.3% respectively in the following two years, and then surged again in 1977-78 and 1978-79 to 17.9% and 24.2% respectively, as we sought to make up for time lost during the recession.

(ii) *Relative size of the public sector*

91 So, in response to these different growth rates of public sector expenditure and G.D.P., the relative size of the public sector, defined as the ratio of expenditure on Consolidated Account to the G.D.P., both at current prices, drifted upwards over the decade from 13% in 1970-71 to 18.7% by 1979-80<sup>(97)</sup>. In other words, the relative size of the public sector increased by rather more than 2/5ths over the decade. But I believe this increase is within the capability of our enlarged and more sophisticated economy.

92 It is not really possible to set an upper limit to the relative size of the public sector but, clearly, the implications of sharp increases or decreases need to be carefully considered. Needless to say, the acceptable relative size of the public sector is larger on the downswing phase of the trade cycle

(96)	Growth rates in real terms:	
	G.R.A. expenditure (%)	G.D.P. (%)
1970-71/1970	2.3	6.2
1971-72/1971	7.3	5.0
1972-73/1972	20.0	9.7
1973-74/1973	15.2	16.4
1974-75/1974	12.3	1.8
1975-76/1975	2.3	2.2
1976-77/1976	1.8	18.8
1977-78/1977	17.9	9.8
1978-79/1978	24.2	10.0
1979-80/1979	6.9	11.5

(97)	At current prices:		
	C.A. expenditure (\$ mn) (1)	G.D.P. (\$ mn) (2)	(1) as % of (2)
1970-71/1970	2,504	19,214	13.0
1971-72/1971	2,952	21,873	13.5
1972-73/1972	3,875	25,854	15.0
1973-74/1973	5,048	33,964	14.9
1974-75/1974	6,610	38,786	17.0
1975-76/1975	6,565	40,574	16.2
1976-77/1976	7,348	51,973	14.1
1977-78/1977	9,166	59,429	15.4
1978-79/1978	12,068	69,174	17.4
1979-80/1979	16,200	87,345	18.7

than on the upswing (and it increased from an average of 14.1% in the four pre-recession years to 16.6% in the two recession years). It may increase again as the upswing phase matures (as it certainly did in the last two years of the decade, to an average of 18%). But, as a general rule, when the economy is enjoying strong growth, the relative size of the public sector should fall. It will tend to do so of its own accord, because the growth rate of public expenditure tends, initially, to lag behind the economy on the upswing (as it did in 1976 and so the relative size of the public sector fell from 16.2% in 1975 to 14.1% in 1976); and, anyway, apart from the desirability of having some room for the public sector to expand relative to the economy on the downswing, it is difficult to trim back the growth rate of public expenditure on the downswing in line with the growth rate of the economy (as was the case in 1974-75, when the relative size of the public sector jumped from 14.9% in 1973 to 17% in 1974).

(c) *Pattern of public expenditure*<sup>(98)</sup>

93 The best way of assessing the pattern of public expenditure over the past decade is to analyse expenditure on Consolidated Account at current prices.

94 On this basis, total expenditure in 1970-71 was \$2,504 million, of which \$1,915 million or 76%, was on recurrent account and \$589 million, or 24%, was on capital account. Total expenditure in 1979-80, (revised estimates) was \$16,290 million, of which \$10,202 million, or 63%, was on recurrent account and \$6,088 million, or 37%, was on capital account.

95 The proportion of total expenditure absorbed by general services (including law and order)<sup>(99)</sup> decreased over the decade from 18.2% to 16.3%, by economic services<sup>(100)</sup> from 11% to 7.3%, by common supporting services<sup>(101)</sup> from 6.4% to 3.4% and by other financial obligations<sup>(102)</sup> from 2.8% to 2.3%. By contrast, the proportion of total expenditure absorbed by community services<sup>(103)</sup> increased over the decade from 19% to 23.2%, by social services<sup>(104)</sup> from 40.8% to 43.5% and by unallocable expenditure<sup>(105)</sup> from 1.8% to 4%.

---

(98) See Annex (4).

(99) Administration, law and order, defence, public relations, revenue collection, financial control.

(100) Primary products, airport and harbour, commerce and industry, communications, statistics, land and survey, Royal Observatory, certain miscellaneous subventions.

(101) Launches and dockyard, printing, supplies, common supporting services such as the Electrical and Mechanical Office, the Government Land Transport Agency and the Buildings Ordinance Office.

(102) Pensions and gratuities.

(103) Transport, roads, civil engineering and land, water, fire services, amenities and related services.

(104) Education, medical and health, housing (including flatted factories, and commercial facilities for the Hong Kong Ownership Scheme), social welfare, labour.

(105) Government quarters, passages, recruiting expenses, rent for Government leased accommodation and additional commitments.

96 Within the *general services group*, the proportion of total expenditure absorbed by administration decreased from 2.1% to 1.7% and, indeed, has been less than 2% since 1973-74. Given that total expenditure increased by six and a half times over the decade, this is, in a sense, gratifying, but it does reflect how hard pressed the civil service has been in recent years, and we must bear this in mind in the years ahead. Expenditure on law and order absorbed 9.6% in 1970-71, and as much as 10.4% in 1976-77, but decreased to 8.4% by 1979-80. By the last year of the decade, defence expenditure absorbed 4.5% (or \$737 million) of total expenditure, having been only 1.8% in 1975-76 (or \$117 million). This increased level of expenditure is due to the application of the terms of the Defence Costs Agreement whereby the Hong Kong Government pays 75% of the total cost of the Armed Forces here and additional costs arising from the re-provisioning of facilities at Lyemun and Sham Shui Po Barracks, other supplementary works programmes and the reinforcement of the garrison.

97 Within the *community services group*, the proportion of total expenditure absorbed by transport, roads, civil engineering and land<sup>(106)</sup> was only 6.8% in 1970-71, but was as high as 13.3% by 1979-80; whilst the proportion of total expenditure absorbed by water peaked at 9.6% and 9.5% in 1973-74 and 1974-75 respectively, when work on the High Island Scheme was at its height, having been 5.8% in 1970-71 and it was only 3.2% in 1979-80.

98 Within the *social services group*, the proportion of total expenditure absorbed by education decreased from 20.4% in 1970-71 to 15.8% in 1979-80 but, at \$2,570 million, expenditure was five times more than expenditure ten years previously of \$510 million. The proportion of expenditure absorbed by medical and health services decreased from 10.1% in 1970-71 to 7.6% in 1979-80 but, at \$1,235 million, expenditure was also five times more than expenditure ten years previously of \$252 million. It is in the areas of housing and social welfare that a new emphasis developed over the decade: the proportion of total expenditure absorbed by housing increased from 8.4% to 15.2% and by social welfare from 1.6% to 4.5%. The increases over the

---

(106) *Gross areas of land formed and serviced(\*):*

	<i>Acres</i>
<i>1970-71</i>	<i>141</i>
<i>1971-72</i>	<i>92</i>
<i>1972-73</i>	<i>122</i>
<i>1973-74</i>	<i>170</i>
<i>1974-75</i>	<i>188</i>
<i>1975-76</i>	<i>193</i>
<i>1976-77</i>	<i>262</i>
<i>1977-78</i>	<i>323</i>
<i>1978-79</i>	<i>985</i>
<i>1979-80</i>	<i>1,261</i>

*Note: (\*) By the Public Works Department, but the figures for 1976-77 onwards include land formed for the Yuen Long and Tai Po Industrial Estates.*

decade were from \$211 million to \$2,480 million<sup>(107)</sup>, or by twelve times, on housing; and from \$40 million to \$729 million, or by eighteen times, on social welfare.

(d) *Fiscal policy*

(i) *Balance of the fiscal system*

99 I turn now to the subject of fiscal policy. In our circumstances, there is no alternative to a relatively high dependence on direct taxation<sup>(108)</sup> for the financing of recurrent services within the General Revenue Account and to help finance the deficit on capital account. This is because there is a tendency for the relative importance of earnings and profits taxes to increase and to go on increasing. As the yields from earnings and profits taxes are related to the growth rate of the economy in *money* terms, if that rate is sustained at, say, something like the trend rate experienced over the decade of the 1970s of 18-19%, high yields will be enjoyed<sup>(109)</sup>. Furthermore, there is greater scope for altering the structure of the direct tax system and the applicable rates, whereas, in the case of the indirect tax system<sup>(110)</sup> and fees and charges<sup>(111)</sup>, there are obvious practical constraints.

100 I would like to dwell for a moment on the income-sensitivity of our direct tax system<sup>(112)</sup>: yields from earnings and profits taxes have grown

(107) *Including \$1,788 million for capital expenditure, which may be reconciled with the estimate of total expenditure on housing in f.n. (137), B.S. 1980, as follows:*

	(\$ mn)
Total (1)+(2)+(3)	1,746
Add: <i>Flatted factories</i>	56
	1,802
Add: <i>Housing Society and Local Government Officers' Housing Schemes</i>	15
	1,817
Less: <i>A.D.B. loans</i>	— 29
	1,788

(108) *Direct taxes are defined as earnings and profits taxes. (Estate duty is regarded as capital revenue).*

(109) *Whereas yields from excise duties, for example, are more closely related to the growth rate of the economy in real terms.*

(110) *Indirect taxes are defined as excise duties, General Rates, internal revenue (i.e. bets and sweeps taxes, entertainment tax, hotel accommodation tax and stamp duties), motor vehicle taxes, franchises and airport concessions. (Premia paid for taxi concessions are regarded as capital revenue.)*

(111) *Including receipts appropriated-in-aid.*

(112) *Since the yields from earnings and profits taxes are fairly income-sensitive—and must remain so if the economy's internal flexibility is not to be damaged—whilst yields from indirect taxes, and fees and charges are relatively income-insensitive—and rightly so by their very nature—I believe the net effect is that our fiscal system is compatible with the adjustment process over the course of the trade cycle.*

from \$778 million in 1970-71 to \$5,880 million in 1979-80 (revised estimates)<sup>(113)</sup>. Over the decade, therefore, the yield increased seven and a half times whilst the G.D.P. (at current prices, of course) increased by four and a half times. The only major tax increase during this period was in the rate of corporation profits tax from 15% to 17%, although several reform measures, such as the bringing into charge of profits earned in Hong Kong from offshore borrowing and lending transactions arranged by banks and other financial institutions in Hong Kong, have also increased the yield from the system.

101 Of course, the productivity of the system is also a function of administrative efficiency. Not only have many more persons and businesses been identified as being liable to tax, but also the Inland Revenue Department has been able to step up its investigations into the affairs of persons who seek to evade tax and these investigations are bearing fruit<sup>(114)</sup>.

102 The thesis that there will be a tendency for the relative importance of earnings and profits taxes to increase is borne out by our experience over the decade: the yield from earnings and profits taxes has grown at an average annual rate of 25%, the yield from indirect taxes at 15% and the yield from fees and charges at 17%<sup>(115)</sup>. Thus, whereas in 1970-71 earnings and profits taxes contributed 30% of total recurrent revenue, by 1979-80 they contributed 45%; whilst the contribution of indirect taxes fell away from 39% to 28%. The contribution of fees and charges fell from 31% to 27%.

103 These trends in effect invalidated the guideline ratios I used to bear in mind when assessing the balance of the fiscal system, namely, that the ratio of direct to indirect taxation should be 45:55 and the ratio of direct and indirect taxation taken together to all other recurrent revenue should be 65:35. The average ratio for direct to indirect taxation shifted from 48:52 over the first five years of the decade to 55:45 in the next three and the ratio of direct and indirect taxation taken together to all other recurrent revenue averaged 70:30 over these eight years<sup>(116)</sup>. So, sensibly, therefore, the guideline ratios were revised in the 1978 budget speech to 55:45 and

---

(113) See Annex (5).

(114) In 1979-80, something like \$50 million will be collected in back tax and penalties from 140 cases. The Commissioner of Inland Revenue also pursues a policy of encouraging assessors outside the Investigation Section to handle, as part of their normal duties, a selection of small evasion cases. The direct result of all this activity is, of course, small compared with total tax collected, but it is the immeasurable deterrent effect on would-be evaders which is far more important.

(115) Although these figures reflect both the effects of changes in the tax system and the automatic changes in yields arising from the growth of incomes, the same tendency would emerge even after corrections had been made to remove the effects of tax changes.

(116) See Annex (6).

70:30, not that we have since adhered even to these revised ratios<sup>(117)</sup>, but this does not diminish their purpose which is to remind us of the importance of trying to maintain the yield from indirect taxes and fees and charges.

104 In a low tax environment, and particularly one which is characterized by very high tax thresholds, public services which can be related to individual needs must be charged for in full<sup>(118)</sup>, except where, as is frequently the case, a policy decision has decreed that General Revenue should assist in the financing of those services, in whole or in part. In some instances, charges may be pitched above the level necessary to recover full costs, primarily for the purpose of raising revenue or for deterring usage; and fees which are set for permission to engage in certain activities are not cost-related at all<sup>(119)</sup>.

(ii) *Requirements of the tax system*

105 At the same time, our tax system has been designed to meet six requirements: the *first* requirement is to help to generate sufficient recurrent revenue to finance a major proportion of a given level of total expenditure on General Revenue Account which, incidentally, I set at 88%; and to maintain our fiscal reserves at a satisfactory level.

106 The *second* requirement is that the tax system is as neutral as possible as regards the internal cost/price structure and investment decisions.

107 The *third* requirement is that the laws governing the tax system are adapted from time to time to make them consistent with changing commercial practices.

---

(117) *See paragraph 168, B.S. 1980.*

(118) *Provided adequate remission arrangements are available when required.*

(119) *In other words, there are three groups of fees and charges:*

(1) *Cost-related charges:*

- (a) *those which are designed to cover the full cost (including the cost of capital) of the services provided. These charges may, from time to time, be set at a level above that necessary to recover full cost to deter usage for policy reasons;*
- (b) *those which are set for the public utility-type undertakings operated by the Government, and which are designed to recover the full costs of operation and to earn a required return on capital employed;*
- (c) *those which do not cover the full cost (including the cost of capital) of the services provided, because there is a case on policy grounds for part of the cost of the service concerned being borne by General Revenue.*

(2) *Licences and royalties:*

*these fees and charges are payments for permission to engage in certain activities and trades. This group includes royalties paid by enfranchised companies as well as licences for various (restrictive) trades and practices (ranging from bank licences to tobacco dealers' licences). The level of fees and charges in this group in not directly related to costs.*

(3) *Tax-loaded fees: these are fees and charges for services rendered or permissions given. They are set above the level necessary to recover full costs specifically for the purpose of raising revenue.*

108 The *fourth* requirement is that each and every levy—be it direct or indirect—is simple and easy (and, therefore, inexpensive) to administer for both the Government and the taxpayer and does not encourage evasion, for a low and narrowly based tax system cannot afford to finance costly overheads.

109 The *fifth* requirement is that the tax system is equitable as between different classes of taxpayers or potential taxpayers and between different income groups (and this means, *inter alia*, setting relatively high thresholds for personal taxation and generally ensuring that the system rests as lightly as possible on the disposable income of those at the lower end of the income spectrum, or leaves them virtually untouched).

110 Exceptionally, and this is the *sixth* requirement, the tax system must be capable of being used to achieve non-fiscal (i.e. economic and social policy) objectives when necessary. I stress the word *exceptionally* because I believe that such policy objectives should be pursued directly through public expenditure programmes and by appropriate legislative measures, and not indirectly by adjustments to tax rates and amendments to tax laws. Once a government starts to tread that path the consequences are unpredictable, and the costs unquantifiable.

111 The tax changes introduced in the past ten years have all been consistent with one or more of these requirements as honourable Members will see from a study of Annex (7) to the printed version of this speech. But I am none too happy with the present distribution of the tax burden as between some *classes* of taxpayers—and I stress classes, *not* income groups. I am particularly concerned about the contribution to total recurrent revenue of (non-corporate) property taxpayers, ratepayers, consumers of dutiable commodities and patrons of the Jockey Club<sup>(120)</sup>.

(e) *Management of the General Revenue Account*

(i) *General*

112 So much for the relationship between the public sector and the economy, trends in the pattern of cash disbursements on Consolidated Account and fiscal policy in the 1970s. I turn now to an assessment of the management of the General Revenue Account over the decade.

---

(120)	<i>Contribution to total recurrent revenue:</i>		
	<i>1970-71 (%)</i>	<i>Peak year (%)</i>	<i>1979-80 (%)</i>
<i>Direct taxes:</i>			
<i>Property tax</i>	2.7	3.7 (1976-77)	2.1
<i>Indirect taxes:</i>			
<i>Rates</i>	11.8	11.8 (1970-71)	6.8
<i>Dutiable commodities</i>	16.0	16.0 (1970-71)	6.7
<i>Bets and sweeps</i>	1.5	5.0 (1978-79)	4.8
<i>Ratio of property tax to rates</i>	18:82	29:71 (1976-77)	24:76



(ii) *Budgetary guidelines*

113 The Government's own annual budgets were constructed so as to ensure that, taking one year with another, we achieved at least a balance between revenue and expenditure on General Revenue Account, having regard to the need to make additions to our fiscal reserves in line with the growth of expenditure and our contingent liabilities. In other words, we allowed surpluses to accrue when revenues (on either recurrent or capital account) were flushing and did not seek to eliminate deficits that might arise from a temporary—or what was thought to be a temporary—slowing down of the economy's growth rate.

114 Each annual budget itself was generally set in the context of revenue and expenditure trends in the current year and in preceding years and, also, in the context of a forecast of revenue and expenditure over the three years following the budget year. Then, an appropriate relationship between the recurrent and capital accounts was determined, because the rate at which our recurrent commitments grow in relation to recurrent revenue must be limited in order to secure the financing of the capital account. The guidelines adopted in the 1970s were that recurrent revenue should meet at least 88% of total expenditure, that recurrent expenditure should absorb no more than 80% of recurrent revenue, and that at least 60% of capital expenditure should be financed by the surplus on recurrent account and at least 20% by capital revenue. In other words, the view was taken that the residual deficit on capital account, if any, should be financed in a certain way, that is to say, at least 50% by capital revenue and no more than 50% by debt. In addition, an upper limit was set to recurrent expenditure of 70% of total expenditure(121). But, as the surplus on recurrent account could finance a quantum of capital expenditure which these ratios did not define, separate absolute guideline figures were set for the various components of the capital account and these were revised periodically.

---

(121) *In summary:*

(1) $\frac{\textit{Recurrent revenue}}{\textit{Total expenditure}}$	<i>Guideline</i> <i>At least 88%</i>
(2) $\frac{\textit{Recurrent expenditure}}{\textit{Recurrent revenue}}$	<i>No more than 80%</i>
(3) $\frac{\textit{Surplus on recurrent account}}{\textit{Capital expenditure}}$	<i>At least 60%</i>
(4) $\frac{\textit{Recurrent expenditure}}{\textit{Total expenditure}}$	<i>No more than 70%</i>
(5) $\frac{\textit{Capital revenue}}{\textit{Capital expenditure}}$	<i>At least 20%</i>

115 Taking each of the five guidelines in turn<sup>(122)</sup>: the ratio of recurrent revenue to total expenditure (Guideline (1)) fell from around 112% in the first three years of the decade to 98% in 1973-74. In 1974-75, the guideline of 88% was breached (the ratio fell to 86%): this was due to the fact that recurrent revenue increased in that year more slowly than total expenditure. The ratio then recovered to 104% in 1976-77, but declined to 93% by the end of the decade, as the growth rate of total expenditure persistently exceeded the growth rate of recurrent revenue.

116 Only in one year in the decade did the ratio of recurrent expenditure to recurrent revenue (Guideline (2)) exceed the guideline of 80%, namely, in the recession year 1974-75. In all other years, the growth rate of recurrent expenditure, in the event, was below the growth rate of recurrent revenue which was in line with the growth rate of G.D.P. in money terms, after allowing for leads and lags<sup>(123)</sup>.

117 Again, only in 1974-75, was the ratio of the surplus on recurrent account to capital expenditure (Guideline (3)), at 55%, less than the guideline of 60%; and as, in that year, the ratio of capital revenue to capital expenditure (Guideline (5)) was only 24%, an overall deficit on General Revenue Account emerged. In all other years, the surplus on recurrent account and flushing capital revenues<sup>(124)</sup>, combined in 1975-76 and 1976-77 with underspending on capital account<sup>(125)</sup>, resulted in overall surpluses on General Revenue Account.

118 Finally, the success with which the growth rate of recurrent expenditure has been contained in relation to recurrent revenue, combined with a new emphasis on capital expenditure, has meant that the balance between recurrent expenditure and capital expenditure (Guideline (4)) has shifted: in the first two years of the decade, the average ratio of recurrent expenditure

---

(122) See Annex (8).

(123)	Growth rates of:	
	Recurrent revenue (%)	G.D.P. in money terms (%)
<i>Pre-recession years:</i>		
1971-72/1971	17	14
1972-73/1972	29	18
1973-74/1973	16	31
<i>Post-recession years:</i>		
1976-77/1976	17	28
1977-78/1977	19	14
1978-79/1978	25	16
1979-80/1979	30	26

(124) Particularly in 1970-71 and 1972-73 and in the last three years of the decade when capital revenue financed more than 60% of capital expenditure.

(125) In relation both to the Approved Estimates and expenditure in the preceding years.

to total expenditure at 75% exceeded the guideline of 70% and this was the case again in the three years 1975-76 to 1977-78 when it was 76%. But, in the last two years of the decade, the ratio fell to 67% and then to 64%.

(iii) *Fiscal reserves*

119 Needless to say, steady, as opposed to erratic, progress is not just a matter of fixing upon a growth rate of expenditure on General Revenue Account which is both practicable and consistent with the need to contain the relative size of the public sector, or even of devising a management system which is subject to the discipline of guidelines that force us to think through the consequences of particular courses of action. It also depends on the extent to which we are able to insulate the public finances from shortterm deviations from the trend paths of revenue and expenditure.

120 I have stressed repeatedly that such deviations should not, ideally, affect the implementation of the Government's policies and programmes or involve adjustments to tax rates and charges. Of course, a sudden change of pace is inevitable in a situation in which the world trading environment shifts adversely, *or* when, perhaps through failure to exercise proper control over expenditure, a risk of persistent deficit emerges; *or* when the growth rate of expenditure has been accelerating and a period of consolidation is desirable (for instance on administrative grounds); *or* when a situation of demand-pull inflation threatens the ability of the economy to maintain internal and external equilibrium. But situations involving a short-lived tendency for expenditure to exceed revenue, or for revenue yields to fall below expectations, are best dealt with by having available adequate fiscal reserves; and, happily, adequate they are as we enter the uncharted waters of the 1980s. At the same time, our fiscal reserves must be adequate to provide cover for our contingent liabilities and to enable us to take equity positions in trading enterprises (such as the M.T.R.C.) and to put certain statutory funds in a position to meet their commitments (e.g. the Development Loan Fund and the Home Ownership Fund) for there is no reason why annual revenues should necessarily have to meet these particular calls.

121 Calculating our fiscal reserves on the same basis as at present, that is to say, by reference to the General Revenue Balance only<sup>(126)</sup>, and allowing for differences in exchange values and in the book values of fixed interest bearing assets in the relevant period<sup>(127)</sup>, the following picture

---

(126) *This balance is the excess of the Government's financial assets over its short-term liabilities and is available, if needed, over and above the general revenues of the Colony for appropriation.*

(127) *That is, in the period up to 31 March 1976 since when virtually all the General Account's foreign currency assets were transferred to the Exchange Fund against interest bearing debt certificates: see B.S., 1976, paras. 75-84. Incidentally, the Hong Kong dollar balances of the General Account over and above the Treasury's current cash requirements are also now held in Exchange Fund debt certificates in accordance with the concept of the Exchange Fund being effectively banker to the Government.*

emerges<sup>(128)</sup>: our fiscal reserves at 1 April 1970 represented as much as 64% of budgetted expenditure in 1970-71 of \$2,227 million but, at 1 April 1976, they represented only 39% of budgetted expenditure in 1976-77 of \$7,212 million. When I decided in 1977 that we had to make specific provision to secure our significantly larger contingent liabilities<sup>(129)</sup>, on the basis of a gearing of three, our 'free' reserves stood at \$1,213 million<sup>(130)</sup>, or nearly 15% of budgetted expenditure in 1977-78 of \$8,143 million. This was equal to the guideline I selected. By 1979-80 the position had improved to \$3,416 million<sup>(131)</sup>, or 27% of budgetted expenditure in 1979-80 of \$12,446 million.

### APPENDIX III

#### Paragraphs 128-134 of the printed version of the Budget Speech 1980

##### (1) *The Outlook for the World Economy*

###### (a) *Oil*

128 So much for our economic and financial experience in the past decade. I turn now to the immediate outlook, and the natural starting point, I am afraid, is oil.

129 In the past year or so, the posted prices of crude oil have increased more rapidly than in any period since the autumn of 1974. As a result, the

(128)	<i>Fiscal Reserves</i> (\$ mn) (1)	<i>Budgetted Expenditure</i> (*) (\$ mn) (2)	(1) as % of (2)
1 April 1970/1970-71	1,426	2,227	64
1 April 1971/1971-72	2,066	2,665	78
1 April 1972/1972-73	2,916	3,406	86
1 April 1973/1973-74	3,089	4,208	73
1 April 1974/1974-75	2,809	5,492	51
1 April 1975/1975-76	2,522	6,615	38
1 April 1976/1976-77	2,810	7,212	39
1 April 1977/1977-78	3,713	8,143	46
1 April 1978/1978-79	4,949	10,144	49
1 April 1979/1979-80	6,416(**)	12,446	52

Notes: (\*) Including, for this purpose, debt repayments.

(\*\*) This figure is, of course, not of the cost of the Government's equity position in the M.T.R.C. of \$1,144 million. The cost of the Government's equity positions in other enterprises has been charged to the Development Loan Fund.

(129) B.S., 1977, paragraph 106.

(130) Fiscal reserves at 1 April 1977=\$3,713 million, minus \$2,500 million being 1/3 of contingent liabilities at 31 March 1981 (i.e. the end of the then forecast period)= 'free' fiscal reserves of \$1,213 million.

(131) Fiscal reserves at 1 April 1979=\$6,416 million, minus \$3,000 million being 1/3 of contingent liabilities at 31 March 1983 (i.e. the end of the then forecast period)= 'free' fiscal reserves of \$3,416 million.

posted prices of most oil products have doubled, or more than doubled<sup>(135)</sup>. In addition, a greater proportion than previously of the world's supply of oil products is presently traded on the spot market and, for this part of the supply, price increases have generally been even larger. Although the recent increases in posted prices seem to be helping to close the gap between spot market and posted prices, the prospect for 1980 is that the prices of oil products are more likely to rise further than to fall. However, as the demand for, and supply of, oil products are likely to be more nearly in balance in 1980, availability of supply will probably be less of a problem than in 1979.

130 Although these price increases have direct implications for the Hong Kong economy, particularly as our energy supplies are based on oil products, their implications for the world economy as a whole are at least as important to us, because of the externally oriented nature of our economy. Following the 1973-74 increases in oil prices, the world economy moved into its most severe post-war recession which was characterized by very low or even negative growth rates of output and high rates of inflation. The latter were partly the direct consequence of increased oil prices and partly due to the efforts by some governments to mitigate, by expansionary fiscal and monetary policies, the recessionary impact of the shift in world purchasing power in favour of the oil exporting countries.

131 Although there is a possibility of this scenario being repeated in 1980, it is likely that most of the governments of major industrialized countries will adopt, or maintain, restrictive fiscal and monetary policies, although domestic political considerations are bound to exercise some influence. If so, these countries, which include Hong Kong's main markets, are likely to suffer a sharper, but shorter, period of recession accompanied by lower rates of inflation than in the post-1973 period.

132 As the recent (and likely further) increases in oil prices will constitute yet a further transfer of purchasing power from oil importing countries to oil exporting countries, the growth rates of the economies of the latter group are likely to accelerate, but it is difficult to quantify the extent to which new or enlarged markets for Hong Kong's exports will be opened up.

*(b) Projected growth rates of major industrialized countries*

133 Attempting to quantify the implications in 1980 of increases in oil prices, and of other factors affecting the growth rates of the world's major industrialized countries, is particularly difficult as prospects are also affected

---

(135) *For example, increases in posted prices in Singapore by the Shell Oil Company between January 1979 and January 1980 were:*

	(%)
<i>Motor gasoline</i>	82
<i>Gas oil</i>	111
<i>Kerosene</i>	112
<i>L.P.G.</i>	116

by geo-political uncertainties to an unusual degree. But, to the extent that a concensus can be detected, and most forecasts for 1980 have been quite drastically revised in recent months, it is that the growth rates of the economies of these countries are now expected to slow down in the first half of 1980 followed by a weak recovery in the second half. The growth rates of G.D.P. in both the United States and the United Kingdom are actually forecast to be negative in 1980<sup>(136)</sup>. This general slowing down in growth rates is the result of higher oil prices, which will reduce real purchasing power in the countries concerned thus reinforcing the effects of the fiscal and monetary policies already being pursued to restrain demand in order to try to reduce current rates of inflation.

(c) *Growth versus inflation*

134 However, with several exceptions, such as the United Kingdom, the slow down in the growth rates of most of the economies of the world's major industrialized countries is not expected to result in a significant reduction in their rates of inflation in 1980<sup>(137)</sup>. The main reason for this is that, although the increases in oil prices will reduce the pressure of demand, their impact is on the level of domestic prices and, furthermore, workers are likely to try to maintain their standards of living by demanding increased wages, even if this results in higher unemployment.

(136) For example, *O.E.C.D. forecast in November/December 1979:*

	G.N.P./G.D.P.		
	(% changes on immediately preceding period at annual rates)		
	1979	1980	
	2nd half	1st half	2nd half
<i>United States</i>	0.25	-2.75	0.25
<i>Canada</i>	0.50	2.00	2.00
<i>Japan</i>	6.25	4.50	3.75
<i>Germany</i>	4.00	1.75	1.50
<i>France</i>	3.00	1.75	1.50
<i>Italy</i>	3.25	1.75	1.25
<i>United Kingdom</i>	-2.25	-2.75	-0.50
<i>Major Seven</i>	<u>2.25</u>	<u>0.00</u>	<u>1.25</u>
<i>Total O.E.C.D.</i>	<u>2.25</u>	<u>0.50</u>	<u>1.50</u>

(137) For example, *O.E.C.D. forecast in November/December 1979:*

	Consumer Prices (% changes on immediately preceding period at annual rates)		
	1979	1980	
	2nd half	1st half	2nd half
<i>United States</i>	10.00	9.50	9.25
<i>Canada</i>	8.50	8.50	8.50
<i>Japan</i>	7.00	7.00	7.25
<i>Germany</i>	6.25	5.00	3.25
<i>France</i>	12.75	11.00	10.75
<i>Italy</i>	17.25	17.50	13.50
<i>United Kingdom</i>	<u>21.75</u>	<u>13.75</u>	<u>13.75</u>
<i>Major Seven</i>	<u>10.25</u>	<u>9.25</u>	<u>8.75</u>
<i>Total O.E.C.D.</i>	<u>10.00</u>	<u>9.25</u>	<u>8.75</u>

Annex (1)

THE HONG KONG ECONOMY 1970 TO 1979: GROWTH RATES OF  
SELECTED AGGREGATES AND VARIABLES (%)

<i>Growth rate in real terms of:</i>	1970	1971	1972	1973	1974	1975	1976	1977	1978(**)	1979(***)	<i>Average annual growth rate over the decade</i>
Private Consumption Expenditure	8.0	12.8	6.2	18.4	-1.1	2.0	8.8	17.3	18.4	7.7	9.6
Government Consumption Expenditure	5.6	1.6	8.7	12.0	10.1	5.1	8.1	12.5	12.8	12.3	8.8
Gross Domestic Fixed Capital											
Formation:	14.9	20.3	5.0	15.9	-3.1	1.4	16.8	24.1	17.7	23.7	13.3
Plant and machinery	17.7	15.2	3.1	21.4	-12.7	-3.9	18.7	17.8	17.9	46.3	13.1
Building and construction:	10.9	26.6	4.8	8.3	11.6	6.3	14.2	29.8	15.7	4.0	12.9
Private	27.6	24.7	4.4	-0.8	1.2	4.1	13.4	21.2	7.4	9.1	10.8
Public	-18.7	31.6	5.8	31.9	32.1	9.6	15.3	41.9	25.5	-1.2	15.9
Exports of Goods:	8.4	6.5	6.8	12.3	-6.3	3.2	28.0	5.1	13.8	19.5	9.4
Domestic exports	9.5	4.3	4.3	7.3	-2.8	3.2	29.5	4.8	10.4	16.6	8.4
Re-exports	3.8	16.6	17.3	30.4	-16.7	3.4	23.1	6.0	25.8	28.8	12.9
Imports of Goods	13.6	13.6	3.5	10.7	-10.3	3.8	24.8	7.9	21.5	15.6	10.0
Gross Domestic Product	6.2	5.0	9.7	16.4	1.8	2.2	18.8	9.8	10.0	11.5	9.0
Real Income (*)	8.2	8.7	11.4	15.5	-2.5	3.4	22.7	8.9	9.2	11.1	9.5
Gross Domestic Product <i>per capita</i>	3.7	2.7	7.8	13.7	-0.7	0.5	17.5	8.1	7.8	4.8	6.5
Real Income <i>per capita</i>	5.6	6.4	9.5	12.8	-4.9	1.6	21.3	7.2	7.0	4.4	6.9
Total Final Demand	9.6	9.0	6.7	13.4	-3.8	2.9	21.4	9.0	15.1	13.4	9.5
Domestic Demand:	9.1	13.5	6.1	17.5	-0.3	2.8	15.2	14.4	16.3	8.6	10.2
Private	10.3	14.0	5.9	17.4	-2.1	2.5	15.8	13.3	15.7	8.4	10.0
Public	-1.6	9.1	8.4	18.8	17.2	5.6	10.4	24.3	20.6	9.6	12.0
G.D.P. Deflator	11.1	8.4	7.8	12.9	12.2	2.3	7.8	4.1	5.8	13.3	8.5
Consumer Prices	7.1	3.4	6.1	18.2	14.4	1.2	4.0	5.5	5.8	11.6	7.6

Note: (\*) Growth rate of G.D.P. adjusted for shifts in the terms of trade.

(\*\*) Based on provisional estimates.

(\*\*\*) Based on preliminary estimates.

GENERAL REVENUE ACCOUNT (adjusted)						
	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76
	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)
<i>Revenue:</i>						
Recurrent	2,587	3,033	3,910	4,550	5,156	5,843
Capital	<u>327</u>	<u>315</u>	<u>761</u>	<u>466</u>	<u>437</u>	<u>412</u>
Total	2,914	3,348	4,671	5,016	5,593	6,255
<i>Expenditure:</i>						
Recurrent	1,764	1,973	2,464	3,231	4,175	4,450
Capital	<u>528</u>	<u>732</u>	<u>1,068</u>	<u>1,411</u>	<u>1,796</u>	<u>1,573</u>
Total	2,292	2,705	3,532	4,642	5,971	6,023
Surplus on recurrent account	823	1,060	1,446	1,319	981	1,393
Deficit on capital account	201	417	307	945	1,359	1,161
Overall surplus/deficit	622	643	1,139	374	-378	232
Actual surplus/deficit carried forward to the General Revenue Balance	619	640	636	72	-380	487



Annex (2)

1970-71 TO 1980-81  
figures)

		<i>1978-79 (Revised Estimates)</i>	<i>1978-79 (\$ mn)</i>	<i>1979-80 (Estimates)</i>	<i>1979-80 (Revised Estimates)</i>	<i>1980-81 (Draft Estimates)</i>
<i>1976-77 (\$ mn)</i>	<i>1977-78 (\$ mn)</i>	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>(\$ mn)</i>
6,850	8,151	9,932	10,146	11,476	13,214	14,798
<u>644</u>	<u>1,232</u>	<u>2,326</u>	<u>2,296</u>	<u>2,412</u>	<u>3,336</u>	<u>6,630</u>
7,494	9,383	12,258	12,442	13,888	16,550	21,428
5,224	6,219	7,444	7,308	8,360	9,081	10,702
<u>1,353</u>	<u>1,939</u>	<u>3,583</u>	<u>3,648</u>	<u>4,073</u>	<u>5,151</u>	<u>7,326</u>
<u>6,577</u>	<u>8,158</u>	<u>11,027</u>	<u>10,956</u>	<u>12,433</u>	<u>14,232</u>	<u>18,028</u>
1,626	1,932	2,488	2,838	3,116	4,133	4,096
709	707	1,257	1,352	1,661	1,815	696
917	1,225	1,231	1,486	1,455	2,318	3,400
903	1,236	1,211	1,467	1,433	1,925	3,091

(a) *General Notes on the Adjustments*

(1) The Urban Council and Housing Authority were established on 1 April 1973. Figures for 1970-71, 1971-72 and 1972-73 have been adjusted to exclude the previous activities of the Urban Services and Resettlement Departments which were taken over by the Urban Council and the Housing Authority. Between 1 April 1973 and 31 March 1975 the Government continued to be responsible for certain expenditure (e.g. personal emoluments), reimbursements from the Urban Council and the Housing Authority being credited to General Revenue. These transactions were taken below-the-line with effect from 1 April 1975 and so the figures for 1973-74 and 1974-75 have been adjusted to exclude them. Since 1 April 1975 Urban Council and Housing Authority revenue and expenditure have not appeared in the Government's accounts and so no adjustments are necessary for 1975-76 onwards.

(2) Adjustments have been made in respect of three types of transactions, namely:

- (a) transactions, which *could* have been dealt with below-the-line, but which, *in fact* have been passed through the General Revenue Account in accordance with the Government's accounting principles or for some other reason (e.g. purchase of equity in the Mass Transit Railway Corporation);
- (b) drawdowns of loans and repayments or principal. These transactions have to be passed through the General Revenue Account in accordance with the Government's accounting principles, but they affect the General Revenue *Balance* rather than the Account;
- (c) debits and credits in respect of transactions within the same financial year which it was decided to pass through the General Revenue Account not so much for accounting reasons but in order to define the Government's total commitment (e.g. land grants to the Mass Transit Railway Corporation paid for by contra-transfers to the Mass Transit Fund and land grants to the Home Ownership Scheme paid for from the Home Ownership Fund using funds transferred from General Revenue).

## (b) Detailed Notes on the Adjustments

<i>Year</i>	<i>Recurrent Revenue</i>	<i>Capital Revenue</i>	<i>Recurrent Expenditure</i>	<i>Capital Expenditure</i>
1970-71	-157 (U.C. & H.A.)		-136 (U.C. & H.A.)	-21 (U.C. & H.A.) -3 (D.R.)
1971-72	-193 (U.C. & H.A.)		-174 (U.C. & H.A.)	-19 (U.C. & H.A.) -3 (D.R.)
1972-73	-265(U.C. & H.A.)		-236(U.C. & H.A.)	-500 (M.T.F.) -29 (U.C. & H.A.) -3 (D.R.)
1973-74	-225 (U.C. & H.A.)		-225 (U.C. & H.A.)	-300 (M.T.F.) -2 (D.R.)
1974-75	-282 (U.C. & H.A.)		-282 (U.C. & H.A.)	-2 (D.R.)
1975-76		-264 (Loans)		-9 (D.R.)
1976-77			-14 (D.R.)	
1977-78		-335 (L.P., M.T.R.) -488 (L.P., H.O.S.) -27(Loans)		-335 (M.T.F.) -488 (H.O.F.) -16(D.R.)
1978-79		-115 (L.P., H.O.S.)		-5 (M.T.F.) -115 (H.O.F.) -14 (D.R.)
1979-80 (Estimates)			-8 (M.T.F.) -13(D.R.)	
1979-80 (Revised Estimates)			-4 (M.T.F.) -18 (D.R.)	
1980-81 (Draft Estimates)		-80 (L.P., H.O.S.) -25 (S.C.S.A.)	-5(M.T.F.)	-80 (H.O.F.) -303 (D.R.) -25 (J.S.C.)

---

<i>Legend:</i>	U.C. & H.A.	=Urban Council & Housing Authority
	D.R.	=Debt repayment
	M.T.F.	=Mass Transit Fund
	H.O.F.	=Home Ownership Fund for land premia
	L.P., M.T.R.	=Land premia, Mass Transit Railway
	L.P., H.O.S.	=Land premia, Home Ownership Scheme
	J.S.C.	=Jubilee Sports Centre
	S.C.S.A.	=Special Coin Suspense Account

## Annex (3)

APPLICATION OF CASH LIMITS 1979-80  
(adjusted figures)

	<i>Approved Estimates 1979-80 (\$ mn)</i>	<i>Revised Estimates 1979-80 (\$ mn)</i>	<i>Increase (\$ mn)</i>	<i>Increase exempted from cash limits (\$ mn) (% of A.E.)</i>	<i>Increase in breach of cash limits (\$ mn) (% of A.E.)</i>
Recurrent Expenditure	8,360	9,081	721	659 (1)	7.9 62 0.7
Capital Expenditure	<u>4,073</u>	<u>5,151</u>	<u>1,078</u>	<u>774 (2)</u>	<u>19.0</u> <u>304</u> <u>7.5</u>
Total Expenditure	<u><u>12,433</u></u>	<u><u>14,232</u></u>	<u><u>1,799</u></u>	<u><u>1,433</u></u>	<u><u>—</u></u> <u><u>366</u></u> <u><u>—</u></u>

(1) Largely attributable to the Pay Trend Survey salary revision w.e.f. 1 April 1979, the implementation of Report No. 2 of the Standing Commission on Civil Service Salaries w.e.f. 1 October 1979, expenses related to anti-illegal immigration measures and higher payments under the Defence Costs Agreement because of the decline in the Hong Kong dollar/sterling exchange rate.

(2) Includes \$290 million for the purchase of Fairmount Gardens, \$257 million for price increase in excess of expectations, \$122 million for unforeseen extraordinary items (e.g. camps for Vietnamese refugees and additional expenditure on dangerous slopes), and \$105 million for reinforcement of the garrison.

Annex (4)

SUMMARY OF CONSOLIDATED ACCOUNT EXPENDITURE BY  
MAIN FUNCTIONS 1970-71 TO 1975-76

(adjusted figures)

	1970-71		1971-72		1972-73		1973-74		1974-75		1975-76	
	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)
(A) <i>General Services</i>												
(1) Administration	52	2.1	63	2.1	80	2.1	103	2.0	120	1.8	120	1.8
(2) Law and order	240	9.6	285	9.6	349	9.0	453	9.0	601	9.1	637	9.7
(3) Defence	104	4.1	116	3.9	129	3.3	114	2.3	119	1.8	117	1.8
(4) Others	60	2.4	63	2.2	79	2.0	103	2.0	110	1.7	113	1.7
	<u>456</u>	<u>18.2</u>	<u>527</u>	<u>17.8</u>	<u>637</u>	<u>16.4</u>	<u>773</u>	<u>15.3</u>	<u>950</u>	<u>14.4</u>	<u>987</u>	<u>15.0</u>
(B) <i>Economic Services</i>	<u>277</u>	<u>11.0</u>	<u>318</u>	<u>10.8</u>	<u>369</u>	<u>9.5</u>	<u>439</u>	<u>8.7</u>	<u>530</u>	<u>8.0</u>	<u>550</u>	<u>8.4</u>
(C) <i>Community Services</i>												
(1) Transport, roads, civil engineering and land	170	6.8	243	8.2	358	9.2	595	11.8	717	10.8	640	9.7
(2) Water	146	5.8	201	6.8	366	9.4	485	9.6	629	9.5	480	7.3
(3) Others	159	6.4	196	6.7	249	6.5	329	6.5	459	7.0	432	6.6
	<u>475</u>	<u>19.0</u>	<u>640</u>	<u>21.7</u>	<u>973</u>	<u>25.1</u>	<u>1,409</u>	<u>27.9</u>	<u>1,805</u>	<u>27.3</u>	<u>1,552</u>	<u>23.6</u>
(D) <i>Social Services</i>												
(1) Education	510	20.4	596	20.2	711	18.3	1,011	20.0	1,164	17.6	1,290	19.6
(2) Medical and health	252	10.1	305	10.3	379	9.8	457	9.1	560	8.5	562	8.6
(3) Housing	211	8.4	218	7.4	247	6.4	339	6.7	675	10.2	667	10.2
(4) Social welfare	40	1.6	60	2.0	88	2.3	153	3.0	276	4.2	359	5.5
(5) Labour	8	0.3	9	0.3	11	0.3	13	0.3	16	0.2	17	0.2
	<u>1,021</u>	<u>40.8</u>	<u>1,188</u>	<u>40.2</u>	<u>1,436</u>	<u>37.1</u>	<u>1,973</u>	<u>39.1</u>	<u>2,691</u>	<u>40.7</u>	<u>2,895</u>	<u>44.1</u>
(E) <i>Common Supporting Services</i>	<u>159</u>	<u>6.4</u>	<u>160</u>	<u>5.4</u>	<u>200</u>	<u>5.2</u>	<u>238</u>	<u>4.7</u>	<u>318</u>	<u>4.8</u>	<u>246</u>	<u>3.7</u>
(F) <i>Unallocable Expenditure</i>	<u>44</u>	<u>1.8</u>	<u>44</u>	<u>1.5</u>	<u>161</u>	<u>4.2</u>	<u>98</u>	<u>2.0</u>	<u>164</u>	<u>2.5</u>	<u>168</u>	<u>2.6</u>
(G) <i>Other Financial Obligations</i>	<u>72</u>	<u>2.8</u>	<u>76</u>	<u>2.6</u>	<u>99</u>	<u>2.5</u>	<u>118</u>	<u>2.3</u>	<u>152</u>	<u>2.3</u>	<u>167</u>	<u>2.6</u>
Total Expenditure	<u><u>2,504</u></u>		<u><u>2,953</u></u>		<u><u>3,875</u></u>		<u><u>5,048</u></u>		<u><u>6,610</u></u>		<u><u>6,565</u></u>	

Annex (4) cont'd.

SUMMARY OF CONSOLIDATED ACCOUNT EXPENDITURE BY  
MAIN FUNCTIONS 1976-77 TO 1980-81

(adjusted figures)

	1976-77		1977-78		1978-79		1979-80 (Revised Estimates)		1980-81 (Draft Estimates)	
	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)	(\$ mn)	(%)
(A) <i>General Services</i>										
(1) Administration	140	1.9	171	1.9	226	1.9	274	1.7	337	1.6
(2) Law and order	764	10.4	906	9.9	1,052	8.7	1,365	8.4	1,502	7.2
(3) Defence	253	3.4	388	4.2	597	5.0	737	4.5	928	4.5
(4) Others	146	2.0	170	1.8	289	2.4	276	1.7	319	1.5
	<u>1,303</u>	<u>17.7</u>	<u>1,635</u>	<u>17.8</u>	<u>2,164</u>	<u>18.0</u>	<u>2,652</u>	<u>16.3</u>	<u>3,086</u>	<u>14.8</u>
(B) <i>Economic Services</i>	<u>570</u>	<u>7.8</u>	<u>645</u>	<u>7.0</u>	<u>781</u>	<u>6.5</u>	<u>1,192</u>	<u>7.3</u>	<u>1,677</u>	<u>8.0</u>
(C) <i>Community Services</i>										
(1) Transport, roads, civil engineering and land	738	10.1	1,100	12.0	1,765	14.6	2,176	13.3	2,685	12.8
(2) Water	466	6.3	462	5.0	394	3.3	515	3.2	678	3.3
(3) Others	540	7.3	629	6.9	776	6.4	1,090	6.7	1,241	5.9
	<u>1,744</u>	<u>23.7</u>	<u>2,191</u>	<u>23.9</u>	<u>2,935</u>	<u>24.3</u>	<u>3,781</u>	<u>23.2</u>	<u>4,604</u>	<u>22.0</u>
(D) <i>Social Services</i>										
(1) Education	1,431	19.5	1,655	18.0	1,964	16.3	2,576	15.8	2,968	14.2
(2) Medical and health	648	8.8	756	8.2	955	7.9	1,235	7.6	1,491	7.1
(3) Housing	621	8.4	1,027	11.2	1,692	14.0	2,480	15.2	3,888	18.6
(4) Social welfare	365	5.0	399	4.4	550	4.6	729	4.5	839	4.0
(5) Labour	20	0.3	24	0.3	31	0.2	72	0.4	89	0.4
	<u>3,085</u>	<u>42.0</u>	<u>3,861</u>	<u>42.1</u>	<u>5,192</u>	<u>43.0</u>	<u>7,092</u>	<u>43.5</u>	<u>9,275</u>	<u>44.3</u>
(E) <i>Common Supporting Services</i>	<u>270</u>	<u>3.7</u>	<u>344</u>	<u>3.8</u>	<u>439</u>	<u>3.6</u>	<u>554</u>	<u>3.4</u>	<u>651</u>	<u>3.1</u>
(F) <i>Unallocable Expenditure</i>	<u>162</u>	<u>2.2</u>	<u>235</u>	<u>2.6</u>	<u>275</u>	<u>2.3</u>	<u>651</u>	<u>4.0</u>	<u>1,253</u>	<u>6.0</u>
(G) <i>Other Financial Obligations</i>	<u>214</u>	<u>2.9</u>	<u>255</u>	<u>2.8</u>	<u>282</u>	<u>2.3</u>	<u>368</u>	<u>2.3</u>	<u>385</u>	<u>1.8</u>
<i>Total Expenditure</i>	<u><u>7,348</u></u>		<u><u>9,166</u></u>		<u><u>12,068</u></u>		<u><u>16,290</u></u>		<u><u>20,931</u></u>	

Annex (5)

SUMMARY OF ACTUAL REVENUE BY MAIN SOURCES  
1970-71 TO 1975-76

(adjusted figures)

	1970-71 (\$ mn)	1971-72 (\$ mn)	1972-73 (\$ mn)	1973-74 (\$ mn)	1974-75 (\$ mn)	1975-76 (\$ mn)
<i>Recurrent Account:</i>						
DIRECT TAXES						
Earnings and profits tax	778	929	1,083	1,680	2,144	2,234
INDIRECT TAXES						
Duties	413	451	472	442	473	558
General rates	306	314	291	369	408	534
Internal revenue:						
Bets and sweeps tax	38	51	53	62	96	161
Entertainment tax	31	32	34	4	4	19
Hotel accommodation tax	4	4	5	6	6	9
Stamp duties	127	214	713	463	303	382
Motor vehicle taxes	40	44	57	46	32	49
Franchises	28	26	35	34	40	51
Airport concessions	13	20	36	45	42	51
OTHER REVENUE	809	948	1,131	1,399	1,608	1,795
Total Recurrent	<u>2,587</u>	<u>3,033</u>	<u>3,910</u>	<u>4,550</u>	<u>5,156</u>	<u>5,843</u>
<i>Capital Account:</i>						
DIRECT TAXES						
Estate duty	25	27	40	50	42	64
INDIRECT TAXES						
Taxi concessions			39	85		
OTHER REVENUE						
Land Sales	272	269	669	318	287	346
Others	30	19	13	13	108	2
Total Capital	<u>327</u>	<u>315</u>	<u>761</u>	<u>466</u>	<u>437</u>	<u>412</u>
Total Revenue	<u>2,914</u>	<u>3,348</u>	<u>4,671</u>	<u>5,016</u>	<u>5,593</u>	<u>6,255</u>

Annex (5) cont'd.

SUMMARY OF ACTUAL REVENUE BY MAIN SOURCES  
1976-77 TO 1980-81

(adjusted figures)

		1976-77	1977-78	1978-79	1979-80 (Revised Estimates)	1980-81 (Draft Estimates)
		(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)
<i>Recurrent Account:</i>						
DIRECT TAXES	Earnings and profits tax	2,699	3,357	4,115	5,880	6,920
INDIRECT TAXES	Duties	681	734	830	888	942
	General rates	618	723	807	892	973
	Internal revenue:					
	Bets and sweeps tax	265	336	509	640	720
	Entertainment tax	23	27	29	36	39
	Hotel accommodation tax	15	20	24	33	43
	Stamp duties	428	490	762	800	750
	Motor vehicle taxes	102	148	259	320	365
	Franchises	51	63	74	85	96
	Airport concessions	62	71	88	100	115
OTHER REVENUE		<u>1,906</u>	<u>2,182</u>	<u>2,649</u>	<u>3,540</u>	<u>3,835</u>
	Total Recurrent	<u>6,850</u>	<u>8,151</u>	<u>10,146</u>	<u>13,214</u>	<u>14,798</u>
<i>Capital Account:</i>						
DIRECT TAXES	Estate duty	85	110	128	190	170
INDIRECT TAXES	Taxi concessions		112	250	275	275
OTHER REVENUE	Land Sales	557	1,008	1,893	2,858	6,169
	Others	<u>2</u>	<u>2</u>	<u>25</u>	<u>13</u>	<u>16</u>
	Total Capital	<u>644</u>	<u>1,232</u>	<u>2,296</u>	<u>3,336</u>	<u>6,630</u>
	Total Revenue	<u><u>7,494</u></u>	<u><u>9,383</u></u>	<u><u>12,442</u></u>	<u><u>16,550</u></u>	<u><u>21,428</u></u>



*Annex (6)*

## BALANCE OF THE FISCAL SYSTEM 1970-71 TO 1980-81

	<i>1970-71</i>	<i>1971-72</i>	<i>1972-73</i>	<i>1973-74</i>	<i>1974-75</i>	<i>1975-76</i>
<u>Direct</u>						
Indirect	44:56	45:55	39:61	53:47	60:40	55:45
<u>Direct and Indirect</u>						
All other Recurrent Revenue	69:31	69:31	71:29	69:31	69:31	69:31
	<i>1976-77</i>	<i>1977-78</i>	<i>1978-79</i>	<i>1979- 80(Revised Estimates)</i>	<i>1980- 81(Draft Estimates)</i>	
<u>Direct</u>						
Indirect	55:45	56:44	55:45	61:39	63:37	
<u>Direct and Indirect</u>						
All other Recurrent Revenue	72:28	73:27	74:26	73:27	74:26	

## Annex (7)

FISCAL CHANGES 1970-71 TO 1979-80  
(IN TERMS OF THE REQUIREMENTS OF FISCAL POLICY)

I. *To generate sufficient revenue*

<i>Item</i>	<i>Budget</i>
(1) Increase in fresh water charges	1971
(2) Increase in charges for salt water for flushing purposes	1971
(3) Increase in car parking charges	1972
(4) Increase in <i>ad valorem</i> stamp duty on contract notes in respect of share transactions	1973
(5) Increase in excise duty on intoxicating liquors	1974
(6) Increase in excise duty on tobacco	1974
(7) Phased introduction of property tax on properties assessed to rates in the New Territories	1974
(8) Increase in vehicle licence fees	1974
(9) Increase in vehicle first registration tax from 10% to 15%	1974
(10) Increase in fees for additional endorsements on drivers' licences	1974
(11) Increase in off-street car parking charges	1974
(12) Increase in the rate of Corporation Profits Tax by 1½ percentage points	1975
(13) Increase in the rate of betting duty	1975
(14) Increase in General Rates by 2 percentage points	1975
(15) Increase in excise duty on intoxicating liquors	1975
(16) Increase in excise duty on tobacco	1975
(17) Increase in stamp duty on cheques	1975
(18) Increase in stamp duty on certain conveyances on sales, etc.	1975
(19) Reintroduction of entertainment tax on cinema admission charges	1975
(20) Increase in business registration fees	1975
(21) Increase in companies' registration fees	1975
(22) Increase in Macau Ferry Terminal passenger charges (subsequently partially reduced)	1975
(23) Increase in buoy fees	1975
(24) Increase in bank licence fees	1975
(25) Introduction of a finance companies' registration fee	1975
(26) Introduction of a fee for textile export licences	1975
(27) Increase in vehicle first registration tax and abolition of Commonwealth preference tax	1975 (December)
(28) Increase in excise duties on manufactured tobacco and intoxicating liquors and abolition of Commonwealth preferences	1975 (December)
(29) Increase in the rate of Corporation Profits Tax by one-half of a percentage point	1976
(30) Increase in the maximum rate of estate duty to 18%	1976
(31) Increase in General Rates by 1 percentage point	1976
(32) Extension of rating to seven new areas in the New Territories	1976

<i>Item</i>	<i>Budget</i>
(33) Increase in stamp duty on certain conveyances on sales, etc.	1976
(34) Increase in excise duty on hydrocarbon oils	1976
(35) Increase in business registration fees	1976
(36) Reductions in General Rates to 7½% and 11% (as a consequence of a substantial increase in rateable values)	1977
(37) Increase in excise duty on tobacco	1978
(38) Increase in postal charges	1978
(39) Introduction of a scale for vehicle first registration tax	1978
(40) Increase in first registration tax on motor vehicles	1978
(41) Increase in motor vehicle licence fees	1978
(42) Increase in buoy and anchorage fees	1978
(43) Increase in business registration fees	1978
II. <i>To make the fiscal system neutral as regards the cost/price structure and investment decisions</i>	
(1) Abolition of excise duties on hydrocarbon oils other than furnace oil, aircraft and motor spirits and diesel oil	1972
(2) Abolition of excise duties on furnace oil	1973
(3) Increase in the initial depreciation allowance and new table of rates of depreciation for plant and machinery	1974
(4) Reduction in the rate of stamp duty on contract notes	1978
III. <i>Adaptation of the fiscal system to accord with changing commercial practices</i>	
(1) Exemption of stamp duty on contract notes on purchases and sales by a broker performing a jobbing function (but not, in the event, implemented)	1973
(2) Abolition of stamp duties on a miscellany of documents	1973
(3) Reduction in the ambit of the Stamp Ordinance	1978
IV. <i>To simplify and assist administration and discourage evasion</i>	
(1) Introduction of lower income relief	1970
(2) Abolition of television licence fees (effective from 1 April 1972)	1971
(3) Abolition of the tax on ships working cargo on Sundays	1971
(4) Abolition of duty on methyl alcohol	1972
(5) Reduction in the maximum rate of estate duty to 15%	1972
(6) Increase in personal, wife and child allowances, alteration of schedular rates, and abolition of lower income relief, dependent parent's relief, deductions for life insurance and similar payments, and working wife allowance	1973
(7) Abolition of stamp duty on receipts	1973
(8) Increase in vehicle licence fees	1973
(9) Further surcharge on late payment of rates and taxes	1974
(10) Abolition of stamp duty on five archaic heads in the Schedule to the Stamp Ordinance	1977
(11) Increase in excise duty on tobacco	1978
(12) Full tax becoming due if the first instalment is not paid by the due date	1978

<i>Item</i>	<i>Budget</i>
(13) Amendment of Dutiable Commodities Ordinance to make it an offence to use kerosene for automotive purposes	1978
(14) Introduction of a 'pooling' system of depreciation allowances for plant and equipment	1979
(15) Amendment of Estate Duty Ordinance to close the loophole whereby duty is avoided through controlled companies overseas	1979
V. <i>To maintain equity between different groups and classes of taxpayers and to minimize the tax burden of those on lower taxable incomes</i>	
(1) Abolition of concessionary rate of duty paid by enfranchised bus companies on automotive diesel oil, offset by a corresponding reduction in the rate of royalty	1970
(2) Introduction of dependent parent's relief for the widowed mother of either the taxpayer or his wife or for the father of either who is dependent on them for reasons of age or incapacity	1970
(3) Introduction of working wife allowance	1970
(4) Introduction of lower income relief	1970
(5) Abolition of entertainment tax on all live entertainment, except on race meeting where a <i>pari-mutuel</i> is being operated	1970
(6) Abolition of public dance halls tax	1970
(7) Reduction of maximum rate of estate duty from 25% to 20%	1970
(8) Reduction in the maximum rate of estate duty to 15%	1972
(9) Revision in schedular steps (from 5% to 2½%) to reduce the burden of those on lower taxable incomes	1972
(10) Increase in personal, wife and child allowances, alteration of schedular rates, and abolition of lower income relief, dependent parent's relief, deductions for life insurance and similar payments, and working wife allowance	1973
(11) Relief from stamp duties in respect of conveyances of low value properties	1973
(12) Abolition of excise duty on table water	1973
(13) Increase in excise duties on imports of alcoholic liquors in bulk	1973
(14) Abolition of entertainment tax on admission charges to cinemas	1973
(15) Increase in General Rate charge in Tsuen Wan and introduction of rating in Tsing Yi	1974
(16) Phased introduction of property tax on properties assessed to rates in the New Territories	1974
(17) Increase in the exemption limit from \$200,000 to \$300,000 for estate duty purposes	1974
(18) Abolition of stamp duty on student loan documents	1974
(19) Increase in the assessed value of free or subsidized quarters for salaries tax purposes	1975
(20) Extension of rating to seven new areas in the New Territories	1976
(21) Scheme of relief of limiting increases in rates payments following revaluation	1977
(22) Increase in the exemption limit from \$300,000 to \$400,000 for estate duty purposes	1977
(23) Introduction of supplementary basic allowances and increase in child allowances	1977
(24) Abolition of stamp duty on five archaic heads in the Schedule to the Stamp Ordinance	1977

<i>Item</i>	<i>Budget</i>
(25) Full tax becoming due if the first instalment is not paid by the due date	1978
(26) Introduction of a scale for vehicle first registration tax	1978
(27) Reduction of 'claw-back' in respect of supplementary personal allowance from 15% to 10%	1979
(28) Abolition of the 30% marginal rate applicable to net chargeable income in excess of \$50,000 a year under salaries tax	1979
(29) Increase in duty-free limit on gifts <i>inter vivos</i> from \$5,000 to \$50,000	1979
(30) Relief from interest tax where trustees both receive and pay out interest	1979
VI. <i>Exceptionally to achieve certain non-fiscal objectives</i>	
(1) Increase in car parking charges	1972
(2) Relief from stamp duties in respect of conveyances of low value properties	1973
(3) Increase in drivers' licence fees	1974
(4) Increase in fees for additional endorsements on drivers' licences	1974
(5) Increase in off-street car parking charges	1974
(6) Abolition of stamp duty on charitable gifts of shares and property	1973
(7) Increase in the initial depreciation allowance and new table of rates of depreciation for plant and machinery	1974
(8) Introduction of surcharge on peak hour air movements	1975
(9) Increase in vehicle first registration tax and abolition of Commonwealth preference tax	1975
	(December)
(10) Increase in excise duties on manufactured tobacco and intoxicating liquors and abolition of Commonwealth preferences	1975
	(December)
(11) Further relief from stamp duties in respect of conveyances of low value properties	1977
(12) Amendment of Dutiable Commodities Ordinance to make it an offence to use kerosene for automotive purposes	1978

Annex (8)

BUDGETARY GUIDELINES 1970-71 TO 1974-75  
(\$ MILLION AND %)

(adjusted figures)

	<i>Guideline</i>	<i>1970-71</i>	<i>1971-72</i>	<i>1972-73</i>	<i>1973-74</i>	<i>1974-75</i>
(1)	$\frac{\text{Recurrent Revenue}}{\text{Total Expenditure}}$ At least 88%	$\frac{2,587}{2,292}=113$	$\frac{3,033}{2,705}=112$	$\frac{3,910}{3,532}=111$	$\frac{4,550}{4,642}=98$	$\frac{5,156}{5,971}=86$
(2)	$\frac{\text{Recurrent Expenditure}}{\text{Recurrent Revenue}}$ No more than 80%	$\frac{1,764}{2,587}=68$	$\frac{1,973}{3,033}=65$	$\frac{2,464}{3,910}=63$	$\frac{3,231}{4,550}=71$	$\frac{4,175}{5,156}=81$
(3)	Surplus on $\frac{\text{Recurrent Account}}{\text{Capital Expenditure}}$ At least 60%	$\frac{823}{528}=156$	$\frac{1,060}{732}=145$	$\frac{1,446}{1,068}=135$	$\frac{1,319}{1,411}=93$	$\frac{981}{1,796}=55$
(4)	$\frac{\text{Recurrent Expenditure}}{\text{Total Expenditure}}$ No more than 70%	$\frac{1,764}{2,292}=77$	$\frac{1,973}{2,705}=73$	$\frac{2,464}{3,532}=70$	$\frac{3,231}{4,642}=70$	$\frac{4,175}{5,971}=70$
(5)	$\frac{\text{Capital Revenue}}{\text{Capital Expenditure}}$ At least 20%	$\frac{327}{528}=62$	$\frac{315}{732}=43$	$\frac{761}{1,068}=71$	$\frac{476}{1,411}=34$	$\frac{437}{1,796}=24$

Annex (8)

cont'd.

BUDGETARY GUIDELINES 1975-76 TO 1980-81  
(\$ MILLION AND %)

(adjusted figures)

	<i>Guideline</i>	<i>1975-76</i>	<i>1976-77</i>	<i>1977-78</i>	<i>1978-79</i>	<i>1979-80</i> <i>(Revised</i> <i>Estimates)</i>	<i>1980-81</i> <i>(Draft</i> <i>Estimates)</i>
(1)	$\frac{\text{Recurrent Revenue}}{\text{Total Expenditure}}$	At least 88%	$\frac{5,843}{6,023} = 97$	$\frac{6,850}{6,577} = 104$	$\frac{8,151}{8,158} = 100$	$\frac{10,146}{10,956} = 93$	$\frac{13,214}{14,232} = 93$ $\frac{14,798}{18,028} = 82$
(2)	$\frac{\text{Recurrent Expenditure}}{\text{Recurrent Revenue}}$	No more than 80%	$\frac{4,450}{5,843} = 76$	$\frac{5,224}{6,850} = 76$	$\frac{6,219}{8,151} = 76$	$\frac{7,308}{10,146} = 72$	$\frac{9,081}{13,214} = 69$ $\frac{10,702}{14,798} = 72$
(3)	$\frac{\text{Recurrent Account}}{\text{Capital Expenditure}}$	At least 60%	$\frac{1,393}{1,573} = 89$	$\frac{1,626}{1,353} = 120$	$\frac{1,932}{1,939} = 100$	$\frac{2,838}{3,648} = 78$	$\frac{4,133}{5,151} = 80$ $\frac{4,096}{7,326} = 56$
(4)	$\frac{\text{Recurrent Expenditure}}{\text{Total Expenditure}}$	No mre than 70%	$\frac{4,450}{6,023} = 74$	$\frac{5,224}{6,577} = 79$	$\frac{6,219}{8,151} = 76$	$\frac{7,308}{10,956} = 67$	$\frac{9,08}{14,232} = 64$ $\frac{10,702}{18,028} = 59$
(5)	$\frac{\text{Capital Revnue}}{\text{Capital Expenditure}}$	At least 20%	$\frac{412}{1,573} = 26$	$\frac{644}{1,353} = 48$	$\frac{1,232}{1,939} = 64$	$\frac{2,296}{3,648} = 63$	$\frac{3,336}{5,151} = 65$ $\frac{6,630}{7,326} = 90$

Annex (9)

FORECAST OF EXPENDITURE ON THE GROSS DOMESTIC  
PRODUCT IN 1980

Component	At Constant (1973) Prices			Rate of increase in prices (%)	At Current Prices	
	Preliminary estimates 1979 (\$ mn)	Forecast 1980 (\$ mn)	Growth rate in real terms 1980 (%)		Preliminary estimates 1979 (\$ mn)	Forecast 1980 (\$ mn)
Private Consumption Expenditure	39,054	42,500	9	10	57,666	69,000
Government Consumption Expenditure	3,407	3,800	12	10	5,503	6,750
Gross Domestic Fixed Capital Formation(*):	13,876	15,550	12	16	25,298	33,000
Plant and machinery	7,332	8,400	15	8	12,758	15,850
Building and construction:	6,040	6,620	10	25	11,841	16,250
Public	2,832	3,250	15	25	5,552	7,980
Private	3,208	3,370	5	25	6,289	8,250
Exports of Goods:	46,041	50,000	9	10	75,966	90,800
Domestic exports(**)	34,153	36,500	7	10	55,941	65,800
Re-exports	11,888	13,500	14	10	20,025	25,000
Imports of Goods(***)	51,130	56,700	11	10	86,469	105,750
Exports less Imports of Services	5,893	6,400	9	10	10,018	12,000
Stocks	-564	150			-637	200
Gross Domestic Product	56,577	61,800	9	11	87,345	106,000

Notes: (\*) Included here, but not shown separately, is a small element of net expenditure incurred in connection with the transfer of ownership of land and of existing buildings; this element is calculated as the sum of stamp duty collections, together with the legal fees and charges involved in the transactions. The growth rate of this small element is assumed to be the same as that of private expenditure on building and construction.

(\*\*) Forecast growth rates in real terms of domestic exports by major markets: U.S., 4%; F.R.G., 10%; U.K., 6%; rest of the world, 9%.

(\*\*\*) Included here, but not shown separately, is an estimate of imports of gold for industrial and commercial use, and imports of water.



*Annex (10)*

## FINANCIAL INFORMATION SYSTEM

Another important development in improving the system of financial administration is the introduction of a financial information system by the Treasury. The Estimates do not give a clear indication of the true costs of the services provided for the public; they are set out in such a way as to provide the information necessary to assist the Legislative Council in the voting of funds each year, and because they are related to the annual appropriation exercise, they are concerned with cash expenditure rather than true costs. With the growing sophistication of the Government's activities, and indeed with the sheer size of the funds for which appropriation has been sought in recent years and in 1980-81, there is a growing need to be able to provide additional information indicating the true costs of services.

2 With effect from 1 April 1980 the Treasury will introduce a financial information system which will eventually provide management information on a cost centre basis for all departments, thus making it possible to calculate the true costs of the various services provided by the Government. This information will help to improve the decision making process and enable the evaluation of the effect of both past and future policies. The system will be introduced gradually over a period of years beginning with the Medical and Health Department, the Kowloon-Canton Railway and the Prisons Department this year. The information system is a logical development of the computerization of the accounting system introduced a year ago.

3 The existing principles of control of Government funds by cash allocation will, however, not be affected, and Controlling Officers will continue to be responsible for the disbursement of funds. The financial information system will provide additional information based on the cash accounts with the purpose of improving the decision making process.

4 In parallel with the development of financial information system, a reappraisal of the contents of the printed Estimates is taking place since in recent years there has been a tendency to show expenditure in the form of rather ill-defined cost centres which confuse the separate concepts of expenditure and cost. In order that the financial information system can be made more effective, steps will be taken during the course of the year to eliminate these cost centres in the Estimates so that expenditure information is provided in a consistent manner that will facilitate the preparation of true cost centre information.

*Annex (11)*

## EXPENDITURE IN THE MAIN PROGRAMME AREAS

(1) *Law and order*

The Draft Estimates provide for expenditure of \$1,502 million on law and order services<sup>(1)</sup>. This represents 8.3% of total expenditure in 1980-81.

2 The process of consolidation within the Police Force continued during 1979-80. Police management services were expanded to increase planning capability and police headquarters was reorganized. This has been followed by a manpower deployment study of commands at district and divisional levels. The Force continued to expand<sup>(2)</sup>; and further expansion is envisaged in 1980-81.

3 Reported crime rose significantly during the year<sup>(3)</sup> showing a 22% increase in violent crime and a 17% increase in serious crime. This trend coincided with a marked shortage at street level of illegal narcotics due partly to successful enforcement action both here and in Thailand, resulting in higher prices of illegal narcotics. There is no doubt an inter-relationship

(1)	<i>Approved Estimates 1979-80 (\$ mn)</i>	<i>Draft Estimates 1980-81 (\$ mn)</i>
<i>R.H.K.P.F.</i>	731	979
<i>R.H.K.A.P.F.</i>	37	34
<i>Immigration</i>	60	101
<i>I.C.A.C.</i>	58	66
<i>Judiciary</i>	44	64
<i>Legal</i>	19	25
<i>Prisons</i>	135	197
<i>Registrar General</i>	23	24
<i>Expenses of refugees</i>	—	12
	<u>1,107</u>	<u>1,502</u>

(2) *Police Establishment:*

*Approved Estimates 1979-80*

22,687 (including 3,617 civilians)

*Draft Estimates 1980-81*

24,769 (including 3,884 civilians)

(3) *Violent Crime:*

		%
1975	18,423	-2
1976	16,436	-11
1977	14,731	-10
1978	14,376	-2
1979	17,604	+22

*Serious Crime (i.e. reported crimes less blackmail and minor offences):*

		%
1975	52,050	-2
1976	52,812-12	+1
1977	51,610	-2
1978	52,383	+1
1979	61,516	+17

between this and the incidence of quick-cash crime such as robberies, burglaries and theft. But the prison muster of convicted criminals dropped from 6,406 in January to 5,919 in December 1979. Efforts to encourage more reporting of crime and better communication with the public include the expansion by 149 posts of the neighbourhood policing scheme and an additional 46 neighbourhood police units and police reporting centres in 1980-81.

4 A major effort was required from the Force during the year in the fight against illegal immigration. A small boat unit was established, and nine new sector launches were ordered for delivery in 1980-81 at a total capital cost of \$61.7 million.

5 During 1979, 70,456 legal immigrants and an estimated 115,100 illegal immigrants entered Hong Kong. 89,967 illegal immigrants were caught of whom 89,562 were returned. In addition to these, 73,692 refugees from Vietnam came to Hong Kong in 1979, plus 751 subsequently reclassified as illegal immigrants. At the end of 1979, 4,395 immigrants were being detained in Prisons Department institutions.

6 To meet these pressures the Immigration Department was expanded dramatically. Its authorized establishment has increased from 1,757 in 1979-80 to 2,570 in the 1980-81 Draft Estimates. Another 500 or so posts may be required during 1980-81. The Draft Estimates provide for expenditure of \$101 million for the Immigration Department, an increase of 68% over the provision in the 1979-80 Approved Estimates. A full review of the Immigration Department is in hand to assist in the assimilation and final deployment of this large number of new posts.

(2) *Defence*

7 The Draft Estimates provide for expenditure of \$928 million on defence<sup>(4)</sup>. As in previous years, this is due principally to the Hong Kong Government's 75% share of the cost of the garrison under the Defence Costs Agreement, and the full costs of certain major reprovisioning work agreed in supplementary programmes. New liabilities reflected in the Draft Estimates include a 75% share<sup>(5)</sup> of the cost of five replacement patrol craft for the

(4)	<i>Approved Estimates</i> 1979-80 (\$ mn)	<i>Draft Estimates</i> 1980-81 (\$ mn)
<i>Auxiliary Medical Service</i>	4	4
<i>Civil Aid Services</i>	8	10
<i>Defence Costs Agreement</i>	390	471
<i>Miscellaneous Measures</i>	35	401
<i>Royal Hong Kong Auxiliary Air Force</i>	7	31
<i>Royal Hong Kong Regiment</i>	9	11
	<u>453</u>	<u>928</u>
(5) <i>R.N. patrol craft:</i>	\$ mn	
<i>Approved commitment</i>	270	
<i>Provision in Draft Estimates</i>	38	

Royal Navy, and an estimated payment<sup>(6)</sup> of \$180 million as the Hong Kong Government's contribution, assessed partly at 75% and partly at 100%, towards the cost of reinforcements to assist the resident garrison and the Police in measures to prevent illegal immigration. The reprovisioning of Lyemun Barracks, Sham Shui Po Camp, Bowring Camp and other sites to be released commenced in 1979, and \$132.7 million is provided in the Draft Estimates for this purpose.

8 It was necessary in 1979-80 to provide an additional fixed wing twin-engined aircraft for the Royal Hong Kong Auxiliary Air Force at a cost of \$3.1 million, and to order three new twin-engined helicopter for delivery in 1980-81, at a cost of \$22.8 million, to replace the three single-engined helicopters, one of which crashed during the year. A further major item of defence expenditure made necessary in 1979-80 was the construction of a new border fence from Sha Tau Kok to Lo Wu, for which \$30 million is provided in the Draft Estimates.

(3) *Education*

9 The Draft Estimates provide for expenditure of \$2,943 million on education<sup>(7)</sup>. This represents 16.3% of total expenditure in 1980-81.

10 In line with the Government's policy that no child should have to travel an unreasonable distance to attend primary school, eight new primary schools are expected to be completed in 1980-81, in conjunction with the development of public housing estates in the new towns and other developing areas. These schools will provide an additional 12,960 places.

11 In the field of special education the provision of hearing tests and educational aptitude tests for Primary 1 pupils, as proposed in the 1977 White Paper 'Integrating the Disabled into the Community: a United Effort', will be fully achieved in 1980-81. It is expected that the full extent of demand for vision tests for the same category of pupils will also be met next year. An additional 3,741 places will be provided in special schools and classes, and in resource classes, bringing the total number of such places to over 26,500. In line with another White Paper recommendation, that the Education Department should assume responsibility for the development of pre-vocational and vocational training for the handicapped, the World Rehabilitation

(6) <i>Reinforcement costs:</i>	\$ mn		
<i>Revised Estimates 1979-80</i>	105		
<i>Draft Estimates 1980-81</i>	180		
(7) <i>Recurrent</i>	\$ mn	<i>Capital</i>	\$ mn
<i>Education Department</i>	338	<i>Public Works Non-Recurrent</i>	131
<i>Education subventions</i>	1,557	<i>Education subventions</i>	91
<i>U.P.G.C.</i>	459	<i>U.P.G.C.</i>	287
<i>Transfer to Student Loan Fund</i>	36	<i>Departmental special</i>	
<i>Student fare subsidies</i>	41	<i>expenditure</i>	3
	<u>2,431</u>		<u>512</u>

Fund Day Centre will be transferred from the Social Welfare Department to the Education Department in August 1980. The aim of the changeover in departmental responsibilities is to ensure that capable handicapped youths are given access to the same standard of vocational training available to the able-bodied.

12 The provision of places in junior secondary forms for all children in the 12-14 age group will be fully achieved in September 1980. In 1978, tuition fees at this level were abolished and this has now been followed by the abolition of tong fai and similar charges in aided and Government schools, with effect from September 1979. Nine years of free education has thus become a reality. At the senior secondary level (Forms IV and V) the Draft Estimates provide for an increase in the number of places in the public sector from approximately 56,000 to 64,000 thereby catering for 29% of the 15-16 age group.

13 Of the total of 360,000 places in secondary schools in the public sector which will become available in the 1980-81 academic year, 57% will be provided in Government and aided schools. Present planning provides for this proportion to rise to 90% by September 1983, by which time the majority of private non-profit-making schools will have come on to full aid and the opening of new schools will permit the phasing out of those bought places in private independent schools which are of an unsatisfactory standard. Revised population projections have necessitated a re-examination of the shortfall in the provision of new secondary school places, and the secondary schools building programme has now increased to 130 schools of which 55 have been completed and 75 are either under construction or in the planning stage.

14 Several significant proposals contained in the 1978 White Paper 'The Development of Senior Secondary and Tertiary Education' have been implemented during the course of 1979-80. These include the first stage of a four-stage scheme to bring those private non-profit-making schools which are willing, and are found to be suitable, onto full subsidy under the Code of Aid for Secondary Schools. Fifty-six schools commenced the conversion process in September 1979, and the Draft Estimates include \$28.5 million in improvement grants to enable these schools to improve the standard of education provided in their junior secondary forms.

15 In September 1979 the Government entered into arrangements with the Baptist and Lingnan Colleges to provide financial assistance towards the cost of certain courses which will contribute to the achievement of Government's overall educational targets. The 1979-80 Approved Estimates provided for the opening of courses at the sixth form level. A further \$5 million is provided in the Draft Estimates to enable full development of these courses plus the opening of new two-year post-Form VI courses in September 1980.

16 In mid-1980 the two universities and the Polytechnic will enter the final year of the triennium 1978-79 to 1980-81. In addition to \$403 million provided in approved recurrent grants (including supplementary grants in respect of the 1978 and 1979 salaries revisions), the Draft Estimates include provision for earmarked recurrent grants totalling \$35.2 million, of which \$19.5 million is for expenses in connection with the setting up of a dental school at the University of Hong Kong. The Dental Teaching Hospital, which will house facilities for the clinical training of dental students, is in an advanced stage of construction and is due for completion in time for the first intake of eighty students in September 1980.

17 The universities and the Polytechnic are committed to major capital works programmes, both in respect of the construction of additional teaching and student amenity buildings, as well as staff quarters and recreational facilities. The Draft Estimates provide \$287 million for the funding of capital items in 1980-81 and it is expected that completion of existing approved programmes will cost a further \$504 million at current prices in later years.

18 A separate Student Loan Fund was set up with effect from 1 February 1980 and it is expected that gross payments of the order of \$53.8 million will be made in loans to students of the universities and the Polytechnic and the approved post-secondary colleges for the 1980-81 academic year. Some \$15.7 million will be recovered in loan repayments during the same period.

(4) *Medical and health services*

19 The Draft Estimates provide for expenditure of \$1,491 million on medical and health services<sup>(8)</sup>. This represents 8.3% of total expenditure in 1980-81.

20 During 1980-81 an additional 1,672 hospital beds will become available in Government and subvented hospitals. Of this total, 1,336 beds will be provided in the new Princess Margaret Hospital Psychiatric Wing. The overall provision of hospital beds, including those in the private sector, is expected to reach 22,000 by 31 March 1981, a figure which represents some 88% of the target requirement as identified by the Medical Development Advisory Committee for 1980-81.

21 Three new Government clinics are expected to be completed in 1980-81, together with a new departmental laundry. Apart from these projects the Draft Estimates also include provision for staff for the commissioning of the new Sha Tin Hospital.

---

(8) <i>Recurrent</i>	<i>\$ mn</i>	<i>Capital</i>	<i>\$ mn</i>
<i>Government Laboratory</i>	9	<i>Public Works Non-Recurrent</i>	203
<i>Medical and Health</i>		<i>Medical subventions</i>	56
<i>Department</i>	802	<i>Departmental special</i>	
<i>Medical subventions</i>	388	<i>expenditure</i>	33
	<u>1,199</u>		<u>292</u>

22 Several major projects are underway in subvented hospitals, namely, a cardiac thoracic centre at Grantham Hospital, and extensions and improvements to the Wong Tai Sin Infirmary, the Caritas Medical Centre and the Yan Chai and Pok Oi Hospitals in the New Territories. A new pathology building at Kwong Wah Hospital is due to open in late 1980. The large number of capital projects now underway is reflected in an increase in expenditure on capital subventions to medical organizations from \$29 million in the 1979-80 Approved Estimates to \$56 million in the Draft Estimates.

23 Funds are provided in the Draft Estimates to enable improvements to be made to the standard hospital diets for patients in Government hospitals. The proposed new dietary scales will provide hospital dieticians with greater flexibility to meet the needs of individual patients. Provision is also included for a further expansion of the community nursing service, including the opening of a new nursing station at Princess Margaret Hospital with five satellite centres in the Tsuen Wan area. A training course for community nurses will supply an additional 75 community nurses per year up to 1984.

24 The School Dental Care Service will come into operation in September 1980 and will gradually be extended to cover all primary school children. The first school dental clinic is located in the MacLehose Dental Centre, where the first group of 30 student dental therapists are in the final year of their training. Four other school dental clinics are planned.

(5) *Social welfare services*

25 The Draft Estimates provide for expenditure of \$792 million on social welfare services<sup>(9)</sup>. This represents 4.4% of total expenditure in 1980-81, and means that expenditure on these services has increased twentyfold during the past decade.

26 The White Paper 'Social Welfare into the 1980s', published in April 1979, proposed improvements and expansion of the scope of benefits under the social security schemes, and of services for the elderly and young people. In addition to proposals which have already been implemented since 1 April 1978<sup>(10)</sup>, in advance of the publication of the White Paper, two further proposals to improve and expand the social security schemes will be implemented with effect from 1 April 1980. These are the introduction of a disability supplement, under the public assistance scheme, for the partially

---

(9) *Including expenditure on the Social Welfare Department, subventions to voluntary agencies, certain miscellaneous subventions and the Legal Aid Department.*

(10) *The following have been implemented with effect from:*

*1 April 1978*

*(a) old age supplement*

*(b) long-term supplement*

*(c) disregard of earnings*

*(d) extension of old age and disability allowances to those living in residential institutions 1 October 1978*

*(e) lowering of qualifying age for old age allowance from 75 to 70.*

disabled, and the extension of the disability allowance scheme to the profoundly deaf. Total expenditure on these two proposals in 1980-81 is estimated at \$8.9 million rising to \$14.7 million in 1984-85<sup>(11)</sup>. In 1980-81 these proposals will enable an estimated 1,000 partially disabled people already in receipt of public assistance to receive improved benefits, and 3,800 profoundly deaf people to become eligible for the disability allowance. The Draft Estimates anticipate expenditure of \$476 million on all forms of social security in 1980-81<sup>(12)</sup>.

27 Sufficient funds have been included in the Draft Estimates to implement proposals to meet the targets set out in the White Paper for improving and expanding services for the elderly and young people<sup>(13)</sup>. The additional annually recurrent expenditure arising from implementation, in 1980-81 onwards, of the White Paper's proposals for improvements and expansion of social security schemes and of services for the elderly and young people, is estimated to be \$73 million by 1984-85<sup>(14)</sup>. During the same five-year period from 1980-81 to 1984-85, capital expenditure, including disbursements from the Lotteries Fund, will total \$189 million at 1979 prices.

(11) Additional expenditure arising from these proposals over the next five years is:

	1980-81 (\$ mn)	1981-82 (\$ mn)	1982-83 (\$ mn)	1983-84 (\$ mn)	1984-85 (\$ mn)
Disability supplement for the partially disabled	1.4	\$=A.4	1.5	1.5	1.5
Disability allowance for the profoundly deaf	7.5	10.6	12.4	12.9	13.2

(12) Total provision for all forms of social security in the Draft Estimates:

	\$ mn
Public assistance	211.3
Special needs allowances:	
Old age allowance	195.2
Disability allowance	<u>69.1</u>
	<u>475.6</u>

These figures do not include provision for compensation for victims of crimes of violence (\$1 million) or for the traffic accident victims assistance scheme (\$18.5 million).

(13) These include:

- (a) in-services for the elderly, the provision of 22 additional home-helpers, 250 additional hostel places and 40 additional places in care and attention homes, and the setting up of one additional home for the aged, two additional multi-service centres and 20 additional social centres; and
- (b) in-services for young people, expanding family life education, the establishment of two additional out-reaching social work teams, and the provision of 27 additional professional social workers for school social work.

(14)	1980-81 (\$ mn)	1981-82 (\$ mn)	1982-83 (\$ mn)	1983-84 (\$ mn)	1984-85 (\$ mn)
Social security: Public assistance	1.4	1.4	1.5	1.5	1.5
Special needs allowances	7.5	10.6	12.4	12.9	13.2
Services for the elderly	6.3	19.7	29.8	38.5	45.7
Services for the young	<u>6.1</u>	<u>9.3</u>	<u>10.4</u>	<u>11.5</u>	<u>12.4</u>
	<u>21.3</u>	<u>41.0</u>	<u>54.1</u>	<u>64.4</u>	<u>72.8</u>



28 A major portion of increased recurrent expenditure will be channelled through social welfare subventions. The Draft Estimates provide \$145 million for this purpose (including \$20 million for rehabilitation services), representing an increase of 24% compared with the approved provision of \$114 million for 1979-80 (including \$15.3 million for rehabilitation services). As in previous years, the bulk of this sum will be disbursed, on the advice of the Social Welfare Advisory Committee, in the form of discretionary grants to voluntary agencies.

(6) *Infrastructure facilities*

(a) *Airport*

29 During the year, the eastern half of Stage I of a multi-storey carpark for 450 cars<sup>(15)</sup>, a new fire station<sup>(16)</sup>, modifications to the existing freight building<sup>(17)</sup> and two new passenger piers with aerobridges<sup>(18)</sup> were completed and put into operation.

30 Construction works currently in progress include a new restaurant and kitchen block, extension of the vehicular podium<sup>(19)</sup>, a new airmail centre<sup>(20)</sup> and refurbishing of the existing terminal building<sup>(21)</sup>, parts of which, including 36 new check-in positions, a baggage handling system for departing passengers and one new arrival baggage reclaim conveyor for arriving passengers, were completed and put into operation.

(b) *Kowloon-Canton Railway*

31 There is provision of \$549 million for twenty-two Railway projects in the Draft Estimates. The total estimated cost of all projects for the modernization and electrification of the Railway is nearly \$2,000 million. Most of

---

(15) Head 72 PWNR: Buildings Subhead 306. Approved project estimate: \$15.50 million; anticipated expenditure to 31 March 1980: \$7.99 million; Draft Estimates for 1980-81: \$0.40 million.

(16) Head 72 PWNR: Buildings Subhead 401. Approved project estimate: \$7.03 million; anticipated expenditure to 31 March 1980: \$6.70 million; Draft Estimates for 1980-81: \$0.18 million.

(17) Head 72 PWNR: Buildings Subhead 303. Approved project estimate: \$4.10 million; anticipated expenditure to 31 March 1980: \$3.99 million; Draft Estimates for 1980-81: \$0.10 million.

(18) Head 72 PWNR: Buildings Subhead 304. Approved project estimate: \$65.0 million; anticipated expenditure to 31 March 1980: \$45.31 million; Draft Estimates for 1980-81: \$16.10 million.

(19) Head 72 PWNR: Buildings Subhead 304. Approved project estimate: \$65.0 million; anticipated expenditure to 31 March 1980: \$45.31 million; Draft Estimates for 1980-81: \$16.10 million.

(20) Head 72 PWNR: Buildings Subhead 755. Approved project estimate: \$13.40 million; anticipated expenditure to 31 March 1980: \$1.10 million; Draft Estimates for 1980-81: \$11.0 million.

(21) Head 72 PWNR: Buildings Subhead 300. Approved project estimate: \$141.14 million; anticipated expenditure to 31 March 1980: \$103.05 million; Draft Estimates for 1980-81: \$10.78 million.

these are related to the double-tracking and electrification of the line from Hung Hom to Lo Wu. Work is well under way on double-tracking from Hung Hom to Tai Po<sup>(22)</sup> with the new double-track tunnel through Beacon Hill<sup>(23)</sup> expected to be completed in early 1981. Consultants have been assigned to undertake the electrification of the Railway<sup>(24)</sup>. The electrical multiple train units have been ordered and progress payments on these during 1980-81 are expected to total \$180 million.

(c) *Highways*

32 Work has begun on the first stage of Victoria Road improvements<sup>(25)</sup>, and on Nathan Road improvements between Salisbury Road and Mong Kok Road associated with M.T.R. permanent reinstatement works<sup>(26)</sup>. Consultants have been retained to study the options for additional cross-harbour facilities<sup>(27)</sup> and for a feasibility study for the Lantau fixed crossing<sup>(28)</sup>, and investigations and preliminary design for a light rail transit system<sup>(29)</sup> have been completed; but no decisions have been reached on any of these three projects. Reclamation for the first stage of the Hong Kong Island eastern corridor<sup>(30)</sup> has been completed and it is hoped to make a start on construction during 1980-81. The construction of the new North Point vehicular ferry pier<sup>(31)</sup> is well under way. Major projects currently in progress include the

- 
- (22) *Head 73 PWN: Engineering Subheads 481 and 490. Approved project estimates: \$122.1 million; anticipated expenditure to 31 March 1980: \$59.10 million; Draft Estimates for 1980-81: \$58.0 million.*
- (23) *Head 73 PWN: Engineering Subhead 488. Approved project estimate: \$97.0 million; anticipated expenditure to 31 March 1980: \$60.68 million; Draft Estimates for 1980-81: \$36.0 million.*
- (24) *Head 73 PWN: Engineering Subhead 493. Approved project estimate: \$662.0 million; anticipated expenditure to 31 March 1980: \$70.42 million; Draft Estimates for 1980-81: \$318.9 million.*
- (25) *Head 73 PWN: Engineering Subhead 669. Approved project estimate: \$12.0 million; anticipated expenditure to 31 March 1980: \$1.33 million; Draft Estimates for 1980-81: \$4.0 million.*
- (26) *Head 73 PWN: Engineering Subhead 744. Approved project estimate: \$5.50 million; anticipated expenditure to 31 March 1980: \$1.64 million; Draft Estimates for 1980-81: \$3.67 million.*
- (27) *Head 73 PWN: Engineering Subhead 726. Approved project estimate: \$6.0 million; anticipated expenditure to 31 March 1980: \$0.60 million; Draft Estimates for 1980-81: \$3.40 million.*
- (28) *Head 73 PWN: Engineering Subhead 882. Approved project estimate: \$34.0 million; anticipated expenditure to 31 March 1980: \$12.92 million; Draft Estimates for 1980-81: \$11.0 million.*
- (29) *Head 73 PWN: Engineering Subhead 725. Approved project estimate: \$9.10 million; anticipated expenditure to 31 March 1980: \$8.70 million; Draft Estimates for 1980-81: \$0.10 million.*
- (30) *Head 73 PWN: Engineering Subhead 652. Approved project estimate: \$373.0 million; anticipated expenditure to 31 March 1980: \$33.10 million; Draft Estimates for 1980-81: \$11.80 million.*
- (31) *Head 73 PWN: Engineering Subhead 431. Approved project estimate: \$22.45 million; anticipated expenditure to 31 March 1980: \$18.71 million; Draft Estimates for 1980-81: \$8.0 million.*

footbridge system at Connaught Road Central<sup>(32)</sup>, the Wong Nai Chung Gap Road/Stubbs Road flyover<sup>(33)</sup> and the elevated link between Pok Fu Lam Road and Connaught Road West<sup>(34)</sup>. Work on the Ap Lei Chau bridge<sup>(35)</sup>, the Aberdeen Tunnel<sup>(36)</sup> and the Canal Road flyover extension<sup>(37)</sup>, all of which will form an important part of the highways network linking the Island to the New Territories, is progressing well. On the Mainland, sections of this network under construction include, in the west, the West Kowloon corridor<sup>(38)</sup>, the Tsuen Wan by-pass<sup>(39)</sup>, the second stage of Tuen Mun Road<sup>(40)</sup>; and in the east, the Airport Tunnel<sup>(41)</sup> and its approach roads.

(d) *Water supplies*

33 The first phase of the project for receiving additional water supply from the East River<sup>(42)</sup> was completed and commissioned on 1 October 1979. The investigation of potential water resources to meet future demand<sup>(43)</sup> continued. Capital expenditure on water supplies in 1980-81 is expected to total \$313 million, compared with a revised estimate for 1979-80 of \$196 million.

---

(32) *Head 73 PWNR: Engineering Subhead 650. Approved project estimate: \$33.72 million; anticipated expenditure to 31 March 1980: \$29.40 million; Draft Estimates for 1980-81: \$6.46 million.*

(33) *Head 73 PWNR: Engineering Subhead 666. Approved project estimate: \$66.70 million; anticipated expenditure to 31 March 1980: \$35.22 million; Draft Estimates for 1980-81: \$34.0 million.*

(34) *Head 73 PWNR: Engineering Subhead 672. Approved project estimate: \$29.03 million; anticipated expenditure to 31 March 1980: \$20.78 million; Draft Estimates for 1980-81: \$15.20 million.*

(35) *Head 73 PWNR: Engineering Subhead 659. Approved project estimate: \$60.0 million; anticipated expenditure to 31 March 1980: \$51.21 million; Draft Estimates for 1980-81: \$3.60 million.*

(36) *Head 73 PWNR: Engineering Subhead 675. Approved project estimate: \$306.0 million; anticipated expenditure to 31 March 1980: \$154.62 million; Draft Estimates for 1980-81: \$105.0 million.*

(37) *Head 73 PWNR: Engineering Subhead 674. Approved project estimate: \$97.0 million; anticipated expenditure to 31 March 1980: \$67.53 million; Draft Estimates for 1980-81: \$15.5 million.*

(38) *Head 73 PWNR: Engineering Subhead 761. Approved project estimate: \$79.0 million; anticipated expenditure to 31 March 1980: \$37.98 million; Draft Estimates for 1980-81: \$8.5 million.*

(39) *Head 74 PWNR: New Towns and Public Housing Subheads 410 and 411. Approved project estimates: \$511.1 million; anticipated expenditure to 31 March 1980: \$45.52 million; Draft Estimates for 1980-81: \$93.54 million.*

(40) *Head 74 PWNR: New Towns and Public Housing Subhead 631. Approved project estimate: \$134.0 million; anticipated expenditure to 31 March 1980: \$44.30 million; Draft Estimates for 1980-81: \$34.0 million.*

(41) *Head 73 PWNR: Engineering Subhead 746. Approved project estimate: \$135.92 million; anticipated expenditure to 31 March 1980: \$107.44 million; Draft Estimates for 1980-81: \$31.0 million.*

(42) *Head 75 PWNR: Waterworks Subhead 853. Approved project estimate: \$147 million; anticipated expenditure to 31 March 1980: \$92.6 million; Draft Estimates for 1980-81: \$45 million.*

(43) *Head 75 PWNR: Waterworks Subhead 859. Approved project estimate: \$19.5 million; anticipated expenditure to 31 March 1980: \$10.4 million; Draft Estimates for 1980-81: \$1.7 million.*

34 Negotiations for a further increase of the water supply from China beyond 1983 were satisfactorily concluded in early 1980, and planning and design work for the reception and transfer facilities to handle the increased supply within the New Territories is now under way. The necessary work is expected to cost about \$800 million, to be implemented over the next 10 to 12 years in step with demand. The first stage of the work is expected to be commissioned initially by 1983 and completed by 1985-86.

(e) *New towns*

35 The Draft Estimates provide for \$1,900 million for the continuing development of the new towns, including \$358 million for land acquisition costs. This exceeds the revised estimate for 1979-80 by 41%. A large proportion of expenditure in 1980-81 will be devoted to the provision of engineering infrastructure and community facilities in line with the policy of making each new town a self-contained entity.

36 In *Tsuen Wan*, the accelerated development of the northern part of the town has continued apace in conjunction with the construction of the Mass Transit Railway depot. The Draft Estimates include about \$213 million for civil engineering, compared with a revised estimate of about \$148 million in 1979-80. In *Sha Tin*, following the completion of major roadworks, priority is being given to the construction of the first stage of a major sewage treatment plant<sup>(44)</sup> and works associated with the double-tracking and electrification of the Kowloon-Canton Railway. Expenditure on civil engineering in 1980-81 is expected to be about \$198 million, compared with a revised estimate of about \$284 million in 1979-80. In *Tuen Mun* and *Tai Po/Fanling/Shek Wu Hui*, land production, roadworks and provision of essential water and sewage treatment services continue to be the main items of development. Expenditure on civil engineering in Tuen Mun is expected to be of the order of \$219 million in 1980-81, compared with a revised estimate of \$181 million in 1979-80. In *Tai Po/Fanling/Shek Wu Hui*, expenditure on civil engineering is expected to be about \$166 million in 1980-81, compared with a revised estimate of \$61 million in 1979-80.

(f) *Mass Transit Railway (M.I.S. and Tsuen Wan Extension)*

37 The cost of the Mass Transit Railway project is estimated at \$9,885 million<sup>(45)</sup>, including a contingency reserve, but excluding profit from property development. This figure allows for cost escalation at 7% per annum, but

---

(44) *Head 74 PWRN: New Towns and Public Housing Subhead 502. Approved project estimate: \$240.4 million; anticipated expenditure to 31 March 1980: \$98.8 million; Draft Estimates for 1980-81: \$58.7 million.*

(45) *Made up of:*

	\$ mn
(a) <i>Modified Initial System</i>	5,800
(b) <i>Tsuen Wan Extension</i>	4,085
	<u>9,885</u>

excludes finance charges. By the end of 1979, the construction of the Modified Initial System had been virtually completed and over 30% of civil engineering work for the construction of the Tsuen Wan Extension had been effected. The first part of the Modified Initial System (Kwun Tong to Shek Kip Mei) was opened on 1 October 1979. By 31 December 1979 all stations in Kowloon were in operation and the whole of the system has been in operation since 12 February this year. The Corporation has let all the major civil engineering and electrical and mechanical engineering contracts for the Tsuen Wan Extension, construction of which began in October 1978. During 1980, the Corporation estimates that it will spend about \$2,000 million, largely on the extension, excluding finance charges.

38 At 31 December 1979, 11,452 shares of \$100,000 each had been issued by the Corporation to the Government. In addition, the Corporation had negotiated \$10,100 million in medium and long-term loans, of which \$4,300 million had been drawn down. It is estimated that by 31 March 1983, outstanding loans guaranteed by the Government will amount to \$5,200 million.

(7) *Public housing and related facilities*

(a) *Introduction*

39 Public housing is defined here as domestic flats (including ancillary commercial facilities) produced by the Housing Department and the Public Works Department for the Housing Authority's rented housing programme, domestic flats for sale produced by the Housing Department for the Government's Home Ownership Scheme and flatted factory units produced by the Housing Department.

40 The following table shows how public housing and related facilities are financed:

<i>Public Housing</i>	<i>Source of funds</i>
(a) Flats (and ancillary commercial facilities) produced by the Public Works Department for the Housing Authority's rented housing programme.	Appropriations from General Revenue reflected in Head 74 Public Works Non-Recurrent: New Towns and Public Housing.
(b) Flats (and ancillary commercial facilities) produced by the Housing Department for the Housing Authority's rented housing programme.	Drawings from the Development Loan Fund, the Housing Authority's own resources and Asian Development Bank loan.
(c) Flats produced by the Housing Department for the Government's Home Ownership Scheme.	Drawings from the Home Ownership Fund.

<i>Public Housing</i>	<i>Source of funds</i>
(d) Commercial facilities in the Home Ownership Scheme.	Drawings from the Development Loan Fund debited to a separately approved allocation.
(e) Flatted factory units	Drawings from the Development Loan Fund debited to a separately approved allocation.

(b) *Actual and forecast production of public housing*

41 In the four years 1976-77 to 1979-80, the Public Works Department and the Housing Authority will have completed 69,845 flats, including 2,579 flats under the Home Ownership Scheme, with a capacity for 424,000 persons. Over the next four years, 1980-81 to 1983-84, a further 142,116 flats are expected to be completed, including 20,410 flats to be built under the Home Ownership Scheme.

42 The annual production figures are:

<i>Year</i>	<i>Housing Authority's rented housing programme (flats)</i>	<i>Home Ownership Scheme (flats)</i>	<i>Total</i>
1976-77 (actual)	9,620	—	9,620
1977-78 (actual)	13,020	—	13,020
1978-79 (actual)	14,130	—	14,130
1979-80 (estimated)	30,496(*)	2,579	33,075
1980-81 (estimated)	28,064	7,893	35,957
1981-82 (estimated)	32,265(*)	2,470	34,735
1982-83 (estimated)	30,112	5,260	35,372
1983-84 (estimated)	31,265	4,787	36,052

Note: (\*) Includes 5,200 flats and 600 flats to be produced by the Public Works Department in 1979-80 and 1981-82 respectively.

43 The revised estimate for 1979-80 of payments from the Home Ownership Fund on the production of the 26,827 flats in Phases I, II, III and IV of the construction programme is \$461 million. The estimate for 1980-81 is \$1,119 million<sup>(46)</sup>. The revised estimate for 1979-80 of drawings from the Development Loan Fund for financing the commercial facilities in Phases I, II and III is \$53 million. The estimate for 1980-81 is \$75 million.

(c) *Housing Authority's rented housing programme*

44 The Public Works Department's revised estimate of expenditure for 1979-80 construction work on those estates on which planning had already started when the new Housing Authority was established on 1 April 1973 is \$52 million, and the estimate for 1980-81 for the completion of construction work on these estates is \$23 million.

(46) See Memorandum Note on the Home Ownership Fund on page 834 of the printed Estimates.

45 The Housing Department's revised estimate of expenditure on construction for the rented housing programme in 1979-80 is \$1,132 million, of which about \$932 million (or 82%) will be met from drawings from the Development Loan Fund. The estimate for 1980-81 is \$1,723 million, of which about \$1,630 million will be met from drawings from the Development Loan Fund.

46 The forecast of production of public housing in paragraph 42 above for the rolled forward four-year programme is based on the Government's aim to achieve an annual level of about 35,000 flats (including flats produced under the Home Ownership Scheme). The financial implications of this aim for drawings from the Development Loan Fund are estimated as follows:

	1980-81	1981-82	1982-83	1983-84	Total 1980-81 to 1983-84
	(flats)	(flats)	(flats)	(flats)	(flats)
Forecast production by Housing Department(*)	28,064 (\$ mn)	31,665 (\$ mn)	30,112 (\$ mn)	31,265 (\$ mn)	121,106 (\$ mn)
Estimated drawings from the Development Loan Fund(**)	1,630	1,561	1,418	1,223	5,832

Notes: (\*) *This forecast excludes production by the Public Works Department and for the Home Ownership Scheme.*

(\*\*) *These estimates include provision for expenditure on contracts relating to production post-1983-84.*

47 At the end of 1979-80, the balance of the existing allocation<sup>(47)</sup> of \$3,966 million from the Development Loan Fund to the Housing Authority's rented housing programme is estimated to be \$2,328 million. The approval of Finance Committee will be sought to replace this balance with a new allocation of \$5,832 million for the rented housing programme alone, for the period 1980-81 to 1983-84.

48 The four-year housing programme is rolled forward annually, on a new price base to be determined, and on the basis of maintaining the production of public housing at an annual level of about 35,000 flats (including flats produced under the Home Ownership Scheme).

(d) *Flatted factory units*

49 During 1979-80, 765 units of flatted factories will have been completed. The revised estimate of expenditure in 1979-80 on the construction of flatted factory units is \$56 million, to be met in full from drawings from the Development Loan Fund. The Housing Department's estimate of demand for flatted factory units in the three years 1980-81 to 1982-83 is 5,601 units, and the forecast of supply for the same period is 7,826 units, of which 1,456 units are expected to be produced during 1980-81. The estimated cost of production is \$342 million, of which \$126 million will be required in 1980-81.

---

(47) *Approved by Finance Committee on 23 May 1979.*

*(e) Summary of expenditure, 1979-80 and 1980-81*

50 The revised estimate for 1979-80 and the estimate for 1980-81 of expenditure on public housing and related facilities, excluding the Housing Authority's own resources, is \$1,583 million and \$3,000 million respectively:

	<i>1979-80</i> <i>Revised</i> <i>Estimates</i> (\$ mn)	<i>1980-81</i> <i>Draft</i> <i>Estimates</i> (\$ mn)
(a) Flats produced by the Public Works Department for the Housing Authority's rented programme	52	23
(b) Flats produced by the Housing Department for the Housing Authority's rented housing programme (drawings from the Development Loan Fund and Asian Development Bank loan)	961	1,657
(c) Flats produced by the Housing Department for the Government's Home Ownership Scheme (drawings from the Home Ownership Fund)	461	1,119
(d) Commercial facilities in the Home Ownership Scheme (drawings from the Development Loan Fund)	53	75
(e) Flatted factory units (drawings from the Development Loan Fund)	56	126
Total	<u>1,583</u>	<u>3,000</u>



*Annex (12)*

SUMMARY OF ACTUAL EXPENDITURE BY MAIN COMPONENTS  
1970-71 TO 1975-76  
(adjusted figures)

	<i>1970-71</i> (\$ mn)	<i>1971-72</i> (\$ mn)	<i>1972-73</i> (\$ mn)	<i>1973-74</i> (\$ mn)	<i>1974-75</i> (\$ mn)	<i>1975-76</i> (\$ mn)
<i>Recurrent Account:</i>						
Personal Emoluments	793	873	1,058	1,336	1,674	1,782
Departmental Other Charges	263	278	341	498	739	781
Public Works Recurrent	105	146	198	224	263	277
Subventions	361	418	551	742	881	950
University and Polytechnic Grants Committee	60	78	97	159	187	217
Defence	70	55	56	56	60	51
Pensions	69	74	97	117	151	166
Public Debt	2	2	2	3	5	9
Miscellaneous	41	49	64	96	215	217
Total Recurrent	1,764	1,973	2,464	3,121	4,175	4,450

Annex (12) cont'd.

SUMMARY OF ACTUAL EXPENDITURE BY MAIN COMPONENTS  
1970-71 TO 1975-76 *contd.*  
(adjusted figures)

	1970-71	1971-72	1972-73	1973-74	1974-75	1975-76
	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)	(\$ mn)
<i>Capital Account:</i>						
Public Works Programme (other than New Towns and Housing)	386	524	764	1,148	1,518	759
Public Works Programme (New Towns and Housing)	—	—	—	—	—	388
Land Acquisition	—	—	—	—	—	—
Transfers to Development Loan Fund for on-lending to the Housing Authority	—	—	—	—	20	125
Transfers to Home Ownership Fund	—	—	—	—	—	—
Subventions:						
Education	25	27	32	55	58	40
Medical	1	3	10	19	10	4
Miscellaneous	—	1	—	—	—	—
University and Polytechnic Grants Committee	33	65	30	26	37	93
Departmental Special Expenditure	35	48	40	50	79	69
Defence Costs Agreement: Capital Works	18	45	51	32	38	44
Defence: Miscellaneous Measures	2	1	1	1	1	2
Other Transfers:						
Emergency Relief Fund	—	4	2	—	2	3
Student Loan Fund	—	—	—	2	—	—
Miscellaneous	28	14	138	80	33	46
Total Capital	528	732	1,068	1,411	1,796	1,573
Total Expenditure	<u>2,292</u>	<u>2,705</u>	<u>3,532</u>	<u>4,642</u>	<u>5,971</u>	<u>6,023</u>

*Annex (12) cont'd.*

SUMMARY OF ACTUAL EXPENDITURE BY MAIN COMPONENTS  
1976-77 TO 1980-81  
(adjusted figures)

	<i>1976-77</i>	<i>1977-78</i>	<i>1978-79</i>	<i>1979-80</i> <i>(Revised</i>	<i>1980-81</i> <i>(Draft</i>
	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>(\$ mn)</i>	<i>Estimates)</i>	<i>Estimates)</i>
<i>Recurrent Account:</i>				<i>(\$ mn)</i>	<i>(\$ mn)</i>
Personal Emoluments	2,135	2,475	2,892	3,560	4,066
Departmental Other Charges	794	844	1,076	1,300	1,545
Public Works Recurrent	287	458	428	578	699
Subventions	1,122	1,327	1,582	1,983	2,250
University and Polytechnic Grants Committee	255	307	348	408	457
Defence	195	270	363	457	440
Pensions	194	234	262	347	367
Public Debt	27	28	29	34	37
Miscellaneous	<u>215</u>	<u>276</u>	<u>328</u>	<u>414</u>	<u>841</u>
Total Recurrent	5,224	6,219	7,308	9,081	10,702

Annex (12) cont'd.

## SUMMARY OF ACTUAL EXPENDITURE BY MAIN COMPONENTS

1976-77 TO 1980-81 *contd.*

(adjusted figures)

	1976-77 (\$ mn)	1977-78 (\$ mn)	1978-79 (\$ mn)	1979-80 (Revised Estimates) (\$ mn)	1980-81 (Draft Estimates) (\$ mn)
<i>Capital Account:</i>					
Public Works Programme (other than New Towns and Housing)	727	753	1,230	1,890	1,817
Public Works Programme (New Towns and Housing)	401	684	1,044	1,348	1,542
Land Acquisition	—	—	—	—	441
Transfers to Development Loan Fund for on-lending to the Housing Authority	—	100	620	1,000	1,831
Transfers to Home Ownership Fund	—	99	284	—	—
Subventions:					
Education	30	39	36	81	91
Medical	2	13	11	23	56
Miscellaneous	—	1	1	2	4
University and Polytechnic Grants Committee	40	25	65	136	288
Departmental Special Expenditure	74	76	105	207	317
Defence Costs Agreement: Capital Works	22	23	38	29	33
Defence: Miscellaneous Measures	17	76	96	172	393
Other Transfers:					
Emergency Relief Fund	2	4	3	10	3
Student Loan Fund	—	—	—	181	36
Miscellaneous	38	46	115	72	475
Total Capital	1,353	1,939	3,648	5,151	7,406
Total Expenditure	<u>6,577</u>	<u>8,158</u>	<u>10,956</u>	<u>14,232</u>	<u>18,028</u>

*Annex (13)*

EXAMPLES OF SALARIES TAX HAVING REGARD TO  
PROPOSED INCREASES IN PERSONAL, CHILD AND  
DEPENDENT PARENT ALLOWANCES

*Example 1—Annual earnings of \$50,000*

	<i>Single</i>	<i>Single</i>	<i>Married</i>	<i>Married</i>	<i>Married</i>
		<i>with two</i>	<i>without</i>	<i>with 2</i>	<i>and 2</i>
		<i>dependent</i>	<i>children</i>	<i>children</i>	<i>dependent</i>
	<i>Single</i>	<i>parents</i>	<i>children</i>	<i>children</i>	<i>parents</i>
	\$	\$	\$	\$	\$
Salary per annum	50,000	50,000	50,000	50,000	50,000
<i>Less:</i> Personal Allowances	<u>15,000</u>	<u>15,000</u>	<u>30,000</u>	<u>30,000</u>	<u>30,000</u>
	35,000	35,000	20,000	20,000	20,000
<i>Less:</i> Child Allowance	—	—	—	9,000	9,000
Dependent Parent Allowance	—	<u>10,000</u>	—	—	<u>10,000</u>
Net Chargeable Income	35,000	25,000	20,000	11,000	1,000
Tax thereon	4,000	2,250	1,500	600	50
Effective Rate	8.0%	4.5%	3.0%	1.2%	0.\$=A%

*Example 2—Annual earnings of \$75,000*

Salary per annum	75,000	75,000	75,000	75,000	75,000
<i>Less:</i> Personal Allowance	<u>15,000</u>	<u>15,000</u>	<u>30,000</u>	<u>30,000</u>	<u>30,000</u>
	60,000	60,000	45,000	45,000	45,000
<i>Less:</i> Child Allowance	—	—	—	9,000	9,000
Dependent Parent Allowance	—	<u>10,000</u>	—	—	<u>10,000</u>
Net Chargeable Income	60,000	50,000	45,000	36,000	26,000
Tax thereon	10,000	7,500	6,250	4,200	2,400
Effective Rate	13.3%	10.0%	8.3%	5.6%	3.2%

*Example 3—Annual earnings of \$125,000*

Salary per annum	<u>125,000</u>	<u>125,000</u>	<u>125,000</u>	<u>125,000</u>	<u>125,000</u>
<i>Less:</i> Personal Allowance	15,000	15,000	30,000	30,000	30,000
	110,000	110,000	95,000	95,000	95,000
<i>Less:</i> Child Allowance	—	—	—	9,000	9,000
Dependent Parent Allowance	—	<u>10,000</u>	—	—	<u>10,000</u>
Net Chargeable Income	110,000	100,000	95,000	86,000	76,000
Tax thereon	18,750	18,750	18,750	16,500	14,000
Effective Rate	15.0%	15.0%	15.0%	13.2%	11.2%

*Annex (13) cont'd.**Example 4—Annual earnings of \$150,000*

	<i>Single</i>	<i>Single</i>	<i>Married</i>	<i>Married</i>	<i>Married</i>
	<i>Single</i>	<i>with two</i>	<i>without</i>	<i>with 2</i>	<i>with 2</i>
	<i>Single</i>	<i>dependent</i>	<i>children</i>	<i>children</i>	<i>children</i>
	<i>parents</i>	<i>parents</i>	<i>and 2</i>	<i>dependent</i>	<i>dependent</i>
	<i>parents</i>	<i>parents</i>	<i>parents</i>	<i>parents</i>	<i>parents</i>
	<i>\$</i>	<i>\$</i>	<i>\$</i>	<i>\$</i>	<i>\$</i>
Salary per annum	150,000	150,000	150,000	150,000	150,000
<i>Less:</i> Personal Allowance	15,000	15,000	30,000	30,000	30,000
	<u>135,000</u>	<u>135,000</u>	<u>120,000</u>	<u>120,000</u>	<u>120,000</u>
<i>Less:</i> Child Allowance	—	—	—	9,000	9,000
Dependent Parent Allowance	—	10,000	—	—	10,000
	<u>135,000</u>	<u>125,000</u>	<u>120,000</u>	<u>111,000</u>	<u>101,000</u>
Net Chargeable Income	135,000	125,000	120,000	111,000	101,000
Tax thereon	22,500	22,500	22,500	22,500	20,250
Effective Rate	15.0%	15.0%	15.0%	15.0%	13.5%

Annex (14)

(1) EFFECT ON SALARIES TAX OF PROPOSED  
INCREASES IN PERSONAL ALLOWANCES*Single person*

<i>Annual income</i>	<i>Present</i>		<i>Proposed</i>	
	<i>Tax payable</i>	<i>Effective rate</i>	<i>Tax payable</i>	<i>Effective rate</i>
<i>\$</i>	<i>\$</i>	<i>%</i>	<i>\$</i>	<i>%</i>
25,000	875	3.5	500	2.0
35,000	2,212	6.3	1,500	4.3
(37,500)	2,625	7.0	1,875	5.0
45,000	4,000	8.9	3,000	6.7
55,000	6,250	11.4	5,000	9.1
65,000	8,750	13.5	7,500	11.5
(75,000)	11,250	15.0	10,000	13.3
(87,500)	13,125	15.0	13,125	15.0

*Married person, with no children*

35,000	600	1.7	250	0.7
45,000	1,800	4.0	1,000	2.2
55,000	3,600	6.6	2,250	4.1
65,000	6,000	9.2	4,000	6.2
(75,000)	8,750	11.7	6,250	8.3
(100,000)	15,000	15.0	12,500	12.5
110,000	16,500	15.0	15,000	13.6
(125,000)	18,750	15.0	18,750	15.0

(2) EFFECT ON SALARIES TAX OF PROPOSED INCREASES IN  
IN PERSONAL & CHILD ALLOWANCES*Single Person, with two children*

<i>Annual income</i>	<i>Present</i>		<i>Proposed</i>	
	<i>Tax payable</i>	<i>Effective rate</i>	<i>Tax payable</i>	<i>Effective rate</i>
<i>\$</i>	<i>\$</i>	<i>%</i>	<i>\$</i>	<i>%</i>
25,000	337	1.4	50	0.2
35,000	1,300	3.7	600	1.7
(37,500)	1,575	4.2	850	2.3
45,000	2,700	6.0	1,650	3.7
55,000	4,600	8.4	3,200	5.8
65,000	7,000	10.8	5,250	8.1
(75,000)	9,500	12.7	7,750	10.3
(92,500)	13,875	15.0	12,125	13.1
100,000	15,000	15.0	14,000	14.0
(110,000)	16,500	15.0	16,500	15.0

*Married Person, with two children*

40,000	475	1.2	50	0.1
50,000	1,575	3.2	600	1.2
60,000	3,300	5.5	1,650	2.8
(75,000)	7,000	9.3	4,200	5.6
85,000	9,500	11.2	6,500	7.7
95,000	12,000	12.6	9,000	9.5
110,000	15,750	14.3	12,750	11.6
(117,500)	17,625	15.0	14,625	12.5
130,000	19,500	15.0	17,750	13.7
(147,500)	22,125	15.0	22,125	15.0

*Annex (14) cont'd.*

(3) EFFECT ON SALARIES TAX OF PROPOSED INCREASES IN  
PERSONAL, CHILD AND DEPENDENT PARENT  
ALLOWANCES

*Single Person, with 2 children and 2 dependent parents*

<i>Annual income</i>	<i>Present</i>		<i>Proposed</i>	
	<i>Tax payable</i>	<i>Effective rate</i>	<i>Tax payable</i>	<i>Effective rate</i>
<i>\$</i>	<i>\$</i>	<i>%</i>	<i>\$</i>	<i>%</i>
35,000	487	1.4	50	0.1
(37,500)	750	2.0	175	0.5
45,000	1,500	3.3	600	1.3
60,000	4,000	6.7	2,400	4.0
75,000	7,500	10.0	5,250	7.0
90,000	11,250	12.5	9,000	10.0
100,000	13,750	13.8	11,500	11.5
(112,500)	16,875	15.0	14,625	13.0
120,000	18,000	15.0	16,500	13.8
(135,000)	20,250	15.0	20,250	15.0

*Married Person, with 2 children and 2 dependent parents*

50,000	750	1.5	50	0.1
60,000	2,025	3.4	600	1.0
(75,000)	5,000	6.7	2,400	3.2
90,000	8,750	9.7	5,250	5.8
100,000	11,250	11.3	7,750	7.8
120,000	16,250	13.5	12,750	10.6
(137,500)	20,625	15.0	17,125	12.5
150,000	22,500	15.0	20,250	13.5
160,000	24,000	15.0	22,750	14.2
(172,500)	25,875	15.0	25,875	15.0



*Annex (15)*

INCOME LEVELS AT WHICH SALARIES TAX PAYERS ENTER  
THE STANDARD RATE ZONE

	<i>Present</i>	<i>Proposed</i>
	\$	\$
Single	75,000	87,500
Married	100,000	125,000
Married + 1 child	110,000	137,500
Married + 2 children	117,500	147,500
Married + 3 children	122,500	155,000
Married + 4 children	125,000	160,000
Married + 5 children	127,500	162,500
Married + 6 children	130,000	165,000
Married + 7 children	131,250	167,500
Married + 8 children	132,500	170,000
Married + 9 children	133,750	172,500
 (Including 2 Dependent Parents)		
Single	95,000	112,500
Married	120,000	150,000
Married + 1 child	130,000	162,500
Married + 2 children	137,500	172,500
Married + 3 children	142,500	180,000
Married + 4 children	145,000	185,000
Married + 5 children	147,500	187,500
Married + 6 children	150,000	190,000
Married + 7 children	151,250	192,500
Married + 8 children	152,500	195,000
Married + 9 children	153,750	197,500