

# OFFICIAL REPORT OF PROCEEDINGS

Wednesday, 1 March 1989

The Council met at half-past Two o'clock

## PRESENT

HIS EXCELLENCY THE GOVERNOR (*PRESIDENT*)  
SIR DAVID CLIVE WILSON, K.C.M.G.

THE HONOURABLE THE CHIEF SECRETARY  
SIR DAVID ROBERT FORD, K.B.E., L.V.O., J.P.

THE HONOURABLE THE FINANCIAL SECRETARY  
MR. PIERS JACOBS, O.B.E., J.P.

THE HONOURABLE ALLEN LEE PENG-FEI, C.B.E., J.P.

THE HONOURABLE DONALD LIAO POON-HUAI, C.B.E., J.P.  
SECRETARY FOR DISTRICT ADMINISTRATION

THE HONOURABLE STEPHEN CHEONG KAM-CHUEN, O.B.E., J.P.

THE HONOURABLE CHEUNG YAN-LUNG, O.B.E., J.P.

THE HONOURABLE MRS. SELINA CHOW LIANG SHUK-YEE, O.B.E., J.P.

THE HONOURABLE MARIA TAM WAI-CHU, C.B.E., J.P.

DR. THE HONOURABLE HENRIETTA IP MAN-HING, O.B.E., J.P.

THE HONOURABLE CHAN YING-LUN, J.P.

THE HONOURABLE MRS. RITA FAN HSU LAI-TAI, O.B.E., J.P.

THE HONOURABLE PETER POON WING-CHEUNG, O.B.E., J.P.

THE HONOURABLE CHENG HON-KWAN, J.P.

THE HONOURABLE CHUNG PUI-LAM, J.P.

THE HONOURABLE HO SAI-CHU, M.B.E., J.P.

THE HONOURABLE HUI YIN-FAT, O.B.E., J.P.

THE HONOURABLE MARTIN LEE CHU-MING, Q.C., J.P.

THE HONOURABLE DAVID LI KWOK-PO, J.P.

THE HONOURABLE NGAI SHIU-KIT, O.B.E., J.P.

THE HONOURABLE PANG CHUN-HOI, M.B.E.

THE HONOURABLE POON CHI-FAI, J.P.

PROF. THE HONOURABLE POON CHUNG-KWONG, J.P.

THE HONOURABLE SZETO WAH

THE HONOURABLE TAI CHIN-WAH, J.P.

THE HONOURABLE MRS. ROSANNA TAM WONG YICK-MING, J.P.

THE HONOURABLE TAM YIU-CHUNG

DR. THE HONOURABLE DANIEL TSE, O.B.E., J.P.

THE HONOURABLE ANDREW WONG WANG-FAT, J.P.

THE HONOURABLE LAU WONG-FAT, M.B.E., J.P.

THE HONOURABLE GRAHAM BARNES, C.B.E., J.P.  
SECRETARY FOR LANDS AND WORKS

THE HONOURABLE RONALD GEORGE BLACKER BRIDGE, O.B.E., J.P.  
SECRETARY FOR EDUCATION AND MANPOWER

THE HONOURABLE MICHAEL LEUNG MAN-KIN, J.P.  
SECRETARY FOR TRANSPORT

THE HONOURABLE EDWARD HO SING-TIN, J.P.

THE HONOURABLE GEOFFREY THOMAS BARNES, J.P.  
SECRETARY FOR SECURITY

THE HONOURABLE PETER TSAO KWANG-YUNG, C.P.M., J.P.  
SECRETARY FOR ADMINISTRATIVE SERVICES AND INFORMATION

THE HONOURABLE CHAU TAK-HAY, J.P.  
SECRETARY FOR HEALTH AND WELFARE

THE HONOURABLE RONALD JOSEPH ARCULLI, J.P.

THE HONOURABLE MARTIN GILBERT BARROW, O.B.E.

THE HONOURABLE PAUL CHENG MING-FUN

THE HONOURABLE MICHAEL CHENG TAK-KIN, J.P.

THE HONOURABLE DAVID CHEUNG CHI-KONG, J.P.

THE HONOURABLE RONALD CHOW MEI-TAK

THE HONOURABLE MRS. NELLIE FONG WONG KUT-MAN, J.P.

THE HONOURABLE MRS. PEGGY LAM, M.B.E., J.P.

THE HONOURABLE DANIEL LAM WAI-KEUNG, J.P.

THE HONOURABLE MRS. MIRIAM LAU KIN-YEE

THE HONOURABLE LAU WAH-SUM, J.P.

DR. THE HONOURABLE LEONG CHE-HUNG

THE HONOURABLE LEUNG WAI-TUNG, J.P.

THE HONOURABLE JAMES DAVID McGREGOR, O.B.E., I.S.O., J.P.

THE HONOURABLE KINGSLEY SIT HO-YIN

THE HONOURABLE MRS. SO CHAU YIM-PING, J.P.

THE HONOURABLE JAMES TIEN PEI-CHUN, J.P.

THE HONOURABLE MRS. ELSIE TU, C.B.E.

THE HONOURABLE PETER WONG HONG-YUEN, J.P.

THE HONOURABLE THE ATTORNEY GENERAL  
MR. JAMES KERR FINDLAY, Q.C., J.P.

## **IN ATTENDANCE**

THE CLERK TO THE LEGISLATIVE COUNCIL  
MR. LAW KAM-SANG

**PAPERS**

The following papers were laid on the table pursuant to Standing Order 14(2):

*Subject**L.N. No.*

Public Health and Municipal Ordinance Public Health and Municipal Services (Public Pleasure Grounds) (Amendment of Fourth Schedule) Order 1989 .....	52/89
Public Health and Municipal Services Ordinance Public Swimming Pools (Designation) Order .....	53/89
Revised Edition of the Laws Ordinance 1965 Revised Edition of the Laws (Correction of Errors) Order 1989 .....	54/89
Interpretation and General Clauses Ordinance Declaration of Change of Title (Deputy Chief Secretary) Notice 1989 .....	55/89
Dutiable Commodities Ordinance Dutiable Commodities (Liquor Licences) (Specification of Fees) (Regional Council Area) Notice 1988 .....	56/89
Interpretation and General Clauses Ordinance Specification of Public Office .....	57/89

## Sessional Papers 1988-89

- No. 58 — Draft Estimates for the year ending 31 March 1990  
Estimates Summaries — General Revenue Account and Fund  
Accounts including Controlling Officers' Report on Heads of  
Expenditure
- No. 59 — Draft Estimates for the year ending 31 March 1990  
Supporting Details  
Section I: General Revenue Account
- No. 60 — Draft Estimates for the year ending 31 March 1990  
Supporting Details  
Section II: Funds

**Government Business**

**First Reading of Bill**

**APPROPRIATION BILL 1989**

*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 1989**

THE FINANCIAL SECRETARY moved the Second Reading of: "A Bill to apply a sum not exceeding \$70,005,834,000 to the service of the financial year ending on 31 March 1990".

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He said: I move the Appropriation Bill 1989 be read the Second time. My task in preparing this year's Budget has been to try to meet the aspirations of the community without exacerbating the current inflationary situation or placing in jeopardy our prosperity in the longer term.

2. There are three key factors which I have had to take into account: first, inflation; secondly, the accumulation of substantial budget surpluses; and thirdly, the need to embark upon a major programme of infrastructural works to enable Hong Kong to develop in the 1990's and beyond.

3. I shall have more to say about all three, but Members might find it useful if I make some preliminary comment on their inter-relationship. In so doing, I shall set the scene for the presentation of my Budget.

4. The inflation we are experiencing is caused by the very success of our economy. Quite simply, demand for various resources, including labour, is outstripping supply. This strong demand is being translated into higher prices and costs of production. In due course, the economy will adjust and inflationary pressures will ease. But in the meantime, we must endeavour to ensure that our policies do not make matters worse.

5. The accumulation of budget surpluses, while appropriate in an inflationary situation, does create other problems. There is an understandable expectation by the public that the surpluses should be used to fund new or improved services. My colleagues within the Administration who provide these services are naturally keen to respond positively. However, given that the economy is already operating at full capacity, if the Government were to reduce the surpluses by increasing its expenditure substantially, inflationary pressures would be intensified.

6. If expenditure is not to increase, then there will no doubt be calls to reduce the surpluses by introducing tax concessions. But tax concessions themselves can be just as inflationary as increased government expenditure.

7. This brings me to the third factor that I have mentioned; the need to provide for a number of large and expensive infrastructural developments. The dilemma, of course, is that rapidly increasing expenditure on capital works runs counter to my conclusions on expenditure generally. But we simply cannot afford to delay unduly the upgrading of our infrastructural framework if Hong Kong's economy is to continue to develop in the years ahead.

8. These, then, are the major conflicting pressures that I have had to reconcile in the formulation of the Budget for 1989-90. The task has been complex and the solutions I have adopted inevitably represent a compromise. I remain acutely aware of the need for stability and continuity in the management of our public finances.

9. I shall now start by describing the performance of the economy in 1988.

THE ECONOMY IN 1988<sup>1</sup>

10. Following two consecutive years of double-digit growth, the economy slowed down to a more moderate pace last year. It is estimated that our gross domestic product (GDP) grew by about 7.5% in real terms in 1988<sup>2</sup>. This compares with about 14% in 1987<sup>3</sup>

11. The economy escaped largely unscathed from the stock market crash in October 1987, and business confidence had generally returned by the early part of 1988. The slow-down in economic growth can thus be attributed mainly to supply-side constraints. As Members are well aware, the labour market remained tight, with the unemployment rate falling to a record low of 1.3 % in the fourth quarter of the year. As the economy continued to operate virtually at full capacity, keen competition for resources drove up costs.

12. In overall terms, our external sector performed remarkably well. The single most noteworthy feature has been the development of our re-export trade, and in 1988, re-exports overtook domestic exports. Our role as an entrepot serving China and the Asia-Pacific region has again become of major significance. As regards domestic exports, substantial increases were attained in China, the United Kingdom and Japan, while we experienced a decline in respect of the United States market. We are thus witnessing the continuation of a useful diversification of our markets.

<sup>1</sup> See '1988 Economic Background' for further details.

<sup>2</sup> This is a preliminary estimate. Unless otherwise indicated all growth rates for the economy are in real terms. The growth rates of the various major components of expenditure on the GDP in 1988 are as follows:

		%
Private consumption expenditure		7.8
Government consumption expenditure		6.0
Gross domestic fixed capital formation		5.5
of which, building and construction	-0.1	
plant and equipment	12.6	
Total exports of goods		26.3
domestic exports	8.9	
re-exports	45.7	
Imports of goods		26.6
Net exports of services		15.5
Gross domestic product		7.4

<sup>3</sup> This is a provisional estimate.

Imports also rose rapidly, with the result that our visible trade account showed a larger deficit last year than in 1987<sup>4</sup>

13. Domestic demand continued to be boosted mainly by consumer spending and by investment in plant and equipment. In national accounts terms, public sector expenditure grew more slowly than that of the private sector<sup>5</sup>. Let me add that, in the current inflationary situation, there is particular merit in seeking to keep down the share of available resources absorbed by the public sector.

14. As domestic exports grew by nearly 9 % while domestic demand grew by about 7 %, the forces driving economic growth in 1988 were more balanced than in the previous two years<sup>6</sup>. However, the growth rate of demand exceeded that of output<sup>7</sup>.

<sup>4</sup> Hong Kong's visible trade in 1988:

	\$ million	% increase in money terms
Domestic exports	217,664	11.5
Re-exports	275,405	50.7
Total exports	493,069	30.4
Imports*	501,174	31.9
Visible trade balance	-8,105	
Visible trade deficit as a percentage of the total value of imports of goods		1.6% <sup>+</sup>

\* including an estimate of imports of gold for industrial and commercial use.

+ 0.5% in 1987

<sup>5</sup> Public sector expenditure in national accounts terms differs from that shown in the Consolidated Account. Details of the difference are given in Appendix A. In national accounts terms, public sector expenditure grew by 4.2% in 1988; the corresponding growth rate of private sector expenditure was 7.5%.

Growth rates (%):	1986	1987	1988
Domestic exports	16.1	23.1	8.9
Domestic demand	10.1	11.9	7.2

<sup>7</sup> Growth rates in 1988 (%):

Total final demand	17.3
Total final demand (excluding re-exports)	8.7
Gross Domestic Product	7.4

Thus, with full employment, not only was there a deficit on visible trade, but also the rate of inflation increased during the year<sup>8</sup>.

*Inflation*

15. Indeed, one of the main problems we have to face is inflation. During the Budget Debate last year I shared Members' concern that there was a risk that inflation would rise, and my forecast of an average rise in consumer prices of 7 % reflected this. In the event, consumer prices in 1988 rose by 7.5 %<sup>9</sup>. For Hong Kong, this is high. And I am aware that for some the increase in the cost of living may be even higher, having regard to personal spending patterns. It is, therefore, appropriate that I should devote some time to discussing this important issue, which touches every member of our community.

16. Over the past three years we have enjoyed a remarkable period of sustained economic growth. In real terms, GDP has increased by 11 % per annum on average. This growth has been largely export led. Our domestic exports have remained highly competitive internationally, and have grown by an average of 16 % per annum over the past three years. Re-exports have increased by an average of 34 % per annum over the same period.

17. To meet this export demand and the additional domestic demand associated with it, the economy has expanded rapidly and unemployment has fallen to an historic low. The resultant overheating has led to an increase in inflation. Then there is the effect of inflation elsewhere.

18. Some have expressed concern about the impact on our economy of inflation in China. While China's inflation is running ahead of that in Hong Kong, so far this has had only a limited effect on prices here. Import prices of Chinese goods increased by about 1.5 % in 1988 and although at the retail level the prices of Chinese goods rose more rapidly than this, the increases were not significantly out of line with those of goods from other sources, both domestically produced and imported.

19. As I intimated earlier, inflation is part of the economy's adjustment process. If the growth rate of demand outruns the growth rate of supply, wages and prices rise. This process can be accommodated within the economy for a while. But as inflation

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<sup>8</sup> Year-on-year rates of increase in the CPI(A) (%):

1988	Q1	6.8
	Q2	7.0
	Q3	8.1
	Q4	7.9
Average		7.5

<sup>9</sup> According to the CPI(A), the most broadly-based measure of consumer prices.

feeds through to export prices, the competitiveness of our products will be reduced. This reduction in competitiveness should slow down the growth rate of exports, which in turn will ease the inflationary pressure and thus inflation itself.

20. There are signs that this adjustment process is already underway, in the sense that the growth rate of demand was lower in 1988 than in 1987<sup>10</sup>. The adjustment process has, however, not gone as far as was implicit in my budget forecast last year for the growth rate of the economy. Domestic inflation has not yet been fully reflected in the rate of increase of export prices, and as a result, domestic exports have grown more strongly than expected.

21. There appear to be a number of reasons for this. The prices of imported raw materials and semi-manufactures have been rising quite slowly<sup>11</sup>. Furthermore, the transfer of some or all of their production processes to China has enabled a number of manufacturers to hold down their costs. In addition, market pressures, especially in overseas markets with weak demand, appear to have resulted in some exporters being prepared to accept narrower profit margins in defence of their market share.

22. What, then, can we do to curb inflation? The plain fact of the matter is that there are few viable policy options open to a small, externally-oriented economy like ours.

23. On the monetary side, as far as possible, interest rates should be kept high. But it is important to recognize that what we can do in this area is constrained by the over-riding need to ensure exchange rate stability within the linked exchange rate system. Hong Kong dollar interest rates generally have to follow those of the US dollar. In recent months, US dollar interest rates have firmed up significantly in response to the threat of higher inflation in the United States. They seem likely to remain high for the time being. If so, this would be of some help to us in curbing inflation.

24. On the fiscal side there is again little scope for action primarily because the small size of the public sector and the openness of the economy limit the leverage that can be exerted through changing either tax rates or the level of public expenditure. Nevertheless, it is necessary for the Government to ensure that its actions help rather than exacerbate the situation. In this respect, running a larger than planned budget

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<sup>10</sup> Growth rate of total final demand (%):

	<i>including re-exports</i>	<i>excluding re-exports</i>
1986	12.8	12.6
1987	21.9	16.2
1988	17.3	8.7

<sup>11</sup> Prices of retained imports of raw materials and semi-manufactures were, on average, about 5% higher in 1988 than in 1987.

surplus in the current year is, in economic terms, entirely the right course to take in the face of the inflationary pressures. In our present circumstances, increased public sector expenditure is acceptable only so long as the increase is manageable, and only so long as revenue rises more rapidly, with the result that, overall, the Government is removing spending power from the economy<sup>12</sup>.

25. So, beyond keeping our own house in order, there is only a limited amount we can do to alleviate inflation. In due course, possibly over a longer period of time than we would wish, the economy will adjust. To indicate how I see this adjustment taking place, I turn now to the prospects for our economy in 1989.

### ECONOMIC PROSPECTS FOR 1989<sup>13</sup>

26. With the momentum in the latter part of 1988 expected to continue at least through the first half of 1989, the economy should be able to enjoy another year of satisfactory growth. However, because we remain up against capacity constraints, I expect the GDP growth rate for this year to be somewhat below that achieved last year.

27. The major markets for our domestic exports are expected to show a mixed performance. Domestic exports to the United States may pick up somewhat, but those to the Federal Republic of Germany are expected to remain sluggish. Re-exports should continue to increase, partly because of the expansion of output processing activities and partly because of the fast growth in indirect trade between China and some of the other industrializing economies in the region. Overall, I expect domestic exports to rise by 7 % and re-exports by 22% this year. In addition, trade in services should continue to contribute significantly to economic growth.

28. In the domestic sector, private consumption expenditure should remain buoyant. Investment in plant and equipment should also increase, but probably more moderately than in the past two years. Building and construction output will continue to be affected by capacity constraints. The growth rate of government consumption expenditure in national accounts terms is expected to remain below that of the GDP.

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<sup>12</sup> If GDP in money terms rises faster than expected, spending power is removed from the economy automatically. Growth in government expenditure is constrained by financial control while the structure of our revenue system means that revenue rises sharply in response to faster economic growth and to higher inflation.

<sup>13</sup> See "1989 Economic Prospects" for further details.

29. Bearing in mind the uncertainties inherent in economic forecasting, I expect a 6% growth in the GDP for 1989<sup>14</sup>.

30. I should like to draw Members' attention to some of the implications of this forecast. First, as in 1988, a fairly close balance is expected to be maintained between the growth rates of domestic demand and external demand<sup>15</sup>. However, given the pressure of demand on the economy as a whole, it is likely that more imports will be required and that the visible trade deficit will increase<sup>16</sup>.

31. Secondly, considerable inflationary pressures still exist, and these will tend to push the inflation rate higher before it begins to fall, probably in the latter part of the year. This year I expect the Consumer Price Index (A) to rise by an average of 8.5%<sup>17</sup>.

32. Thirdly, the labour market is likely to remain tight. The pressure to adopt labour-saving processes and techniques will thus be sustained. While employers are experiencing labour shortages and increased labour costs, it should be remembered that employees as a group should continue to be able to share in the fruits of prosperity through ample job opportunities and better pay.

<sup>14</sup> The forecast growth rates of the various major components of expenditure on the GDP in 1989 are as follows:

		%
Private consumption expenditure		7.0
Government consumption expenditure		4.6
Gross domestic fixed capital formation		5.8
of which, in building and construction	3.0	
in plant and equipment	8.1	
Total exports of goods		15.2
domestic exports	7.0	
re-exports	22.0	
Imports of goods		15.5
Net exports of services		14.1
 Gross domestic product		 6.0

<sup>15</sup> The forecast growth rate of domestic demand, at 5.9%, is close to that of domestic exports, at 7%.

<sup>16</sup> As an indication of the pressure of demand, total final demand (excluding re-exports) is forecast to increase by 6.9% (11.2% if re-exports are included), which is higher than the growth rate of the GDP, or net output, of 6%. As a result, retained imports are forecast to grow by 9.5% (total imports of goods by 15.5%) and the visible trade deficit to increase from \$8.1 billion to \$12.6 billion.

<sup>17</sup> The forecast rate of increase in the GDP deflator is 9%, and that of the domestic demand deflator is 9.3%. A much faster rate of increase is, however, expected for building and construction costs, at an average of around 20%.

33. Fourthly, as a reflection of growing affluence, per capita GDP in current price terms is expected to rise to US\$11,000. This is a remarkable achievement, of which we can be justly proud<sup>18</sup>.

#### MONETARY ISSUES

34. Before dealing with the public finances, I would like to digress to say a few words about some monetary issues. We have seen in 1988 the introduction of various arrangements helpful to the maintenance of exchange rate stability, and I shall now describe briefly some of the more significant. I shall also outline our current thinking in relation to the development of the local financial markets.

35. In the early part of last year, the Hong Kong Association of Banks introduced the Specified Rate Rules and the subsequent amendments to the Rules on Interest Rates in order to make it possible to have negative interest rates should the need arise. In July, the Government introduced the New Accounting Arrangements, which enabled the Administration to exert more effective influence on monetary conditions in the interbank market. I am grateful to all in the banking community who have contributed towards putting together these arrangements. Those involved have given a clear demonstration of their support to our firm policy of maintaining exchange rate stability and of their commitment to ensuring the general stability of our monetary system.

36. When intervention through the New Accounting Arrangements is necessary, money market operations are carried out and the market informed. So far, these operations have taken the form of direct borrowing or lending, and the buying or selling of foreign currency. The same effect could be achieved through the buying or selling of Hong Kong dollar financial assets of acceptable quality. In other financial centres these assets are usually in the form of debt instruments issued by the Government. Such instruments provide a flexible, low-risk, and possibly more cost-effective alternative for conducting money market operations. But there is in Hong Kong a lack of such instruments because there is virtually no government debt.

37. We have carried out a study of this matter, and there has been informal consultation with the Hong Kong Capital Markets Association and with leading banks. I have also sought the advice of the Exchange Fund Advisory Committee. Following upon this consultation and advice, my present intention is to develop a programme for the issue of short-term Exchange Fund bills. The bills would constitute direct, unsecured, unconditional and general obligations of the Government for the account of the Exchange Fund. Given that the bills would be used for monetary purposes, they would be for the account of the Exchange Fund and not for the general revenue as is the case for Treasury bills elsewhere. I must emphasize that the proceeds could not be

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<sup>18</sup> Per capita GDP is forecast to increase by 14.3% in money terms, or 4.8% in real terms. At current prices, it would amount to \$85,600, or about US\$11,000, in 1989.

used for the purpose of financing fiscal deficits or public expenditure. They would be suitably invested along with other assets of the Exchange Fund and would be available only for those purposes for which the resources of that Fund may properly be used. In other words, we would not be borrowing to finance public expenditure.

38. Operational details are still being worked out. There will need to be further discussion with potential market makers and market participants on secondary market development, which I regard as being of some importance. Before we started issuing such bills I would make a further statement in this Council.

39. Our policy has always been to leave the initiative of market development to those who deal in the market itself. But where fiscal or institutional factors are identified as inhibiting development, we are prepared to consider appropriate modifications. This policy remains unchanged.

40. The under-developed state of the Hong Kong dollar paper market has been attributed by some market participants not only to the lack of government debt but also to the incidence of interest tax. The issue of Exchange Fund bills, as I have explained, should be helpful to the development of this market. Furthermore, I have considered the difficult question of interest tax and I shall come back to this latter subject when presenting my revenue proposals.

41. Lastly, in relation to monetary issues, I intend to seek amendments to the Protection of Investors Ordinance in order to streamline the authorization procedures for advertisements concerning the issue of commercial paper and for the issue of certificates of deposit. We are in the process of consulting the parties concerned and, subject to the advice of the Executive Council, I hope to be able to introduce a Bill into this Council in the not too distant future.

42. So, without undue drama, I am seeking to create a more favourable environment for the development of the Hong Kong dollar paper market. Of course, those who use the market must themselves decide on where the market goes from here. My task is to remove impediments to healthy growth.

#### PRESENT STATE OF PUBLIC FINANCES AND REVISED ESTIMATES 1988-89

43. I turn now to the present state of our public finances. The revenue out-turn at the end of 1988-89 will be significantly higher than forecast, while for the first time for some years expenditure will also exceed the forecast.

44. General Revenue Account expenditure, excluding transfers to funds, of \$43.3 billion exceeds the original estimate by about 2 %; the bulk of the increase is due to the implementation of the "Rennie" report on pay for the disciplined services<sup>19</sup>.

45. The revised estimate of expenditure on General Revenue Account of \$49.6 billion, including transfers to funds, is close to the original estimate. The transfer of \$1.1 billion to the Development Loan Fund allowed for in the original estimate will not now be made because the revised financial arrangements with the Housing Authority have reduced that authority's drawings on the fund.

46. Expenditure of \$14.5 billion from our various funds is about 12 % above budget. This considerable increase was caused largely by the revised financial arrangements with the Housing Authority, which required the handing over to the authority of the balance on the Home Ownership Fund. Other increases in fund expenditure were from the Capital Works Reserve Fund, because of higher than expected cost increases in the construction industry and some acceleration of capital projects.

47. Spending in cash terms from the General Revenue Account and from the funds together is likely to be about 20 % above the actual figure for 1987-88 and about 4 % above the original estimates.

48. Consolidated Account expenditure, which includes Housing Authority and Urban and Regional Councils expenditure, is in cash terms expected to be about 22 % above the actual figure for 1987-88. Expressed in real terms the increase is about 9 % compared with an original estimate of 7 %.

<sup>19</sup>

*Expenditure from General Revenue Account and from the Funds*

	<i>EXPENDITURE 1988-89 \$M</i>	
	<i>REVISED ESTIMATE</i>	<i>ORIGINAL ESTIMATE</i>
<i>General Revenue Account</i>	49,610	49,976
<i>Less transfers to Funds</i>	<u>6,310</u>	<u>7,410</u>
	43,300	42,566
<i>Capital Works Reserve Fund</i>	10,905	10,180
<i>Development Loan Fund</i>	580	1,790
<i>Home Ownership Fund</i>	2,795	800
<i>Mass Transit Fund</i>	90	95
<i>Student Loan Fund</i>	<u>110</u>	<u>109</u>
<i>Total – Funds</i>	14,480	12,974
<i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>	57,780	55,540

49. The growth in the establishment of the Civil Service is about 3.3 %. This is still in excess of our guideline of 2.5 %, and we must continue our efforts to control the size of the Civil Service as well as overall expenditure<sup>20</sup>.

50. On the revenue side, the higher than expected out-turn is particularly noteworthy. In preparing the 1988-89 estimate we made allowance for the anticipated effects of the events of October 1987. As I have already said, those events had remarkably little impact. Furthermore, the estimate was based on a GDP growth of around 14 % in 1987 and 5 % in 1988. The GDP grew faster in 1988 than expected, and the revised estimate for general revenue exceeds the budget by about 21 %.

51. Revenue for the account of the various funds is now expected to be about 7 % below the estimate mainly because revenue which was expected to accrue to the Home Ownership Fund will now accrue to the Housing Authority. But this reduction was largely offset by higher than expected proceeds from land sales. Combining General Revenue Account and fund account revenue the increase on the original budget is 18%<sup>21</sup>.

<sup>20</sup>

*Growth in the Civil Service*

	<i>Posts</i>	<i>Strength</i>
31.3.87	185,682 + 2.3%	179,986 + 2.0%
31.3.88	191,830 + 3.3%	183,654 + 2.0%
31.3.89 (Estimate)	198,240 + 3.3%	
31.3.90 (Estimate)	206,000 + 3.9%	

<sup>21</sup>

*Revenue to the General Revenue Account and to the Funds*

	<i>REVENUE 1988-89 \$M</i>	
	<i>REVISED ESTIMATE</i>	<i>ORIGINAL ESTIMATE</i>
<i>General Revenue Account</i>	65,130	53,740
<i>Capital Works Reserve Fund</i>	6,340	4,480
<i>Development Loan Fund</i>	415	786
<i>Home Ownership Fund</i>	--	1,981
<i>Mass Transit Fund</i>	--	--
<i>Student Loan Fund</i>	<u>85</u>	<u>83</u>
<i>Total - Funds*</i>	6,840	7,330
<i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>	71,970	61,070

\* Excluding transfers from General Revenue Account.

52. On the basis of this increased revenue out-turn, and despite expenditure being above the estimate, I expect an overall surplus in 1988-89 of \$14.2 billion compared with a budgetted surplus of \$5.5 billion<sup>22</sup>. This substantial surplus, which is clearly more than sufficient to maintain our reserves in real terms, is the product of three years of exceptional economic performance. But it should be seen in the context of our total economic activity during the year; the GDP in 1988 amounted to \$426 billion.

53. In sum, Consolidated Account expenditure in 1988-89 is estimated to be 15.4 % of GDP. Recurrent expenditure absorbed only two-thirds of recurrent revenue, thus leaving a comfortable margin to finance capital expenditure. This enabled about half of our capital expenditure to be so financed, in accordance with our aim of limiting dependency on capital revenue.

54. Here I must add that some disturbing trends are becoming evident. First, growth in public sector expenditure exceeds the growth rate of the economy. Secondly, the growth in civil service establishment remains higher than our target. Thirdly, although recurrent revenue is buoyant, it is increasingly dependent on direct taxes, which are vulnerable to the volatility of the economy.

## STRATEGY FOR PUBLIC FINANCES

55. Against this economic and financial background, I shall now say a few words about my overall strategy for managing the public finances. Central to this strategy is the discipline that public expenditure should be based on the trend growth rate of GDP. In this connection, clearly, the assumptions built into the Medium Range

<sup>22</sup>

### *General Revenue Account and the Funds*

#### *SURPLUS / (DEFICIT) 1988-89 \$M*

	<i>REVISED ESTIMATE</i>		<i>ORIGINAL ESTIMATE</i>
	<i>BEFORE TRANSFERS</i>	<i>AFTER TRANSFERS</i>	<i>(AFTER TRANSFERS)</i>
<i>General Revenue Account</i>	21,830	(6,310)	15,520
<i>Capital Works Reserve Fund</i>	(4,565)	6,200	1,635
<i>Development Loan Fund</i>	(165)	--	(165)
<i>Home Ownership Fund</i>	(2,795)	--	(2,795)
<i>Mass Transit Fund</i>	(90)	100	10
<i>Student Loan Fund</i>	(25)	10	(15)
<i>Total - Funds</i>	(7,640)	6,310	(1,330)
<i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>	14,190	--	14,190
			5,530

Forecast are fundamental<sup>23</sup>. For planning purposes I have, during the current financial year, adjusted the trend growth rate assumption for the forecast period from 5.5% to 6%. Recently, we have experienced particularly rapid economic growth, and we can expect reasonable growth in the next few years. I therefore consider 6% as a trend growth rate to be an appropriate planning assumption.

56. It is inevitable that we will experience considerable year to year variations in revenue, dependent as it is on our economic performance. Notwithstanding this, we seek to maintain stability in public expenditure growth. Such steady growth within our budgetary guidelines is essential to the orderly development and expansion of public services. If we are to manage our finances effectively we need to plan ahead and determine over a period of four or five years the levels of public expenditure that we can sustain without the public sector claiming too great a share of the territory's resources.

57. By establishing budgetary guidelines, we seek to ensure that spending levels are planned by reference to what the economy can support and not by the revenue available. At the same time, there is a need for essential infrastructural development, and this may require us to accept levels of expenditure which from time to time take us outside our guidelines. It must be remembered, however, that capacity constraints in the economy can mean that higher spending translates into higher prices with little real gain.

#### *Strategy for expenditure*

58. I turn now specifically to my strategy for expenditure. Average annual real growth in Consolidated Account expenditure over the forecast period is projected to be 4.8%, which is within the 6% trend growth rate of the GDP. This average is affected to some extent by the phasing of capital expenditure. It also includes a projection of an overall growth rate of 9% in the coming year 1989-90. Furthermore, because there is a tendency to underestimate expenditure in the later years it is possible that the actual average growth rate of expenditure over the forecast period will significantly exceed this figure of 4.8%. Thus, we must continue to monitor carefully the growth in public expenditure. This is particularly so in relation to recurrent expenditure, which is already projected to grow by an average of 5.5% a year over the forecast period.

59. There are obviously implications for staff growth. I have already indicated my concern regarding the growth of the Civil Service. The estimates I shall be presenting make provision for a 3.9% growth in the size of the Civil Service in 1989-90 compared with our target of 2.5% growth per year. We had already planned for increases in staff numbers which are required for new medical facilities and for the build up of the police force, partly to assume the duties of the British garrison. In addition we now have to provide for higher staffing levels in, for example, the

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<sup>23</sup> Appendix A

Immigration Department and the Post Office to meet the increased demand for their services.

60. We have identified probable commitments and requirements for increased expenditure on capital account over the next decade. When consideration was given to the allocation of the resources available to fund new or improved services for the period to 1992-93, the planned level of spending on capital account was increased by \$2 billion in total over the four years up to and including 1992-93. This reduced the additional resources available for recurrent account spending on new or improved services, but I would stress that it should still be possible to make some provision for such services during the period.

61. In the light of the constraints I have described and in order to improve services to the public within available resources, I look to policy Secretaries and controlling officers to carry out a rigorous examination of on-going or baseline expenditure. Over time it is inevitable that some fat accumulates, and periodic dieting is good for health.

62. I might add that during the period of sustained growth we have been experiencing it has been possible to allow more to be spent in real terms on public services. But it is important to ensure that value for money is obtained. I have, in presenting the supporting documents to the Budget, attempted to provide a more complete picture of the pattern of public expenditure. The printed estimates give an analysis of spending by programme area, and for each head of expenditure a report by the controlling officer indicates the extent to which objectives are being met. We will continue to improve this analysis and focus attention on results rather than cash flows.

63. Overall, the profile of total government expenditure indicates that the allocation of resources over the various programme areas has remained fairly steady in recent years. Social services and education make up about 32 % of the total Consolidated Account expenditure, and housing 14 %. Spending on infrastructure accounts for 15%, and on security also 15 %. However, over the forecast period the social services and education programmes are expected to account for an increasing share of resources<sup>24</sup>.

64. Before I describe my strategy for public revenue, I should mention one important matter concerning the establishment of authorities outside the Administration. We continue to look for better means of delivering services to the public. Some services can be more efficiently provided by agencies freed from the Civil Service structure. However, this is not always so. In any event, the hiving off of services should not be interpreted as an abdication of responsibility by the Government. The bodies established will remain a part of the public sector, most will still rely on public funds for their operations and all will be expected to provide their

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<sup>24</sup> *Appendix B*

services to the satisfaction of the community. Management will be autonomous and, I believe, should be more responsive to changing needs.

65. The Housing Authority and the Urban and Regional Councils are already well established and the new Hospitals Authority will be set up next year. As a result, in money terms almost half our public services will be provided by statutory bodies or agencies<sup>25</sup>. But it still remains necessary for the Government to exercise overall financial control and to set objectives and targets.

66. About a year ago, the new financial arrangements for the Housing Authority came into operation. Similar arrangements will be made with other bodies appropriate to their individual circumstances, and we are formulating plans to modify the role of the Development Loan Fund to accommodate such arrangements.

### *Strategy for Revenue*

67. I turn now to my strategy for public revenue. In line with the performance of the economy, our revenue continues to be buoyant. But we cannot expect the rates of economic growth we have seen in the last three years to continue unabated and my plans for revenue are as usual based on an assessment of the position over the next few years. Whilst we must avoid adding to inflationary pressures there is some scope for lowering the tax burden and I shall have more to say about this later. Before I do so, however, I would like to inform Members as to where we stand on that much debated subject -- the sales tax.

68. Last year when discussing the value of a wider and more stable tax base I informed Members that our researches had suggested that a form of sales tax, though probably not at a retail level, best met the criteria that I described. I said that many factors remained to be considered and that more work had to be done. We have now carried out considerably more research and are preparing a consultative document. We should be in a position to issue this document to a number of professional bodies and other organizations towards the middle of this year. The purpose of this consultative document will simply be to enable me to examine, with the assistance of those to whom the document will be issued, the technical aspects of tax diversification and any possible difficulties in my proposals.

69. I am conscious of the fact that the introduction of a sales tax in Hong Kong would represent a fundamental shift in our taxation policies. Nevertheless, I am anxious to reduce our dependence on sources of revenue which are most vulnerable to the vicissitudes of the economy. I shall not go over all the arguments at this stage but I would like to repeat the criteria that I consider must be met if we are to introduce any indirect tax of the nature that I have described. First, such a tax should produce a stable and worthwhile revenue yield at a low tax rate; secondly, it should cause

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<sup>25</sup> In this context, statutory bodies and agencies also include the Kowloon Canton Railway Corporation, the Mass Transit Railway Corporation and government-subsidized educational, medical and other organizations.

minimal distortion to the economy; and thirdly, it should be simple and cheap to administer. The type of sales tax that I am examining is a tax at the wholesale level and our researches so far have indicated that such a tax does, indeed, meet the criteria that I have mentioned.

70. I believe that a wholesale sales tax could bring to Hong Kong some significant benefits. It would give us scope to reduce some existing taxes, both direct and indirect. We must ensure that the present advantages that we enjoy from our tax system are not eroded over time. Members will be aware that the rest of the world is moving towards lower direct taxes.

71. The introduction of a tax such as I have described would have to be carefully timed. At the moment we are suffering from inflation, and in these circumstances I do not believe that we are yet ready for this tax. But the preparatory work must be done now.

#### *The Government's reserves*

72. I shall now say a few words about our reserves. The consolidated reserves are expected to show a balance of about \$60 billion at the end of 1988-89 rising to about \$71 billion at the end of 1989-90 after allowing for the taxation proposals I shall be making this afternoon. The Medium Range Forecast shows that, in the period to 1992-93, although the level of reserves will be more than maintained in real terms over the forecast period, the reserve balances, when expressed as a percentage of annual spending, will fall from 91% to 87%<sup>26</sup>.

73. I am not proposing any guidelines as to what level of reserves is appropriate. We are comfortable but not excessively so. The position has improved since last year when I forecast that the level of reserves as a percentage of annual expenditure would fall to about 65% by 1991-92. Nevertheless, it is wrong to look upon the reserves as a "pot of gold" available to be spent regardless. Our budgetary guidelines are related to the growth of the economy, and not to the size of the reserves. Furthermore, we have to protect our spending programmes against cyclical changes in revenue levels, and we have contingent liabilities which have to be covered<sup>27</sup>.

74. As I have already indicated, we need to make provision for some major infrastructural projects that are likely to start in the years ahead, such as road and rail networks, port development and drainage and sewage projects. Some of these may have to proceed outwith our on-going basic public works programme. Whilst the scope and cost are not yet clear, it is obvious that the Government will be required to make a major financial contribution.

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<sup>26</sup> Appendix A, paragraph 15. A surplus of \$3 billion per annum would maintain the level of reserves in real terms.

<sup>27</sup> See Appendix C for details of contingent liabilities.

75. Also, Sir, as you said in your opening address to this Council last October, it is increasingly clear that Hong Kong is going to need a new airport. This will be a massive undertaking. It will, of course, involve not only the airport itself, but also a vast amount of infrastructural development including roads, tunnels, possibly bridges and perhaps a railway link. Our studies, including our examination into the financial and institutional arrangements, are progressing well, and we expect to be in a position to announce a decision before the end of this year.

76. The time has come when we should begin putting some money aside. In order to anticipate some of the considerable expenditure involved on infrastructural development, I propose, beginning in the forthcoming financial year, 1989-90, to make regular transfers from the General Revenue Account to appropriate funds. In this way we will be earmarking some of our accumulating surpluses to finance our infrastructural development programme over the next 10 to 15 years. The detailed accounting arrangements are not yet finalized but I envisage transfers both to the Capital Works Reserve Fund in respect of those projects which will be a part of the public works programme, and also to a new fund for investment in those projects which might attract the private sector or which might be implemented by statutory authorities.

77. These transfers, which will be in addition to the transfers we normally make to the various funds, will not alter the overall consolidated reserve balance. They are, however, a clear indication of our intentions. After these transfers, the unassigned reserves will still provide cover for our contingent liabilities and protection against short-term cash flow fluctuations, and will assist in maintaining fiscal stability.

#### DRAFT ESTIMATES 1989-90

78. I now present the draft estimates of expenditure and revenue for 1989-90.

##### *Draft estimates of expenditure*

79. The draft estimates show expenditure on General Revenue Account, including transfers to funds, of \$70 billion. Expenditure on our various funds is estimated to be \$16.8 billion. Total government expenditure excluding transfers to funds is estimated

to be 19 % above the revised estimate for 1988-89<sup>28</sup>. The estimate of \$70 billion for General Revenue Account includes \$4.3 billion for additional commitments to cover those items of expenditure which either cannot be foreseen or are likely to arise but for which we do not yet have firm estimates of cost.

80. Total Consolidated Account expenditure is expected to grow by 9 % in real terms<sup>29</sup>. This is three percentage points above our guideline, namely, the trend growth rate of GDP of 6 % over the period of the Medium Range Forecast.

81. The estimates provide for the cost of maintaining existing services, opening new facilities in 1989-90 and meeting increasing demand for government services. I have allowed provision for some new services to be introduced in 1989-90 and a list of the major items is given in an appendix to the printed version of this speech<sup>30</sup>.

82. Expenditure on capital account allows for an increase in spending on the capital works programme, including the clearance of the Kowloon Walled City, on which expenditure is expected to peak in 1989-90. Expenditure on capital programmes is expected to be \$14.5 billion or 33 % higher in cash terms than in 1988-89. A list of the major capital projects due to start in 1989-90 is also given in an appendix to the printed version of this speech<sup>31</sup>.

83. Provision is made for further equity investment in the Housing Authority in 1989-90 and for the redemption of the government bonds for \$1 billion issued in 1984, which are repayable on 9 April this year.

<sup>28</sup> Expenditure from General Revenue Account and from the Funds

	<i>DRAFT EXPENDITURE ESTIMATES 1989-90 \$M</i>	<i>REVISED ESTIMATES 1988-89 \$M</i>	
<i>General Revenue Account</i>	70,005	49,610	
<i>Less transfers to Funds</i>	<u>17,740</u>	<u>6,310</u>	
			52,265
<i>Capital Works Reserve Fund</i>	14,490	10,905	
<i>Development Loan Fund</i>	2,090	580	
<i>Home Ownership Fund</i>	--	2,795	
<i>Mass Transit Fund</i>	90	90	
<i>Student Loan Fund</i>	<u>130</u>	<u>110</u>	
<i>Total – Funds</i>			16,800
			43,300
<i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>			69,065
			14,480
			57,780

<sup>29</sup> Appendix A

<sup>30</sup> Appendix D

<sup>31</sup> Appendix E

84. In terms of Consolidated Account expenditure we plan to spend \$11.9 billion on social services (an increase of 13% in real terms over 1988-89); \$13.1 billion on education (an increase of 5%); and \$10.6 billion on housing (an increase of 5%). Spending in these areas will represent 45% of total expenditure. Expenditure on security, the environment, and the transport, works and water supply group will, taken together, increase by 10%.

85. These increases in expenditure, which I would emphasize are in real terms, represent the Government's continuing efforts to secure an improvement in the living standards of the community, especially of those who rely heavily on public services.

86. As I have already said, the projected growth rate in the Civil Service in 1989-90 is 3.9%<sup>32</sup>. This increase includes about 5 700 posts in the Government alone. Of this increase 40% is for posts in the disciplined services and 25% for the Health and Hospital Services departments.

87. The draft estimates provide for transfers to funds from General Revenue Account totalling \$17.7 billion. Of this, \$10.7 billion will cover the net expenditure on the various funds and will maintain their balances in real terms. I have already spoken of my intention to set aside funds for some of the major infrastructural projects that I have mentioned. For this purpose I am transferring \$7 billion to the Development Loan Fund.

88. As a result of these expenditure estimates, Consolidated Account expenditure as a proportion of GDP will increase from 15.4% in 1988-89 to 16.4%.

#### *Draft estimates of revenue*

89. I turn now to the draft estimates of revenue. General Revenue Account revenue before my budget proposals is estimated to be \$73.4 billion, an increase of about 13%

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<sup>32</sup> In this context, the Civil Service comprises employees in government departments, the Housing Authority and the Urban and Regional Councils.

over 1988-89<sup>33</sup>. Revenue from direct taxes is expected to be 18% above the figure for 1988-89, and for other revenue, 8%.

90. On the basis of this forecast, direct taxes will represent 65% of the total of direct and indirect taxes taken together, compared with 62% in 1988-89 and 60% in 1987-88. Members will note the inexorable trend. Revenue accruing to the various funds is estimated at \$7.8 billion, an increase of about 13% over 1988-89. This is largely accounted for by revenue from expected land sales. Combined revenue on General Revenue Account and the funds will thus be about \$81.2 billion, an increase of 13% over 1988-89.

91. As our tax revenues will continue to reflect our recent economic performance, revenue will remain buoyant next year despite the slow down in the rate of economic growth which I have forecast. Generally, fees and charges will be adjusted in line with inflation.

*Summary of draft estimates*

92. The draft estimates of expenditure and revenue for 1989-90, before revenue measures, indicate a surplus on General Revenue Account of \$3.4 billion and an

<sup>33</sup>

*Revenue to the General Revenue Account and to the Funds*

	<i>DRAFT REVENUE ESTIMATES 1989-90 \$M</i>	<i>REVISED ESTIMATES 1988-89 \$M</i>
<i>General Revenue Account</i>	73,415	65,130
<i>Capital Works Reserve Fund</i>	7,040	6,340
<i>Development Loan Fund</i>	630	415
<i>Home Ownership Fund</i>	--	--
<i>Mass Transit Fund</i>	--	--
<i>Student Loan Fund</i>	<u>90</u>	<u>85</u>
 <i>Total - Funds*</i>	 7,760	 6,840
 <i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>	 81,175	 71,970

\* Excluding transfers from General Revenue Account.

increase in the balances of the funds of \$8.7 billion giving an overall surplus of \$12.1 billion<sup>34</sup>.

## REVENUE MEASURES

93. I have earlier described the features of the economy that I think are particularly relevant in relation to the formulation of my Budget for 1989-90. In putting together my revenue proposals, I have been conscious of the fact that despite the large forecast surplus for the year ahead, there is a need to ensure that the proposals are compatible with the overall economic situation. The package includes a number of revenue raising measures which will yield some \$550 million in 1989-90, equivalent to \$620 million in a full year. This additional revenue is more than offset by tax concessions estimated to cost \$1.1 billion in 1989-90, and \$1.7 billion in a full year<sup>35</sup>. The effect will be to reduce the surplus on General Revenue Account in 1989-90 from \$3.4 billion to \$2.8 billion and the overall surplus from \$12.1 billion to \$11.5 billion.

### *Dutiable commodities*

94. Sir, I shall deal first with dutiable commodities. The principle underlying my proposals remains that specific duty rates should be maintained in real terms by regular small adjustments.

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#### *General Revenue Account and the Funds*

	<i>ESTIMATED SURPLUS / (DEFICIT) 1989-90 (BEFORE REVENUE MEASURES) \$M</i>		
	<i>BEFORE TRANSFERS</i>	<i>TRANSFERS</i>	<i>AFTER TRANSFERS</i>
<i>General Revenue Account</i>	21,150	(17,740)	3,410
<i>Capital Works Reserve Fund</i>	(7,450)	8,800	1,350
<i>Development Loan Fund</i>	(1,460)	8,900	7,440
<i>Home Ownership Fund</i>	--	--	--
<i>Mass Transit Fund</i>	(90)	--	(90)
<i>Student Loan Fund</i>	<u>(40)</u>	<u>40</u>	<u>--</u>
<i>Total – Funds</i>	(9,040)	17,740	8,700
<i>TOTAL (GENERAL REVENUE ACCOUNT + FUNDS)</i>	12,110	--	12,110

<sup>35</sup> Details can be found in Appendix F.

95. The duty rates on hydrocarbon oils, liquor and tobacco were all revised last year<sup>36</sup>. To maintain the revenue yield, I propose to increase the duty rates on these commodities broadly in line with inflation.

96. I am aware that these increases may be criticized by some as adding to inflationary pressures. I consider, however, that the danger of not maintaining specific duty rates is simply that we would be faced with much larger increases at a later date.

*Imported hydrocarbon oils*

97. I propose to increase the duty rate on motor spirit from \$2.55 a litre to \$2.75 a litre, and on diesel oil for road vehicles from \$1.27 a litre to \$1.37 a litre. The refund on diesel oil to the franchised bus companies will remain at 65 cents a litre. I estimate the additional revenue arising from these increases to be some \$143 million in 1989-90.

*Intoxicating liquor and alcohol*

98. This year I have a number of proposals in relation to intoxicating liquor and alcohol. The first concerns beer. Duty on beer is currently assessed on the quantity and the original specific gravity of the product released to the local market. The antiquated procedures involved, which date back to the early years of this century, are cumbersome and expensive to administer, and are not appropriate in today's rapidly expanding beer market.

99. To overcome these problems, I propose that duty be assessed solely on the volume of beer, whether released from a local brewery or imported. I expect both the trade and the Customs and Excise Department to benefit from the improved efficiency and reduced costs this new arrangement will bring. After taking account of the increase required to maintain the revenue yield in real terms, the revised duty rate will be \$220 a hectolitre. I might add that the full duty increase is equivalent to less than one cent on a can of locally brewed beer.

100. My next proposal is to increase the specific duty rate on liqueurs, whisky, gin, rum, vodka and all other spirituous liquors except brandy by \$4 a litre from \$48 to \$52.

101. I also propose to eliminate the differential on specific duty rates, which exists at present, between brandy and all other spirituous liquors, by reducing -- I should say that again -- by reducing the specific duty rate on brandy by \$3 a litre from \$55 to \$52.

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<sup>36</sup> 1988 Budget Speech, paragraphs 75, 76 and 81

102. In order to restore their real value, I propose to increase by 8 % the specific duty rates in respect of champagne and sparkling wines, still wines, cider and perry, non-European type wines and Chinese type spirits.

103. My last proposal in relation to duties on intoxicating liquors and alcohol is to increase the basic rates for ethyl alcohol and methyl alcohol from \$455 to \$490 a hectolitre.

104. Details of the new rates are given in an appendix to the printed version of this speech<sup>37</sup> Assuming no consumer resistance, I estimate the additional revenue yield to be \$21 million in 1989-90.

### *Tobacco*

105. I propose to increase the duty on cigarettes from \$175 to \$190 per 1 000 sticks. The duty on cigars will be increased from \$233 to \$250 a kilogram; on smoking tobacco from \$212 to \$230 a kilogram; and on Chinese prepared tobacco from \$45.50 to \$50.00 a kilogram. Assuming no consumer resistance, I estimate the additional revenue yield to be \$102 million in 1989-90.

### *Fees and charges*

106. I turn now to fees and charges. The policy on fees and charges continues to be that services should generally be paid for by those who use them<sup>38</sup>. For 1989-90, I propose to increase the following fees and charges: first, the business registration fee; secondly, vehicle and driving licence fees; thirdly, deposit-taking company licence and registration fees; and, lastly, passenger embarkation and port related fees.

### *Business registration fees*

107. In my 1987 Budget the business registration fee was increased to \$550<sup>39</sup>. With effect from 1 April 1989, I propose to increase this fee to \$630. The fee will apply to all registered businesses, but small businesses will continue to be granted exemption if their monthly turnover does not exceed certain prescribed limits. I estimate the additional revenue arising from this increase to be some \$37 million in 1989-90. The levy of \$100 for the Protection of Wages on Insolvency Fund is separate and not affected by this proposal.

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<sup>37</sup> Appendix F(1)

<sup>38</sup> Of the 5 310 fees and charges presently collected, 4 147 are set at levels to ensure full cost recovery. The remainder are grouped into six different categories, that is, nominal, subsidized, deterrent, tax-loaded, utilities and others, to each of which different criteria are applied to determine an appropriate level of fee or charge.

<sup>39</sup> 1987 Budget Speech, paragraph 118

*Vehicle and driving licence fees*

108. I propose to increase vehicle registration and driving licence fees by 8 % from the levels set last year. Details are given in an appendix to the printed version of this speech<sup>40</sup>. I estimate the additional revenue arising from these increases to be \$103 million in 1989-90.

*Deposit-taking company licence and registration fees*

109. As revenue from the licensing and registration of deposit-taking companies does not cover the costs of supervision, I propose to increase their licence and registration fees by 15%. The estimated additional yield of \$3 million in 1989-90 will reduce, though not eliminate, the under-recovery of supervision costs. Details of the new fees are given again in an appendix to the printed version of this speech<sup>41</sup>.

*Port related fees*

110. A new vessel traffic management system for the port will be commissioned later this year. Currently, a passenger embarkation fee of \$15 is payable by those departing from the Macau and China Ferry Terminals. To defray in part the costs of installing and operating the new system, I propose to increase this fee by \$2 to \$17. This increase will be implemented when the new vessel traffic management system is commissioned. At the same time, port and light dues will also be increased. I estimate the total additional revenue yield in 1989-90 to be \$14 million, and \$29 million in a full year.

*Other fees and charges*

111. A number of other fees and charges, including water charges, are scheduled for normal review in 1989. From these sources, I expect additional revenue of about \$130 million in 1989-90, and \$180 million in a full year.

*Tax concessions*

112. I turn now to tax concessions. I propose a reduction in the standard rate of tax, increases in personal allowances, increases in child and dependent parent allowances, and the introduction of a new allowance for single parents who are responsible for the care of dependent children. I also propose a reduction in the rate of tax applicable to corporations, an increase in the initial allowance for machinery and plant, and a number of other concessions of relevance to the business community.

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<sup>40</sup> Appendix F(2)

<sup>41</sup> Appendix F(2)

*Personal taxation*

113. For personal taxation, I propose –

first, to reduce the standard rate from 15.5% to 15%;

secondly, that the basic personal allowance be increased from \$29,000 to \$32,000 for a single person, and from \$60,000 to \$66,000 for a married couple. Taken together, the new basic allowance plus the existing additional personal allowance will total \$39,000 for single persons and \$80,000 for married couples; below these income levels there will be no liability to tax. At their maximum levels, the new allowances will be slightly more than 8 % higher than the present combined basic and additional personal allowances<sup>42</sup>;

thirdly, that the child allowance be increased, for a first child, from \$12,000 to \$13,000, and for a second child from \$8,500 to \$9,000;

fourthly, that the allowance for a dependent parent be increased from \$10,000 to \$11,000. The total allowance in respect of a dependent parent who resides with a taxpayer will be \$14,000; and

lastly, I propose that a new allowance of \$20,000 be provided for those parents, such as widows or single parents, who are solely or predominantly responsible for the care of dependent children, but who are currently ineligible for a personal allowance at the higher rate applicable to married persons.

114. I intend to introduce these concessions with effect from the year of assessment commencing 1 April 1989. Therefore, the first occasion on which they will apply will be to provisional and final tax assessments for 1989-90, and also to 1989-90 personal assessments. I estimate that the cost to the revenue in 1989-90 will be about \$465 million, and \$650 million for a full year.

115. Examples of the effects of these personal taxation concessions upon various categories of taxpayers, together with comparative tables, are set out in an appendix to the printed version of this speech<sup>43</sup>.

<sup>42</sup> *The present basic and additional allowances are –*

	<i>Basic Additional</i>	<i>Allowance Allowance</i>	<i>Total</i>
<i>Single</i>	\$29,000	\$ 7,000	\$36,000
<i>Married</i>	\$60,000	\$14,000	\$74,000

<sup>43</sup> *Appendix F(3)*

*Profits tax*

116. I propose a reduction in the rate of tax on corporate profits from 17% to 16.5%. I estimate the cost of the proposed reduction to be \$345 million in 1989-90, and \$695 million in a full year. The new corporate rate of 16.5% will apply to provisional and final assessments for 1989-90.

*Capital allowances*

117. Sir, the initial allowance for expenditure incurred on qualifying machinery and plant was last revised, to 55%, in 1982<sup>44</sup>. In general, I hold the view that it is better to reduce the rate of tax on business profits, leaving it open to businessmen to make their own decisions about investment. However, a more generous reduction in the rate of tax on profits than I have proposed would be inappropriate at this time, having regard to inflationary pressures. I believe, therefore, that this year it is preferable to give an increase in capital allowances by way of direct encouragement, because much of the additional investment expenditure by businesses is likely to be spent on imported goods and should not therefore contribute to inflationary pressures.

118. Accordingly, I propose that the initial allowance be increased from 55% to 60% for qualifying expenditure. The new initial allowance will apply to provisional and final assessments for 1989-90. I estimate the cost to the revenue of this increased allowance to be some \$110 million in 1989-90, and \$150 million in a full year.

*Interest tax*

119. I turn now to the taxation of interest. The Inland Revenue Ordinance provides for an interest withholding tax. Exemptions from this tax were given in 1982 and 1983 respectively to interest on foreign currency deposits and Hong Kong dollar deposits, where these were held with financial institutions. This has resulted in the yield from this tax declining significantly.

120. Against this background, and because the present discrimination between interest paid by financial institutions and interest paid by other entities is said to have inhibited the development of Hong Kong as an international capital and financial market, I propose to simplify our taxation system by the complete abolition of interest tax with effect from the year of assessment commencing 1 April 1989. I estimate the overall cost of this concession to be some \$140 million in 1989-90.

*Profits tax paid by unincorporated businesses; property tax*

121. The reduction in the standard rate of tax will affect the amount of profits tax to be paid by unincorporated businesses, and reduce yields from property tax. Taken together, I estimate that this will cost a further \$40 million in 1989-90, and \$100

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<sup>44</sup> 1982 Budget Speech, paragraph 81

million in a full year. The new standard rate will apply to provisional and final assessments on unincorporated businesses, and to provisional and final property tax assessments, for 1989-90.

### *Stamp duty*

122. A concession on stamp duty was recommended by the Securities Review Committee where the lending and borrowing of share scrip are used as the means of expediting the settlement of transactions. Stock lending and borrowing are internationally accepted methods of resolving legitimate temporary settlement problems. Provided certain safeguards are introduced, I support the committee's recommendation and, subject to the advice of the Executive Council, I shall shortly be introducing a Bill into this Council providing for the exemption from stamp duty of stock lending transactions entered into for this purpose. The full year cost would amount to some \$40 million.

## IMPLEMENTATION

123. My proposals for the business registration fee, deposit-taking company licence and registration fees, dutiable commodities, and vehicle and driving licence fees were the subject of Public Revenue Protection Orders signed by you, Sir, yesterday. During the current Session a Bill to amend the Inland Revenue Ordinance will be introduced into this Council to give effect to the tax concessions proposed. Other increases in fees and charges will be implemented during the year when the relevant costing reviews are completed.

## OTHER TAXATION MATTERS

124. Before concluding, I wish to mention certain other taxation matters.

### *Taxation of married women*

125. First, Members will wish to know what progress is being made on separate taxation for married women. In my speech concluding the debate on last year's Budget, I undertook to introduce separate taxation as soon as practicable, hopefully during 1990<sup>45</sup>. Since then, much work has been done on the necessary administrative and legal arrangements. Subject to the advice of the Executive Council, I hope to be able to put detailed proposals to this Council later this year.

126. Assuming this timetable can be met, it should be possible to give effect to these proposals in final tax assessments for 1989-90.

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<sup>45</sup> *Speech concluding the Debate on the Second Reading of the Appropriation Bill, 1988, paragraphs 48 and 49*

*Unit trusts and mutual funds*

127. Secondly, there have been calls for an amendment to the Inland Revenue Ordinance to alter the definition of securities so that a wider range of profits made by authorized unit trusts is excluded from profits tax. I have also received representations that mutual fund corporations be exempted from profits tax in similar manner to unit trusts. There has already been consultation with the securities industry and we are giving further thought to these proposals.

*Taxation of the shipping industry*

128. Thirdly, as regards taxation on shipping, we have in recent months consulted with the United States authorities as to how the local shipping industry might overcome the problems posed by the 1986 US Tax Reform Act. We have agreed that the best way to resolve the present difficulties is to formalize arrangements for the reciprocal tax exemption of income derived from the international operation of ships. I hope to be in a position to announce details of the arrangements in the not too distant future.

*Venture capital*

129. Lastly, there has been growing interest in Hong Kong in the use of venture capital. This is a form of financing whereby venture capitalists make equity investments in new businesses with growth potential. The major return to the venture capitalist arises when he disposes of his investment. One of the restrictions on the growth of venture capital financing in Hong Kong is said to be the uncertainty which presently exists as to whether profits arising on disinvestment are liable to profits tax. In some other jurisdictions the problem has been resolved by complex legislation. I am always wary of complicating our tax system unnecessarily but I am, nevertheless, giving this matter careful consideration in order to assess whether a suitable concession would be helpful to the further development of industry in Hong Kong.

## SUMMING UP

130. Sir, I began this speech by identifying the three dominant factors which I have had to take into account in preparing my Budget this year; namely, inflation, budget surpluses, and the need to provide for our major infrastructural requirements. Because the situation is complex, I have considered it more important than ever to explain the precise nature of the problems we are facing and the rationale behind my proposals.

131. I have dwelt at some length on the subject of inflation. I have made the point that increased public expenditure in present circumstances runs the risk of fuelling inflation. Tax concessions can have the same effect. I could not, however, rule out all expenditure increases, since that could damage our future economic growth and the well-being of our community. Neither could I rule out all tax concessions, when

clearly the size of the budget surplus leads to strong expectations of some reduction in tax rates. My proposals have been consciously framed with due regard to the risks involved, and I do not believe that this Budget will add significantly to inflation.

132. The reductions I have proposed in the rates of salaries tax and profits tax will restore us to the position which obtained five years ago, when the rates had to be raised in the face of a sharp slowdown in the economy. The restoration has been achieved steadily and without disturbing the stability of our public finances.

133. As to expenditure, I have throughout this speech stressed that activities in the public sector must not be revenue led. We should not spend more simply because we have collected more. The principal consideration must be to establish and then maintain a proper relationship over time between public expenditure and the performance of the economy.

134. There may be occasions when the breaching of our budgetary guidelines can be justified. Some argue that the public sector's share of the economy should be increased to provide the kind of qualitative improvements in services that our economy now expects. But the public sector share of GDP must not be increased to the point where the wealth-producing capacity of the private sector is seriously impaired. I mention this matter not as a precursor to a change in budgetary policy, but as an indication of the problem that we face.

135. It is clear that in order to provide resources for new or improved services, we will have to be increasingly vigorous in our attack on our baseline expenditure. In other words, we must ensure that we make maximum use of the redeployment of existing resources in order to achieve the nature and quality of services that are needed today and in the future. I know that I can rely on policy secretaries and controlling officers to play their part in this task.

136. Sir, I believe this Budget successfully meets the challenge of reconciling the conflicting pressures that I have described. Our direct taxation rates are back to where they were before we faced a deficit in our public finances. Our programme of public expenditure has been maintained, and we have begun to set aside funds towards the considerable infrastructural programme that is vital to our future economic growth. I have proposed other taxation measures designed to promote investment and to stimulate and encourage further the development of Hong Kong as a financial centre and capital market. This is a Budget which I can commend to this Council.

137. Sir, I move the debate on this matter be now 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 pm on Wednesday, 8 March 1989.

*Adjourned accordingly at eighteen minutes to Five o'clock.*

*Note:* The short titles of the Bills listed in the Hansard have been translated into Chinese for information and guidance only; they do not have authoritative effect in Chinese.

**Appendices**

	<i>Page</i>
<b>A. Medium range forecast 1988-89 to 1992-93</b>	1037-1046
Forecasting Government's expenditure and revenue in the period up to 1992-93 and setting these forecasts in a historical context.	
<b>B. Trends in public expenditure 1984-85 to 1992-93</b>	1047-1060
Showing the past and projected allocation of resources between programme areas.	
<b>C. Contingent liabilities</b>	1061
Setting out the more significant contingent liabilities of Government.	
<b>D. The recurrent cost implications of major new or improved services to begin in 1989-90 to 1992-93</b>	1062-1063
Listing new items selected by the Chief Secretary's Committee for implementation in 1989-90 to 1992-93.	
<b>E. Major capital works projects to begin in 1989-90</b>	1064
Listing projects each with a project cost of \$100 million or over budgetted to begin in 1989-90.	
<b>F. Budget revenue measures</b>	1065-1083
Containing further details of the revenue proposals made.	

**MEDIUM RANGE FORECAST 1988-89 TO 1992-93****INTRODUCTION**

The *Medium Range Forecast* (MRF) is Government's planning tool for ensuring that budgetary policy, and in particular expenditure programmes, are developed and implemented within the context of the economy as a whole looking forward over a five year period. It is the starting point from which detailed expenditure programmes and taxation measures are developed and is a reflection of the financial consequences of policy decisions. The MRF is updated regularly.

2 The MRF is for the period 1988-89 to 1992-93 and has been used in the formulation of the 1989-90 budget. It is presented in three sections:

- (I) Forecasting assumptions and budgetary criteria.
- (II) The MRF for 1988-89 to 1992-93.
- (III) Commentary on the MRF in relation to budgetary criteria.

**SECTION I—FORECASTING ASSUMPTIONS AND BUDGETARY CRITERIA**

3 A number of computer based models are used to derive the MRF. These models reflect a wide range of assumptions about the factors determining each of the components of Government's revenue and expenditure. Some are economic in nature (the general economic assumptions) while others deal with specific areas of Government's activity (the detailed assumptions). These are supported by studies of historical and anticipated trends.

**General Economic Assumptions***Growth in Gross Domestic Product (GDP)*

4 There is a clear link between many of Government's major revenue sources and economic growth. For planning purposes the medium range assumption as to annual GDP growth for the current MRF has been set at 6% in real terms.

*Inflation*

5 The inflation rate fell rapidly in 1985 and 1986 but, since mid-1987, has begun to edge upwards. Over the forecast period the average year on year assumption has been increased to 6% (from 5½% in the previous Medium Range Forecast). It is emphasised that this is a *trend* assumption and the prospect in the short term is that actual inflation will exceed this trend.

**Detailed Assumptions**

6 A wide range of detailed assumptions relating to developing expenditure and revenue patterns over the forecast period are taken into account. These include:

- estimated cash flow on capital projects.
- forecast completion dates of these capital projects and their related recurrent consequences in terms of staffing and running costs.
- the expected pattern of demand for individual services.
- the trend in yield from individual revenue sources.
- changes in taxation rates and fees and charges.

**Budgetary Criteria**

7 In addition to the above forecasting assumptions there are a number of criteria against which the results of forecasts are tested for overall acceptability in terms of budgetary policy. Any significant breach of these parameters results in a review of the underlying programmes and adjustments as necessary.

8 The following are the more important budgetary criteria:

*—Total cash flow surplus/deficit*

As a general aim, a cash flow surplus is sought each year to ensure that total reserves in General Revenue Account and in the Funds maintain their value in real terms. On the basis of the current level of reserves an annual surplus of around \$3.0 billion is necessary to achieve this objective.

*—Operating surplus/deficit*

With the reduction in importance of capital revenue from land sales a continuing substantial element of capital expenditure must now be financed from a surplus on operating account (recurrent revenue in relation to recurrent expenditure). A broad target of at least a 50% funding of capital expenditure from the operating surplus is adopted.

*—Total expenditure growth*

It is intended that expenditure growth should not exceed the *trend* assumption as to growth in GDP taking one year with another.

*—Capital expenditure growth*

By its nature some fluctuations in the level of capital expenditure are to be expected. However, taking one year with another the aim is to contain capital expenditure growth within overall expenditure guidelines, i.e. within the *trend* assumption as to GDP growth. Allowance is made for a number of major projects due to start in the forecast period. In planning the size of the capital programme regard is also had to the recurrent consequences of capital works (staffing, maintenance, etc.).

*—Size of the civil service*

This is a significant determinant of the growth rate of Government's expenditure. A target average annual growth of no more than 2½% in the size of the civil service is adopted.

*—Taxation policy*

The projections reflect the taxation measures introduced in this year's budget. Thereafter, no major shifts in the tax burden are assumed. Account is taken, however, of the need to maintain the real yield from fees and charges, fixed duties etc. and to review periodically the various tax thresholds in the light of inflation.

## Appendix A—Contd.

## SECTION II—THE FORECASTS

9 The current MRF is summarised in the following three tables which indicate the forecast operating position, capital cash flow and the aggregation of the two in a consolidated cash flow statement.

10 It is emphasised that the forecasts are based on *trends* and, therefore, the actual results of any individual year may vary significantly from the *trend* assumption. This is particularly so in Hong Kong's volatile economic circumstances.

Operating Statement (before budget revenue measures)

Table 1

	Revised Estimate	Forecast			
		1988-89	1989-90	1990-91	1991-92
	\$m	\$m	\$m	\$m	\$m
Recurrent expenditure	41,780	49,520	55,610	63,390	72,220
Other non-recurrent	790	630	460	160	170
Total operating expenditure	42,570	50,150	56,070	63,550	72,390
Recurrent revenue before interest but before budget revenue measures	61,110	68,170	75,470	84,550	94,270
Operating surplus before interest	18,540	18,020	19,400	21,000	21,880
Interest on balances	2,540	4,410	4,470	5,000	5,740
Operating surplus after interest but before budget revenue measures	21,080	22,430	23,870	26,000	27,620

Capital Expenditure and Financing Statement

Table 2

	Revised Estimate	Forecast			
		1988-89	1989-90	1990-91	1991-92
	\$m	\$m	\$m	\$m	\$m
Capital expenditure					
General Revenue Account	730	1,120	1,100	1,050	1,120
Capital Works Reserve Fund	10,890	14,490	15,280	15,340	16,320
Other funds*	3,580	2,310	5,390	4,810	2,740
Bond issue repayment	—	1,000	—	—	—
Total capital expenditure	15,200	18,920	21,770	21,200	20,180
Capital revenue					
General Revenue Account	1,480	840	890	950	1,020
Capital Works Reserve Fund (land sales and interest)	6,340	7,040	3,080	3,080	3,080
Other funds*	490	720	730	750	760
Total capital revenue	8,310	8,600	4,700	4,780	4,860
Capital financing (deficit)	(6,890)	(10,320)	(17,070)	(16,420)	(15,320)

\* Development Loan Fund, Home Ownership Fund, Mass Transit Fund and Student Loan Fund. The Home Ownership Fund was transferred to the Housing Authority on 1 April 1988.

Appendix A—Contd.

## Consolidated Cash Flow

Table 3

	Revised Estimate	Forecast			
	1988-89	1989-90	1990-91	1991-92	1992-93
	\$m	\$m	\$m	\$m	\$m
Capital financing (deficit)	(6,890)	(10,320)	(17,070)	(16,420)	(15,320)
Operating surplus before budget revenue measures	21,080	22,430	23,870	26,000	27,620
<b>Consolidated cash surplus before budget revenue measures</b>	<b>14,190</b>	<b>12,110</b>	<b>6,800</b>	<b>9,580</b>	<b>12,300</b>
Less: Impact of budget revenue measures*	—	(640)	(2,100)	(2,390)	(2,680)
<b>Consolidated cash surplus after budget revenue measures</b>	<b>14,190</b>	<b>11,470</b>	<b>4,700</b>	<b>7,190</b>	<b>9,620</b>
Reserve balances at 1 April	45,450	59,640	71,110	75,810	83,000
Reserve balances at 31 March	59,640	71,110	75,810	83,000	92,620

\* Including impact on interest on balances.

11 These tables relate to Government's overall finances. They provide no breakdown of the details between General Revenue Account and the various funds through which, for operational reasons, the Government controls its finances.

12 Exceptional factors contributing to the significant increase in capital spending between 1989-90 and 1992-93 shown in these forecasts are repayment of the 1984 bond issue and further injections of equity into the Housing Authority and the Mass Transit Railway Corporation (MTRC). The latter amounts to \$11.7 billion in total which includes \$2.5 billion for the MTRC.

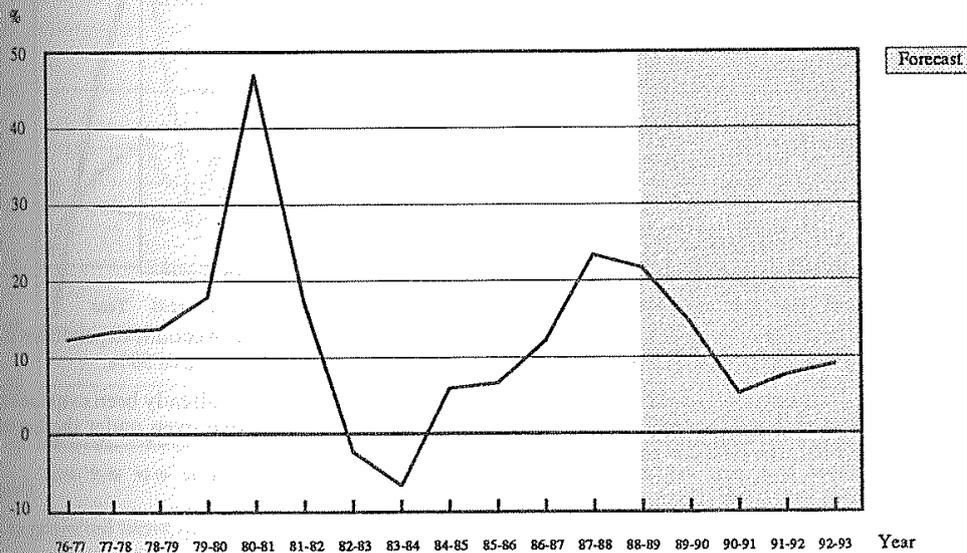
SECTION III—COMMENTARY ON THE FORECAST

The Fiscal Balance

13 Before the 1989-90 taxation measures are taken into account, the forecasts indicate an average consolidated cash flow surplus over the forecast period from 1989-90 to 1992-93 of around \$10.2 billion. This drops to around \$2 billion after the taxation measures proposed in the 1989-90 budget are taken into account. An average surplus of this order is sufficient to ensure that reserve balances are maintained in real terms, provide a cushion for unforeseen events and cover for contingent liabilities. An impression of the relative size of the forecast surplus/deficit can be gained by comparing it with the level of Consolidated Account expenditure<sup>(1)</sup>. The historical and forecast relationship in this respect is illustrated in Diagram 1.

Consolidated Cash Surplus/(Deficit)  
(After 1989-90 Budget Revenue Measures)  
as a Percentage of  
Consolidated Account Expenditure

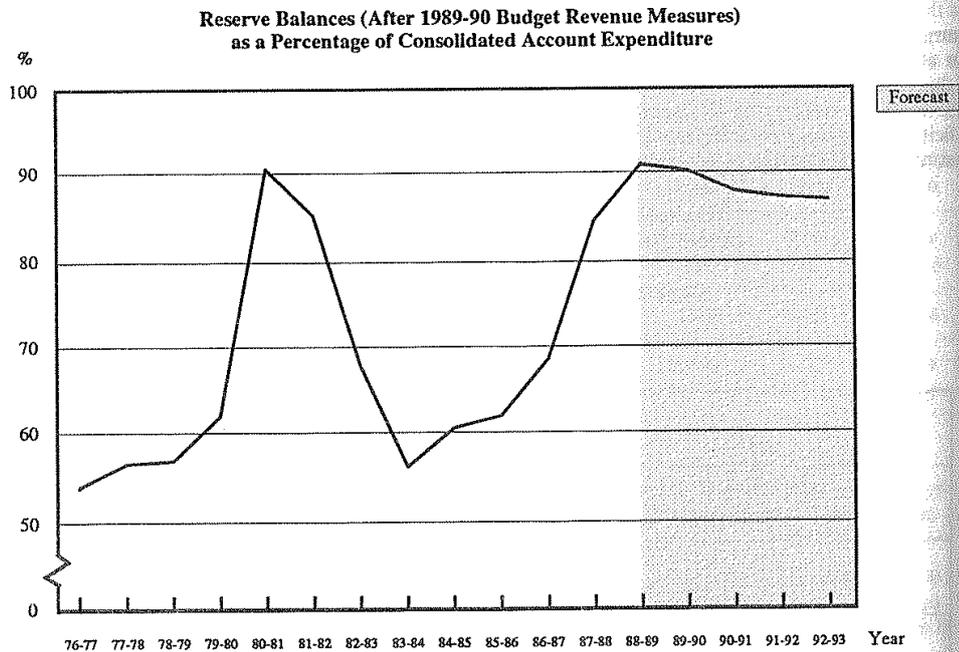
Diagram 1



14 The operating surplus after interest (recurrent revenue over expenditure) is sufficient to finance an average of some 122% of capital expenditure over the forecast period from 1989-90 to 1992-93 before budget revenue measures, but will fall to 112% with the implementation of these measures. This compares with the target of 50%.

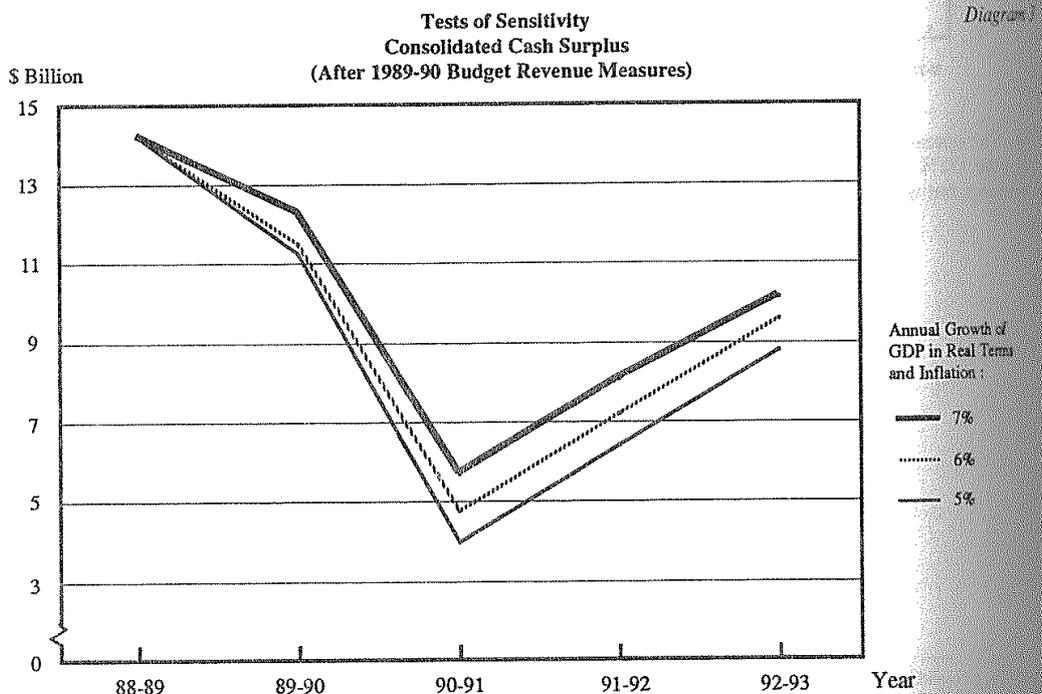
<sup>(1)</sup> The Consolidated Account comprises expenditure by the Housing Authority, the Urban Council and the Regional Council, expenditure financed by the Government's statutory funds and all expenditure charged to the General Revenue Account.

15 Whilst paragraph 13 above indicates that the forecast level of surplus is sufficient to maintain fiscal reserves in real terms, an important additional consideration is the relationship of these reserves to Consolidated Account expenditure. The past and forecast relationship in this respect is illustrated in Diagram 2.



16 It will be noted that the current level of reserves in relation to Consolidated Account expenditure is better than at any time since the early 1980's. The relationship is expected to remain well above 50%.

17 The importance to these forecasts of the economic growth rate assumption has already been emphasised. The tests included in Diagram 3 indicate this sensitivity. It will be noted, however, that even under the lower GDP growth assumption tested, the position remains in balance.

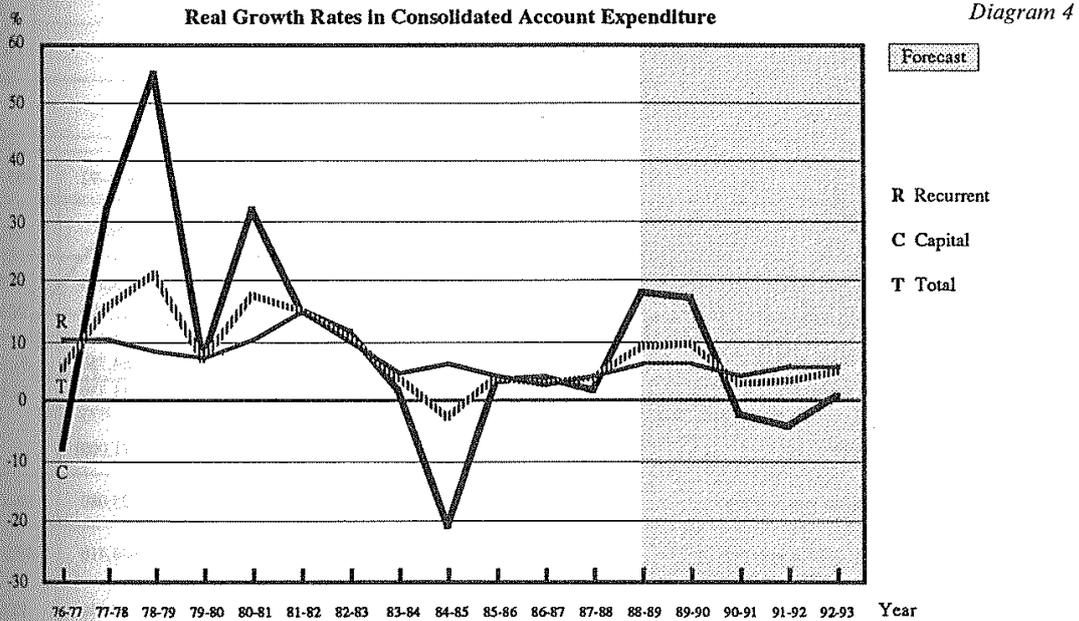


Appendix A—Contd.

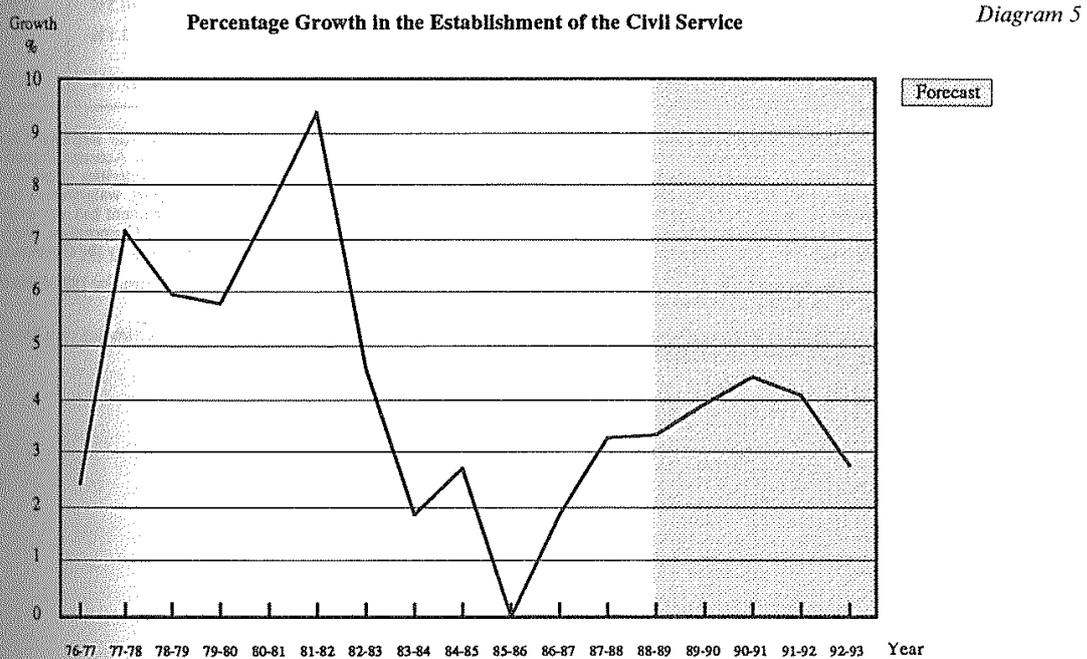
**Expenditure Growth**

18 Diagram 4 indicates the pattern of expenditure growth allowed for in these forecasts compared with results since 1976-77. The following points are of note:

- Recurrent expenditure growth has been successfully stabilised since 1983-84 at around 5%-6%. The forecasts assume a continuation of firm control over recurrent expenditure.
- Capital expenditure growth is inevitably much more volatile and, indeed, was negative in 1984-85. The forecasts assume a return to growth albeit controlled to a narrower range.
- Total real expenditure growth has fallen considerably since the late 1970's and early 1980's and is forecast to be controlled at around 5% p.a.



19 The projected trend in staff growth implied in these forecasts is indicated in Diagram 5 as follows:



## Appendix A—Contd.

20 After a period of high staff growth in the late 1970's and early 1980's, the rate of growth has stabilised from about 1983-84 onwards. However, the target rate (no more than 2½%) will be exceeded in 1989-90 and in the next three years or so as a number of major medical facilities come on stream and as the Royal Hong Kong Police Force is expanded.

**Consolidated Account Expenditure in the Context of the Economy**

21 For monitoring purposes, the Government's own expenditure is consolidated with the expenditure of other public bodies such as the Urban Council in order to compare total Consolidated Account expenditure with the size of the economy.

22 The results of this comparison are set out in Table 4 and the historical and forecast relationship between GDP and Consolidated Account expenditure is illustrated in Diagram 6.

**Consolidated Account Expenditure in the Context of the Economy (Note 1)**

Table 4

	Revised Estimate	Forecast			
		1988-89	1989-90	1990-91	1991-92
	\$m	\$m	\$m	\$m	\$m
Operating expenditure	42,570	50,150	56,070	63,550	72,396
Capital expenditure	15,200	18,920	21,770	21,200	20,180
<b>Total Government expenditure</b>	<b>57,770</b>	<b>69,070</b>	<b>77,840</b>	<b>84,750</b>	<b>92,576</b>
Add: Other public sector bodies	7,780	10,540	9,870	11,330	13,840
Less: Debt repayments	—	(1,000)	—	—	—
MTRC equity injections	—	—	(1,500)	(1,000)	—
<b>Total Consolidated Account expenditure</b>	<b>65,550</b>	<b>78,610</b>	<b>86,210</b>	<b>95,080</b>	<b>106,416</b>
<b>Gross Domestic Product (calendar year) (Note 2)</b>	<b>425,630</b>	<b>478,410</b>	<b>537,730</b>	<b>604,410</b>	<b>679,366</b>
<b>Growth in GDP</b>					
Money terms	15.7%	12.4%	12.4%	12.4%	12.4%
Real terms	7.4%	6.0%	6.0%	6.0%	6.0%
<b>Growth in Consolidated Account expenditure</b>					
Money terms	22.2%	19.9%	9.7%	10.3%	11.2%
Real terms	9.1%	9.0%	2.5%	3.1%	4.6%
<b>Consolidated Account expenditure as a percentage of GDP (at current prices) (Note 3)</b>	<b>15.4%</b>	<b>16.4%</b>	<b>16.0%</b>	<b>15.7%</b>	<b>15.7%</b>

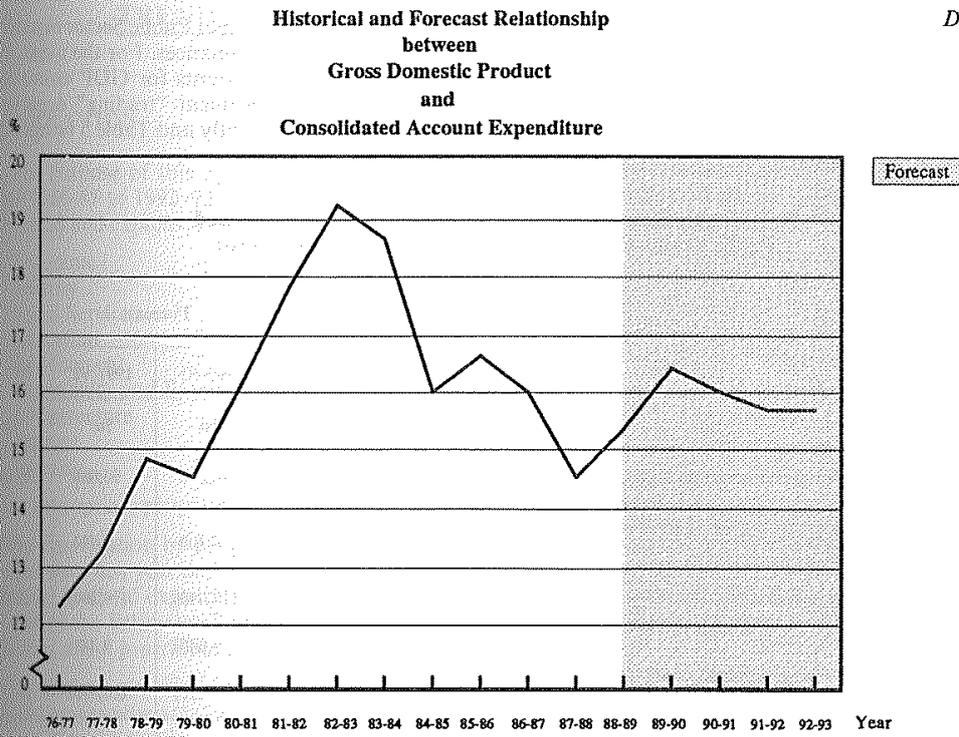
Note 1 The Consolidated Account comprises expenditure by the Housing Authority, the Urban Council and the Regional Council, expenditure financed by the Government's statutory funds and all expenditure charged to the General Revenue Account. Expenditure by institutions in the private or quasi-private 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. airport, waterworks). But not included is expenditure by those organisations, including even statutory organisations, in which the Government has only an equity position, such as the Mass Transit Railway Corporation and, post 1982-83, the Kowloon-Canton Railway Corporation. Similarly, debt repayments and equity payments are excluded as they do not reflect the actual consumption of resources by the Government.

Note 2 For years beyond the current year, the GDP figures are based on *trend* assumptions. In particular, the projection for 1989 differs from the specific forecast for that year published in the '1989 Economic Prospects'.

Note 3 Caution should be exercised in interpreting these percentages as the Consolidated Account expenditure is estimated on a fiscal year basis while the GDP is estimated on a calendar year basis.

Appendix A—Contd.

Diagram 6



## Appendix A—Contd.

23 Table 5 indicates the relationship between Consolidated Account expenditure and Public Sector expenditure. The former has historically been used as a measure for control of Government's finances. For the other, Public Sector expenditure is an economic definition used in the context of national accounts for GDP estimation. It excludes, for instance, government transfers and current expenditure of government "trading" departments. Since the two series of statistics have different components, they may move differently and Table 5 brings out the extent of this difference in movement.

Relationship Between Consolidated Account Expenditure and Public Sector Expenditure as Defined for GDP Purposes

Table 5

	Revised Estimate	Forecast			
	1988-89	1989-90	1990-91	1991-92	1992-93
	\$m	\$m	\$m	\$m	\$m
<b>Total Consolidated Account expenditure (from Table 4)</b>	65,550	78,610	86,210	95,080	106,410
Add: Imputed rent (Note 1) and expenditure by other public sector bodies not included in total Consolidated Account expenditure (Note 2)	6,830	7,330	8,300	9,480	10,470
Less: Transfers					
— recurrent and capital subventions (Note 3)	(12,590)	(14,760)	(17,040)	(19,890)	(22,900)
— other transfer payments made by Government (Note 4)	( 5,450)	( 8,640)	( 9,040)	( 9,380)	( 9,980)
Current expenditure of government "trading" departments (Note 5)	( 7,420)	( 8,200)	( 9,320)	(10,470)	(11,750)
<b>Total Public Sector expenditure in national accounts terms (Note 6)</b>	46,920	54,340	59,110	64,820	72,250
<b>Growth in Public Sector expenditure</b>					
Money terms	19.3%	15.8%	8.8%	9.7%	11.1%
Real terms	4.4%	4.4%	1.7%	2.5%	4.2%
<b>Gross Domestic Product (calendar year) (Note 7)</b>	425,630	478,410	537,730	604,410	679,300
<b>Growth in GDP</b>					
Money terms	15.7%	12.4%	12.4%	12.4%	12.4%
Real terms	7.4%	6.0%	6.0%	6.0%	6.0%
<b>Public Sector expenditure as a percentage of GDP (at current prices) (Note 8)</b>	11.0%	11.4%	11.0%	10.7%	10.6%

Note 1 An estimate of the notional rent of premises owned by the Government and occupied by the non-trading government departments.

Note 2 Capital expenditure by the Mass Transit Railway Corporation and the Kowloon-Canton Railway Corporation and current and capital expenditure by other public organisations such as the Vocational Training Council, Trade Development Council, Hong Kong Productivity Centre, Hong Kong Tourist Association and Consumer Council, etc.

Note 3 Financial assistance to government-assisted institutions in the private or quasi-private sector.

Note 4 Expenditure on land acquisitions, compensations, purchases of properties, welfare payments, grants and loans etc.

Note 5 Government trading departments are distinguished from other government departments in that they are engaged in the production of goods and services principally for sale to the public. The criteria for distinguishing the trading activities of the Government from other activities are:

- (i) that the activity consists of the production of goods and services of a kind which might be provided by a private business; and
- (ii) that sales, either to the public or to other government departments, account for a major part of their activities. Some examples of departments regarded as being engaged in trading activities are Civil Aviation, Housing, Post Office and Water Supplies.

Note 6 Total Public Sector expenditure and its growth rates in this table are calculated on a fiscal year basis. These may, therefore, differ from the corresponding figures for Public Sector expenditure as a component of the GDP calculated on a calendar year basis. Moreover, there is also a difference in the price increase assumptions used.

Note 7 The GDP growth rates for the years 1989 to 1992 (and the GDP figures thus derived) are the *trend* projections used for medium-term budgetary planning purposes. Fluctuations from year to year in the level of economic activity and in prices are not taken into account. Thus, the growth rate in money terms of the GDP in 1989 differs from the short-term GDP forecast quoted elsewhere in the Budget Speech.

Note 8 Caution should be exercised in interpreting these percentages as the Public Sector expenditure is estimated on a fiscal year basis while the GDP is estimated on a calendar year basis.

TRENDS IN PUBLIC EXPENDITURE 1984-85 TO 1992-93**INTRODUCTION**

The purpose of this appendix is to present trends in public expenditure (Consolidated Account) over the period 1984-85 to 1992-93<sup>(1)</sup>. It shows the actual and forecast recurrent and capital expenditure during this nine year period and expresses this in terms of nine main programme area groups:

- Economic
- Security
- Social Services
- Education
- Environment
- Community and External Affairs
- Infrastructure
- Support
- Housing

Where appropriate programme area groups are further analysed by programme areas.

1 The classification by programme area groups and programme areas of services and items of expenditure has changed since last year and the annex to this appendix provides a key to the revised classification. Details of the individual heads of expenditure contributing to a particular programme area are provided in an index on pages 477-484 of the Estimates Summaries. This index further provides details by head of expenditure of individual activities which contribute to a programme area.

2 The analysis provided in this appendix shows how resources have been and are planned to be allocated to different programme area groups. The analysis therefore presents two perspectives:

**Historical**

an analysis of the changes in the share of total expenditure on programme area groups and the balance between them over the last five years (1984-85 to 1988-89).

**Forecast**

an analysis of the planned changes in the share of total expenditure on programme area groups and the balance between them over the five years (1988-89 to 1992-93). This forecast is made on the basis of current trends and commitments but does not take into account new or improved services not already planned<sup>(2)</sup>.

<sup>(1)</sup> This analysis is expressed in Consolidated Account terms as defined in Table 4 of Appendix A and includes expenditure of the Housing Authority, the Urban Council and the Regional Council.

<sup>(2)</sup> Planned changes take account of existing capital programmes, the recurrent consequences in terms of staffing and running costs of new capital assets once completed, underlying requirements of service and service improvements either already under implementation or to be implemented.

## Appendix B—Contd.

## HISTORICAL PERSPECTIVE: THE MAJOR FEATURES

4 The changing share of expenditure on programme area groups from 1984–85 to 1988–89 is illustrated in the following table:

Consolidated Account Expenditure by Programme Area Groups 1984–85 to 1988–89 *Table 1*

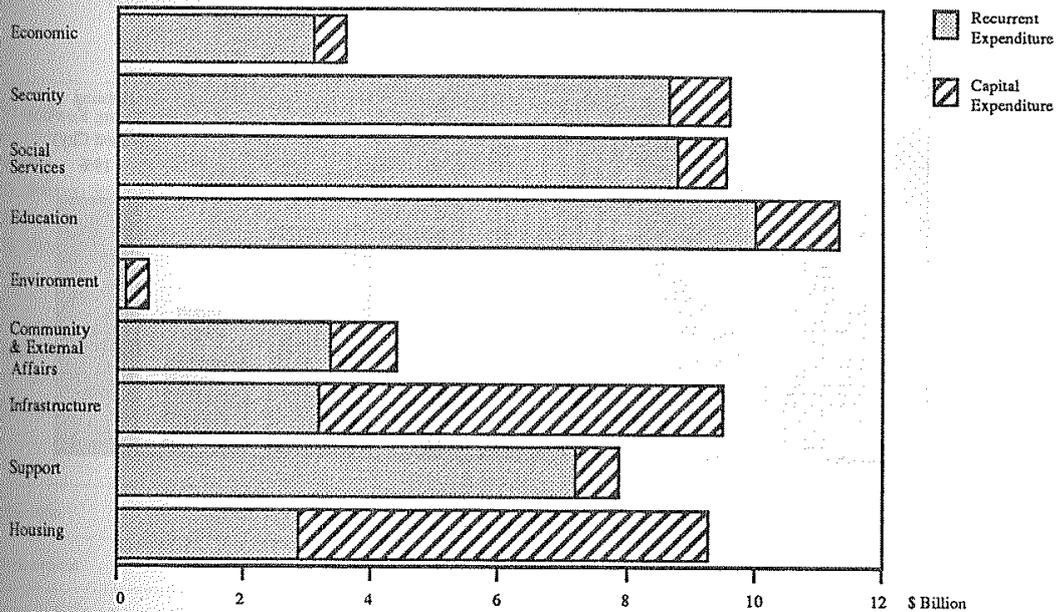
Programme Area Groups	Actual				Revised Estimate
	1984–85	1985–86	1986–87	1987–88	1988–89
	%	%	%	%	%
(A) Economic	4.9	5.1	5.4	5.6	5.5
(B) Security					
(1) Internal Security	12.5	12.6	13.1	12.8	12.5
(2) Immigration	0.7	0.8	0.9	0.9	0.9
(3) Other	1.2	1.3	1.4	1.1	1.1
	14.4	14.7	15.4	14.8	14.5
(C) Social Services					
(1) Social Welfare	5.7	5.8	5.8	5.9	6.0
(2) Health	8.2	8.5	9.1	9.3	8.7
	13.9	14.3	14.9	15.2	14.7
(D) Education	16.7	16.7	17.5	17.1	17.2
(E) Environment	1.1	1.0	0.8	0.8	0.8
(F) Community and External Affairs					
(1) Recreation, Culture and Amenities	6.4	6.5	5.8	5.9	5.7
(2) District and Community Relations	0.6	0.6	0.7	0.7	0.7
(3) Other	0.3	0.3	0.3	0.3	0.3
	7.3	7.4	6.8	6.9	6.7
(G) Infrastructure					
(1) Transport	6.2	4.7	4.4	5.3	5.0
(2) Land and Buildings	5.6	6.2	6.2	5.2	6.3
(3) Water Supply	3.1	3.0	3.3	3.3	3.2
	14.9	13.9	13.9	13.8	14.5
(H) Support	13.5	14.2	13.2	12.7	12.0
(I) Housing	13.3	12.7	12.1	13.1	14.1
	100.0	100.0	100.0	100.0	100.0
	\$m	\$m	\$m	\$m	\$m
Total Consolidated Account expenditure	39,882	43,444	47,930	53,636	65,550

Appendix B—Contd.

5 It should be noted that the volatility in spending on some programme area groups is partly a reflection of the element of capital spending within the total. Capital expenditure is, by its nature, volatile. The following diagram shows the relationship between capital and recurrent spending for each programme area group in 1988-89.

Consolidated Account Expenditure  
by Programme Area Groups  
(1988-89 Revised Estimate)

Diagram 1



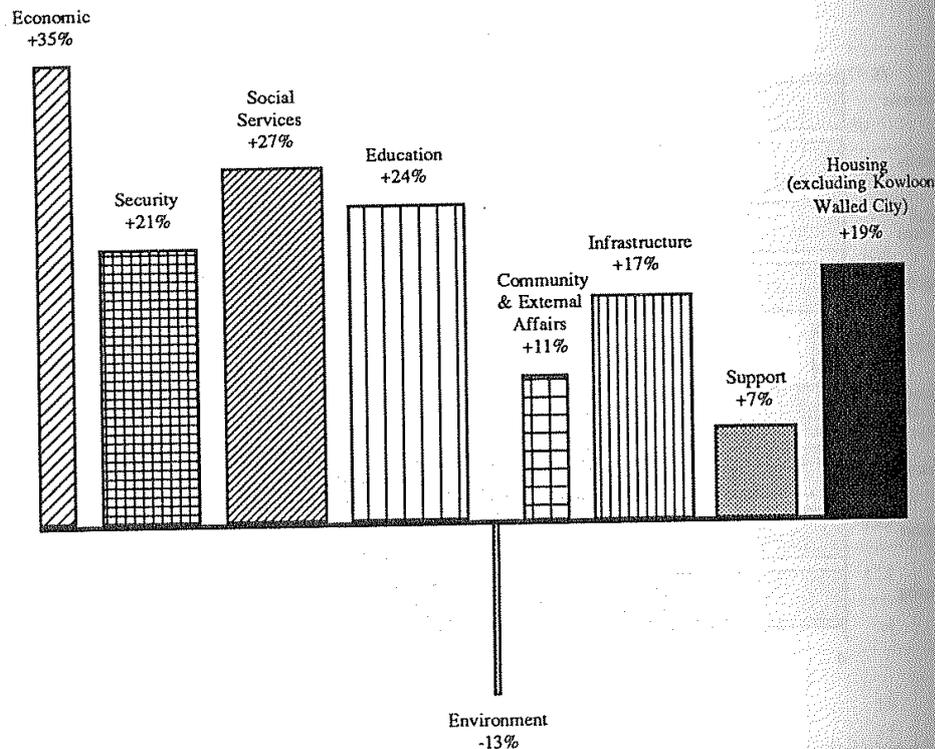
6 It will be noted that capital expenditure accounts for 75% of spending on the *Environment* group, 66% on *Infrastructure* and 69% on *Housing*.

7 Since 1984-85 expenditure on *Social Services* as a share of total spending has increased from 13.9% to 14.7% and on *Education* from 16.7% to 17.2%. This trend reflects the continuing growth in demand for these services and also improvements in standard. The share for the *Economic* group has increased from 4.9% to 5.5% largely as a result of continuing expenditure on the airport to meet growing passenger traffic.

8 The percentage changes in real terms for each programme area group comparing 1984-85 and 1988-89 are illustrated in the following diagram:

Percentage Changes (in real terms)  
in Spending for Programme Area Groups  
Comparing 1984-85 and 1988-89

Diagram 1



Note: The width of each bar on the horizontal axis is proportional to the 1988-89 Revised Estimate

9 Consolidated Account expenditure over this period increased by about 20% in real terms equivalent to an average annual growth rate of about 5%. The overall growth rate reflects the recovery from budgetary restraints imposed in the early 1980's as public expenditure levels increased in response, to some extent, to suppressed demand.

10 Within the overall growth some sectors of Government have grown significantly in terms of expenditure. The *Economic* (including the airport), *Security*, *Social Services* and *Education* groups have grown at rates above the average.

	Total Real Growth 1984-85 to 1988-89 %	Average Annual Growth Rate %
Economic	35	7.8
Security	21	5.0
Social Services	27	6.2
Education	24	5.6

11 Within other programme area groups expenditure on *District and Community Relations* has increased by 41% over the period and on *Land and Buildings* by 36%.

12 Expenditure on the *Environment* group fell in real terms in 1985-86 and 1986-87 but grew by an average of 6.4% a year in 1987-88 and 1988-89.

13 Expenditure on *Transport* also fell in real terms in 1985-86 and 1986-87 but increased by an average of 13.8% in 1987-88 and 1988-89. This trend is a reflection of the pattern of expenditure on capital projects and the completion of the Kowloon-Canton Railway modernisation.

## Appendix B—Contd.

## FORECAST OF TRENDS IN PUBLIC EXPENDITURE 1988-89 TO 1992-93

4. Table 2 shows Consolidated Account expenditure over the period from 1988-89 to 1992-93 and the forecast data for programme area groups.

Consolidated Account Expenditure by Programme Area Groups 1988-89 to 1992-93

Table 2

Programme Area Groups	Revised Estimate	Forecast			
	1988-89	1989-90	1990-91	1991-92	1992-93
	%	%	%	%	%
A. Economic	5.5	5.5	5.5	5.4	5.4
B. Security					
(1) Internal Security	12.5	12.5	12.4	12.4	12.2
(2) Immigration	0.9	1.0	1.0	1.1	1.1
(3) Other	1.1	1.1	1.1	1.1	1.1
	14.5	14.6	14.5	14.6	14.4
C. Social Services					
(1) Social Welfare	6.0	6.3	6.8	7.2	7.3
(2) Health	8.7	8.9	9.9	10.7	11.1
	14.7	15.2	16.7	17.9	18.4
D. Education	17.2	16.6	16.7	17.0	17.0
E. Environment	0.8	1.1	1.4	1.5	1.6
F. Community and External Affairs					
(1) Recreation, Culture and Amenities	5.7	5.6	5.5	5.2	5.2
(2) District and Community Relations	0.7	0.7	0.6	0.6	0.6
(3) Other	0.3	0.3	0.3	0.3	0.3
	6.7	6.6	6.4	6.1	6.1
G. Infrastructure					
(1) Transport	5.0	4.9	4.3	4.1	4.0
(2) Land and Buildings	6.3	6.4	6.9	6.4	6.1
(3) Water Supply	3.2	3.0	2.9	3.1	3.2
	14.5	14.3	14.1	13.6	13.3
H. Support	12.0	12.6	12.0	12.1	12.4
I. Housing	14.1	13.5	12.7	11.8	11.4
	100.0	100.0	100.0	100.0	100.0
	\$m	\$m	\$m	\$m	\$m
Total Consolidated Account expenditure	65,550	78,610	86,350	93,990	103,380

Appendix B—Contd.

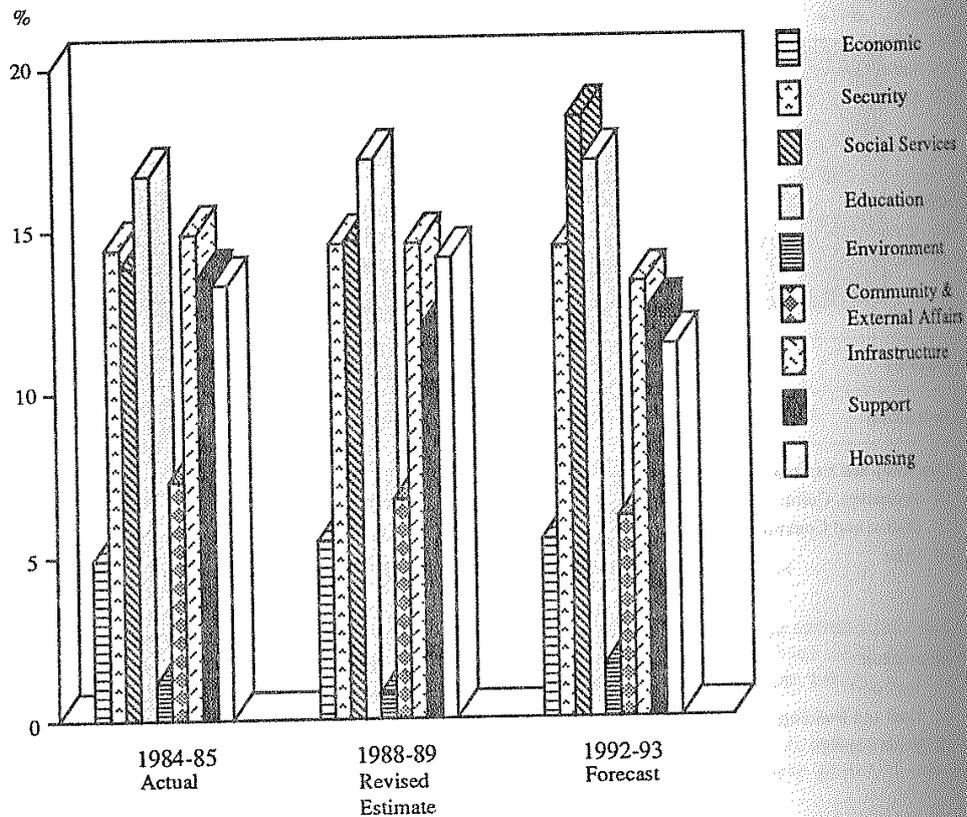
15 This table takes into account current trends and actual or planned commitments. It does not anticipate any changes in policy or decisions on new or improved services which might occur during the forecast period.

16 The pattern of expenditure between the various programme area groups will differ as each has its own characteristics and financial requirements. These will be affected by changes in the level of demand for different services, the phasing of capital expenditure, the recurrent consequences of completed capital projects and the introduction of new or improved services provided for in the 1989-90 budget proposals.

17 The actual and forecast shift in the share of resources by the various programme area groups over the period 1984-85 to 1992-93 is illustrated in the following diagram:

Share of Consolidated Account Expenditure by Programme Area Groups

Diagram 3

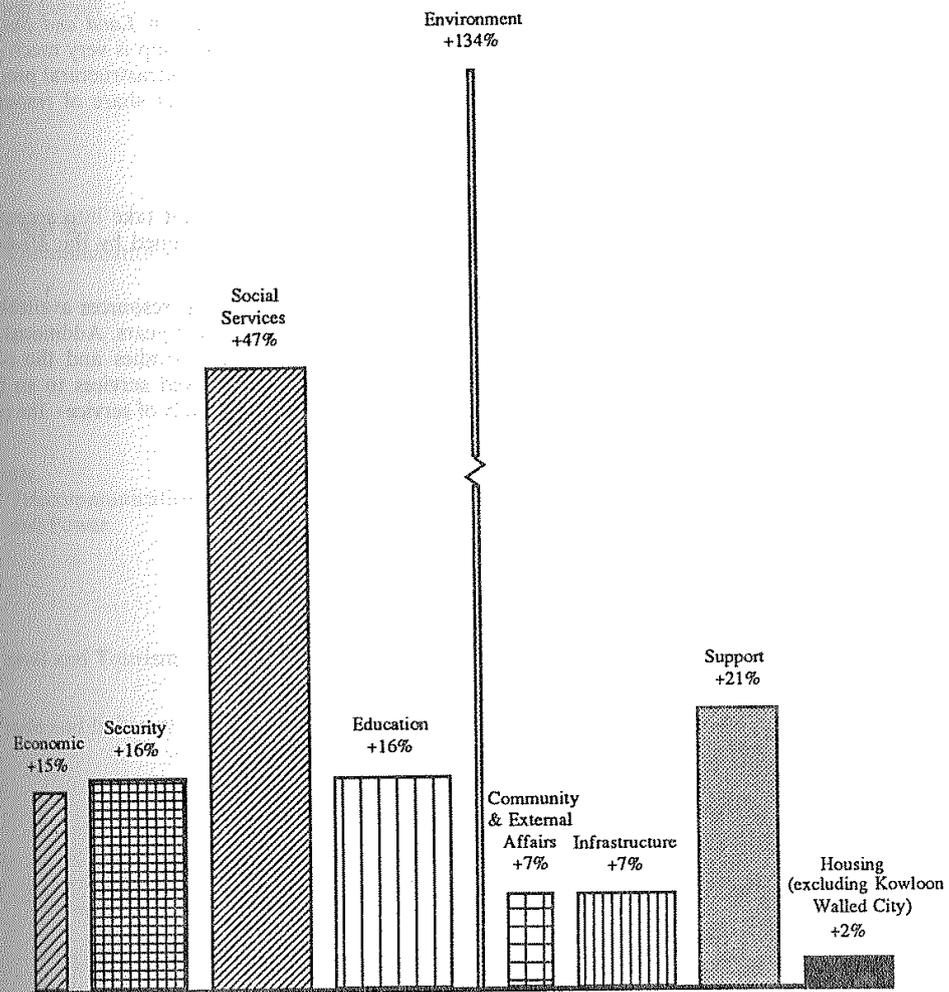


Appendix B—Contd.

18 The forecast percentage changes in real terms in spending on each programme area group between 1988-89 and 1992-93 are illustrated in the following diagram:

**Percentage Changes (in real terms)  
in Spending for Programme Area Groups  
Comparing 1988-89 and 1992-93**

Diagram 4



Note : The width of each bar on the horizontal axis is proportional to the 1988-89 Revised Estimate

## Appendix B—Contd.

- 19 Table 2 and Diagram 4 show a continuation of increased spending on *Social Services* and *Education*.
- 20 Spending on *Social Services* will increase by 47% in real terms at an average annual rate of 10%. Within this group, spending on *Social Welfare* will increase by 42% at an average annual rate of 9% and on *Health* by 49% at an average annual rate of 11%.
- 21 Spending on *Education* will increase by 16% at an average annual rate of 4%. Taken together the share of resources allocated to *Social Services* and *Education* will increase from 32% in 1988–89 to 35% in 1992–93.
- 22 Spending on the *Environment* group will more than double at an average annual growth rate of 25%.
- 23 Spending on *Security* will rise by 16% at an average annual rate of 4% but within that group spending on *Immigration* control will rise by 43% at an annual average rate of 10%.
- 24 Spending on *Housing* (excluding the clearance of the Kowloon Walled City) will rise only moderately—a reflection of the substantial completion of the major housing programme begun in the 1970's.
- 25 Spending on *Infrastructure* will rise by 7% but within this group spending on *Land and Buildings* will increase by 13% and on *Water Supply* by 17%. The pattern of spending on this group is very much influenced by the phasing of capital expenditure and it is anticipated that spending on major infrastructural projects likely to begin towards the end of or beyond the forecast period will result in a greater share of resources being allocated to this group in the future.

**The Scope for New or Improved Services**

- 26 The forecast of Consolidated Account expenditure shown in Table 2 does not take into account new or improved services not already planned. The scope for introducing these is determined by the *Medium Range Forecast* (MRF) (see Appendix A).
- 27 A comparison of the current MRF with the forecast in Table 2 indicates that resources available for new or improved services not already planned are likely to be more scarce than in recent years. Additional resources are expected to become available from savings identified in value for money studies and the consequent redirection of resources. However it will be necessary to finance new or improved services to an increasing extent from resources already committed to or planned for maintaining existing levels of service—the baseline.

Appendix B—Contd.

KEY TO CLASSIFICATION OF EXPENDITURE

Programme Areas	Reference (Note 1)
(A) Economic	
(1) Monetary Affairs	Government Secretariat (Monetary Affairs Branch) Miscellaneous Services (part) Public Debt Registrar General's Department (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Government Secretariat (Monetary Affairs Branch)
(2) Food Supply	Agriculture and Fisheries Department (part) Electrical and Mechanical Services Department (part) Government Laboratory (part) Capital Works Reserve Fund: payments in respect of— Food Supply projects Development Loan Fund: payments in respect of— Primary products
(3) Air and Sea Communications	Civil Aviation Department (part) Electrical and Mechanical Services Department (part) Government Secretariat (Economic Services Branch—part) Marine Department (part) Capital Works Reserve Fund: payments in respect of— Aviation and Shipping projects Major Systems—Civil Aviation Department (part) —Marine Department (part)
(4) Posts, Telecommunications and Power	Electrical and Mechanical Services Department (part) Government Secretariat (Economic Services Branch—part) Post Office (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Post Office Post and Telecommunication projects
(5) Travel and Tourism	Government Secretariat (Economic Services Branch—part) Subventions: Miscellaneous (part)
(6) Trade and Industry	Agriculture and Fisheries Department (part) Census and Statistics Department (part) Customs and Excise Department (part) Government Laboratory (part) Government Secretariat (Trade and Industry Branch—part) Government Secretariat: Overseas Offices (part) Industry Department Miscellaneous Services (part) Post Office (part) Registrar General's Department (part) Subventions: Miscellaneous (part) Trade Department Capital Works Reserve Fund: payments in respect of— Major Systems—Customs and Excise Department (part) —Trade Department Development Loan Fund: payments in respect of— Development of industrial estates Industry

Programme Areas	Reference ( <i>Note 1</i> )
(A) <i>Economic—Contd.</i>	
(7) Public Safety	Agriculture and Fisheries Department (part) Electrical and Mechanical Services Department (part) Government Secretariat (Economic Services Branch—part) Royal Observatory (part)
(8) Employment	Government Secretariat (Education and Manpower Branch—part) Labour Department Registry of Trade Unions Technical Education and Industrial Training Department (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Labour Department Technical Education and Industrial Training subvention projects (part)
(B) <i>Security</i>	
(1) Internal Security	Auxiliary Medical Services Civil Aid Services Civil Aviation Department (part) Correctional Services Department Customs and Excise Department (part) Electrical and Mechanical Services Department (part) Fire Services Department Government Laboratory (part) Government Secretariat (Security Branch) Internal Security: Miscellaneous Measures Marine Department (part) Miscellaneous Services (part) Police Complaints Committee Police: Royal Hong Kong Police Force Royal Hong Kong Auxiliary Air Force Royal Hong Kong Regiment (The Volunteers) Subventions: Miscellaneous (part) Capital Works Reserve Fund: payments in respect of— Equipment Consequential on Major Capital Projects Law and Order projects (Police and Correctional Services) Public Safety projects (Ambulance and Fire Services) Major Systems—Civil Aviation Department (part) —Customs and Excise Department (part) —Fire Services Department —Government Secretariat (Security Branch) —Marine Department (part) —Police: Royal Hong Kong Police Force
(2) Immigration Control	Immigration Department Capital Works Reserve Fund: payments in respect of— Major Systems—Immigration Department
(3) Legal Administration	Legal Department Capital Works Reserve Fund: payments in respect of— Major Systems—Legal Department

Appendix B—*Contd.*

Programme Areas	Reference ( <i>Note 1</i> )
(B) <i>Security—Contd.</i>	
(4) Judicial Administration	Judiciary Capital Works Reserve Fund: payments in respect of— Law and Order projects (Judiciary)
(5) Anti-Corruption	Independent Commission Against Corruption Capital Works Reserve Fund: payments in respect of— Major Systems—Independent Commission Against Corruption
(C) <i>Social Services</i>	
(1) Social Welfare	Education Department (part) Government Secretariat (Health and Welfare Branch—part) Post Office (part) Social Welfare Department (part) Subventions: Miscellaneous (part) Technical Education and Industrial Training Department (part) Transport Department (part) Capital Works Reserve Fund: payments in respect of— Education projects (part) Education Subventions projects (part) Social Welfare projects Major Systems—Transport Department (part)
(2) Health	Lotteries Fund payments Agriculture and Fisheries Department (part) Department of Health (part) Electrical and Mechanical Services Department (part) Government Secretariat (Health and Welfare Branch—part) Hospital Services Department Subventions: Miscellaneous (part) Capital Works Reserve Fund: payments in respect of— Hospital Services Subventions projects Major Systems—Hospital Services Department Medical and Health projects
(D) <i>Education</i>	Education Department (part) Government Secretariat (Education and Manpower Branch—part) Government Secretariat: Overseas Offices (part) Miscellaneous Services (part) Radio Television Hong Kong (part) Subventions: Miscellaneous (part) Technical Education and Industrial Training Department (part) Universities and Polytechnics Capital Works Reserve Fund: payments in respect of— Education projects (part) Education Subventions projects (part) Technical Education and Industrial Training subvention projects (part) Universities and Polytechnics subvention projects

Programme Areas	Reference ( <i>Note 1</i> )
(D) <i>Education—Contd.</i>	Development Loan Fund: payments in respect of— Education Student Loan Fund payments
(E) <i>Environment</i>	Agriculture and Fisheries Department (part) Environmental Protection Department Government Laboratory (part) Government Secretariat: Lands and Works Branch (part) Capital Works Reserve Fund: payments in respect of— Environmental Protection projects
(F) <i>Community and External Affairs</i>	
(1) Recreation, Culture and Amenities	Agriculture and Fisheries Department (part) Electrical and Mechanical Services Department (part) Government Secretariat (Municipal Services Branch) Marine Department (part) Subventions: Miscellaneous (part) Regional Council expenditure Urban Council expenditure Capital Works Reserve Fund: payments in respect of— Recreation, Culture and Amenities projects Subventions to Jubilee Sports Centre Development Loan Fund: payments in respect of— Regional Council
(2) District and Community Relations	Buildings and Lands Department (part) Government Secretariat: City and New Territories Administration Government Secretariat: Overseas Offices (part) Social Welfare Department (part)
(3) Broadcasting and Entertainment	Government Secretariat (Administrative Services and Information Branch—part) Post Office (part) Radio Television Hong Kong (part) Television and Entertainment Licensing Authority Capital Works Reserve Fund: payments in respect of— Major Systems—Radio Television Hong Kong Government Secretariat (General Duties Branch)
(4) Co-ordination of External Matters	
(G) <i>Infrastructure</i>	
(1) Transport	Civil Engineering Services Department (part) Electrical and Mechanical Services Department (part) Government Secretariat (Transport Branch) Highways Department Transport Department (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Transport Department (part) Transport projects Mass Transit Fund payments

Appendix B—*Contd.*

Programme Areas	Reference ( <i>Note 1</i> )
(G) <i>Infrastructure—Contd.</i>	
(2) Land and Buildings	Buildings and Lands Department (part) Civil Engineering Services Department (part) Electrical and Mechanical Services Department (part) Government Secretariat: Lands and Works Branch (part) Rating and Valuation Department (part) Registrar General's Department (part) Territory Development Department (part) Capital Works Reserve Fund: payments in respect of— Civil Engineering projects Land Acquisition (excluding Kowloon Walled City projects) Major Systems—Buildings and Lands Department Public Safety projects (Landslip prevention) Development Loan Fund: payments in respect of— Land development
(3) Water Supply	Government Secretariat: Lands and Works Branch (part) Water Supplies Department Capital Works Reserve Fund: payments in respect of— Water Supplies projects
(H) <i>Support</i>	
(1) Revenue Collection and Financial Control	Audit Department Civil Aviation Department (part) Customs and Excise Department (part) Government Secretariat (Finance Branch) Inland Revenue Department Miscellaneous Services (part) Rating and Valuation Department (part) Treasury Capital Works Reserve Fund: payments in respect of— Major Systems—Customs and Excise Department (part) —Inland Revenue Department —Treasury
(2) Central Management of the Civil Service	Department of Health (part) General Expenses of the Civil Service (part) Government Secretariat (Civil Services Branch) Government Secretariat: Civil Service Training Centre Government Secretariat: Overseas Offices (part) Pensions Public Service Commission Standing Commission on Civil Service Salaries and Conditions of Service Subventions: Miscellaneous (part)
(3) Administrative Services	Architectural Services Department (part) Electrical and Mechanical Services Department (part) General Expenses of the Civil Service (part) Government Laboratory (part)

Programme Areas	Reference (Note 1)
(H) <i>Support—Contd.</i>	
(3) Administrative Services— <i>Contd.</i>	Government Secretariat (Administrative Services and Information Branch—part) Information Services Department Miscellaneous Services (part) Rating and Valuation Department (part) Royal Observatory (part) Subventions: Miscellaneous (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Architectural Services Department (part) Support projects
(4) Intra-Governmental Services	His Excellency the Governor's Establishment Architectural Services Department (part) Census and Statistics Department (part) Civil Engineering Services Department (part) Electrical and Mechanical Services Department (part) Government Data Processing Agency Government Land Transport Agency Government Secretariat (Office of the Deputy Chief Secretary—part) Government Secretariat: Lands and Works Branch (part) Government Supplies Department Marine Department (part) Printing Department Territory Development Department (part) Capital Works Reserve Fund: payments in respect of— Major Systems—Architectural Services Department (part) —Government Data Processing Agency
(5) Constitutional and Electoral Affairs	Government Secretariat (Office of the Deputy Chief Secretary—part) Legal Aid Department Miscellaneous Services (part) Subventions: Miscellaneous (part)
(6) Support for Members of the Executive and Legislative Councils	Office of Members of the Executive and Legislative Councils
(7) Complaints Against Maladministration	Office of the Commissioner for Administrative Complaints
(I) <i>Housing</i>	Housing Department Housing Authority expenditure Capital Works Reserve Fund: payments in respect of— Housing Kowloon Walled City projects (including Land Acquisition) Development Loan Fund: payments in respect of— Housing

*Note 1* Where a department or head of expenditure contributes to more than one programme area, details are given in the relevant controller of expenditure officer's report in the 1989-90 Estimates Summaries.

## Appendix C

**CONTINGENT LIABILITIES AS AT 31 MARCH 1988**

A contingent liability is defined as a liability arising from a condition or situation which exists at the year end, where the amount of the liability, if any, and its timing will depend on the occurrence or non-occurrence of one or more uncertain future events.

1. The Government's contingent liabilities as at 31 March 1988 are listed below. The approximate maximum potential amount of each liability as at that date is indicated in brackets. It is not an assessment of actual risk.

- (1) Capital subscription to Asian Development Bank (\$670.9 million);
- (2) Outstanding currency notes demonetised under the Dollar and Subsidiary Currency Notes Ordinance (Cap. 67) (\$10.2 million);
- (3) One cent notes issued under section 4(1) of the Dollar and Subsidiary Currency Notes Ordinance (Cap. 67) (\$1.1 million);
- (4) Special coins issued under L.N. 73 of 1975 (\$372 million);
- (5) A guarantee on notes issued by the Hong Kong Building and Loan Agency Ltd. (\$200 million);
- (6) All moneys which may become due by the Hong Kong Export Credit Insurance Corporation under contracts of insurance (\$4,131 million);
- (7) Guarantees in respect of the repayment of loans made to and the discharge of indebtedness of the Mass Transit Railway Corporation under the facilities specified in the Schedule to L.N. 242 of 1975 (\$3,770.5 million);
- (8) A guarantee in respect of the reimbursement of costs incurred by the Mass Transit Railway Corporation arising from the possible extension of the mass transit railway to Junk Bay (\$2.4 million);
- (9) Possible equity injections to the Mass Transit Railway Corporation to be made on or after 31 December 1989 (\$2,500 million);
- (10) A guarantee under section 13 of the Kowloon-Canton Railway Corporation Ordinance (Cap. 372) in respect of the repayment of the principal of, the payment of interest on, and the discharge of any other financial obligation in connexion with any sums borrowed by the Kowloon-Canton Railway Corporation (\$500 million);
- (11) A guarantee in respect of a commercial loan to the City Polytechnic of Hong Kong for the acquisition of temporary premises (\$240 million);
- (12) A guarantee in respect of a commercial borrowing facility for the Hong Kong Nuclear Investment Company Limited (\$355 million);
- (13) An underwriting in respect of the costs for the 1988 conference and exhibition on pollution in the metropolitan and urban environment (Polmet 88) (\$0.35 million);
- (14) Outstanding New Territories Land Exchange Entitlements (Letters A/B) (estimated monetised value of \$6,823 million); and
- (15) Outstanding litigation (\$1,244 million).

**THE RECURRENT COST IMPLICATIONS OF MAJOR NEW OR IMPROVED  
SERVICES TO BEGIN IN 1989-90 TO 1992-93**

The following items of major developments have been selected by the Chief Secretary's Committee for implementation in 1989-90 to 1992-93. It shows the cash cost of individual items for each of the four years from 1989-90 to 1992-93. Together with some other minor items, the cash cost of proposals to be introduced in 1989-90 is \$450 million.

Description	Cash Cost			
	1989-90 (\$m)	1990-91 (\$m)	1991-92 (\$m)	1992-93 (\$m)
<b>Economic</b>				
(1) Setting up of new overseas economic and trade offices in North America and Australia	6.8	6.8	13.5	14.7
(2) Improvement to the system of factory and consignment checks	5.5	12.7	15.4	17.4
(3) Quality assurance of the Industrial Development and Support Programme	4.3	5.3	6.3	6.8
(4) Strengthening of the supervision of banks and deposit-taking companies	7.0	6.6	6.7	6.7
<b>Security</b>				
(1) Implementation of Immigration Records Information System	3.1	6.9	6.2	6.8
(2) Expansion of the Royal Hong Kong Auxiliary Air Force to cope properly with day and night search and rescue operations and to localise its flying wing	2.4	5.5	7.8	8.8
(3) Replacement of Identity Card Information System	3.3	2.7	6.1	11.2
(4) Implementation of the planned legislation for sequestration of assets of drug traffickers	14.3	16.7	17.8	17.8
(5) Encouragement of more rapid localisation of government legal services by means of a 'double-ladder' of advancement for selected local lawyers	2.8	3.9	3.2	2.3
<b>Social Services</b>				
(1) Improvement of rehabilitation services for the disabled	3.7	7.2	7.3	7.4
(2) Establishment of the Hospital Authority for improvement to delivery of medical services in Hong Kong	—	15.2	15.3	15.3
(3) Split of the Medical and Health Department into the Hospital Services Department and the Department of Health	13.7	13.7	13.7	13.7
(4) Improvement of staff provision for family services centres and medical social services, and extension of standard costs for social welfare services	3.2	6.3	6.4	6.4
<b>Education</b>				
(1) Increases in financial assistance to Lingnan College	12.4	16.5	18.4	18.8
(2) Initial administrative and operational costs for the Hong Kong University of Science and Technology	30.8	104.7	225.4	228.9
(3) Language improvement measures in public sector schools (provision of one additional graduate teacher of Chinese to secondary schools with 18 classes or more)	32.5	55.7	55.7	55.7
(4) Research grants for the five UPGC-funded institutions	15.0	25.0	50.0	57.5
(5) Recurrent subsidy for the Open Learning Institute	27.4	2.0	—	—
(6) Revised mode of retraining for primary school teachers	12.9	6.9	6.9	6.9

Appendix D—Contd.

Description	Cash Cost			
	1989-90 (\$m)	1990-91 (\$m)	1991-92 (\$m)	1992-93 (\$m)
<b>Environment</b>				
(1) Provision of a refuse transfer station in Kowloon Bay	0.2	16.5	31.5	35.5
(2) Marine disposal of sludges from Sha Tin sewage treatment works	—	15.8	15.8	15.8
(3) Provision of a refuse transfer station in Hong Kong Island West	—	—	0.2	26.9
(4) Provision of a chemical waste treatment centre	5.4	6.7	47.8	62.8
(5) Declaration of water control zones to implement the Water Pollution Control Ordinance	1.0	1.8	3.4	3.5
<b>Community and External Affairs</b>				
(1) Increases in subvention for the performing arts	8.3	9.7	11.8	14.0
(2) Provision of higher level of funding to District Boards for implementation of additional minor environmental improvement projects and community activities	9.8	9.8	9.8	9.8
<b>Infrastructure</b>				
(1) Purchase of additional water from China to meet an enhanced planning standard	42.0	45.4	51.9	51.9
(2) Survey and control of potentially dangerous private buildings of early post-war period	4.2	5.6	6.3	6.8
(3) Strengthening of traffic management	0.7	2.3	3.8	5.3
<b>Support</b>				
(1) Establishment of a permanent Senior Staff Course Centre	8.6	8.9	8.9	8.9
(2) Full population census in 1991	12.6	37.7	54.9	2.2
(3) Establishment of a new Drainage (Consultants Management) Division to handle the environmental improvement programme	5.7	6.7	7.0	5.9
(4) Improvement to the quality of preventive maintenance to public sewers and drains	10.8	12.6	14.0	15.9
(5) Desilting of open nullahs, drains and river channels for pollution abatement	5.6	7.2	7.9	8.3
(6) Facilities for separate taxation for salaries tax purposes for working wives	2.4	12.5	12.8	13.0
(7) Provision of more systematic and professional management of the whole government property	3.2	5.4	5.4	5.4
(8) Restoration of standard level of maintenance of government buildings	4.6	6.6	8.6	10.6

2 This growth in recurrent expenditure is in addition to growth arising from meeting the running costs of buildings (schools, hospitals, etc.) and from responding to changes in the underlying demand for individual services. The latter may be due, for example, to population growth or changes in the number of persons eligible for a particular service.

Appendix E

**MAJOR CAPITAL WORKS PROJECTS TO BEGIN IN 1989-90**

The following is a list of those schemes with a project cost of \$100 million or over, budgetted to begin in 1989-90:

<i>Description</i>	<i>Project Cost (\$m)</i>
(1) Improvement to air-conditioning and building services in the passenger terminal building and old office block at Kai Tak International Airport	120
(2) Kowloon Area Traffic Control System—renewal and enhancement	100
(3) Road improvement and pedestrian schemes in the Salisbury Road, Canton Road and Austin Road Corridors	170
(4) 480 Fire Services rank and fire married quarters at Lung Cheung Road	200
(5) 304 Fire Services rank and fire married quarters in area 22, Junk Bay	120
(6) Ambulance depot and training school at Ho Man Tin	240
(7) Strategic Sewage Disposal Schemes—feasibility investigations	140
(8) West Kowloon medical rehabilitation centre and child assessment centre	120
(9) Tsuen Wan convalescent/infirmity hospital and quarters	140
(10) Fanling development, package 6, stage I—provision of 30 hectares of land for various uses	107
(11) North-west New Territories Development—sewage treatment plant (stage I), effluent tunnel and effluent outfall	520
(12) Junk Bay development phase II, stage II, engineering works—reclamation and drainage in areas 55 and 87 and parts of areas 48, 85 and 86	390
(13) Yau Ma Tei typhoon shelter reclamation stage I—construction of three breakwaters and provision of marine facilities	350
(14) Additional water treatment works facilities for north-east New Territories	210
(15) Water supply from China beyond 1994—consultancy study, site investigations and detailed design	100

The following is a list of major projects for which feasibility studies and design and part of the work will commence in 1989-90:

<i>Description</i>	<i>Total Project Cost (\$m)</i>	<i>Cost in 1989-90 (\$m)</i>
(1) Hong Kong Island South Sewage Disposal Scheme	280	15
(2) East Kowloon Sewerage	670	30
(3) Restoration of landfill sites	730	20
(4) South-east New Territories landfill	565	35
(5) Hong Kong Island West refuse transfer station	120	4
(6) Additional water treatment and water transfer facilities for Tsuen Wan, Sha Tin, Sai Kung and urban areas—remaining works	360	15
(7) Water supply to Tsing Lung Tau and Sham Tseng	175	6
(8) Additional water treatment and water transfer facilities for north-west New Territories	570	15
(9) Development of Tuen Mun New Town areas—site formation, road, water and sewage treatment works	531	24

Appendix F(1)

PROPOSED RATES OF DUTY(i) INTOXICATING LIQUOR AND ALCOHOL

	<u>Present rate</u> (\$)	<u>Proposed rate</u> (\$)
<u>Part I</u>		
Brandy	\$55/L + 30% AV	\$52/L + 30% AV
Whisky, gin, Liqueurs, Rum, Vodka and other Spirituos Liquors	\$48/L + 30% AV	\$52/L + 30% AV
Champagne and Sparkling Wines	\$30/L + 20% AV	\$32/L + 20% AV
Still Wines over 15%	\$20/L + 20% AV	\$22/L + 20% AV
Still Wines not over 15%	\$17/L + 20% AV	\$18/L + 20% AV
Intoxicating liquor in this part above the strength of 45% by volume, for every 1% above such strength in addition to the duties specified above	\$1.40/L	\$1.50/L
<u>Part II</u>		
Cider and Perry	\$1.36/L	\$1.45/L
<u>Part III</u>		
Beer not exceeding 1030° original gravity	\$1.36/L	\$2.20/L
and in addition for every degree by which the original gravity exceeds 1030°	\$0.045/L	-

Appendix F(1)(cont'd)

PROPOSED RATES OF DUTY(i) INTOXICATING LIQUOR AND ALCOHOL (cont'd)

	<u>Present rate</u> (\$)	<u>Proposed rate</u> (\$)
<u>Part IV</u>		
Non-European Type Wines	\$8.80/L	\$9.50/L
Chinese Type Spirits and other Spirituous Liquors, Sake, Arrack	\$4.55/L	\$4.90/L
and in addition for every 1% by which the alcoholic strength by volume exceeds 30%	\$0.151/L	\$0.163/L
<u>Part V</u>		
Ethyl alcohol, and admixtures containing ethyl alcohol	\$4.55/L	\$4.90/L
Methyl alcohol, and admixtures containing methyl alcohol	\$4.55/L	\$4.90/L
and in addition for every 1% by which the alcoholic strength exceeds 30%	\$0.151/L	\$0.163/L

(ii) TOBACCO

The effect of the proposed duty changes on the estimated average retail price of various categories of smoking products might be—

	Existing duty rate	Proposed duty rate	Current average retail price	Estimated average retail price
	(\$/1,000 sticks)	(\$/1,000 sticks)	(\$/1,000 sticks)	(\$/1,000 sticks)
(1) Cigarettes				
(i) imported from US )			431.30	446.30
(ii) imported from UK )	175.00	190.00	475.00	490.00
(iii) locally manufactured			341.70	356.70
	(\$/kg)	(\$/kg)	(\$/kg)	(\$/kg)
(2) Cigars				
(i) ordinary grade )			694.10	711.10
(ii) deluxe grade )	233.00	250.00	3,076.60	3,093.60
(3) Smoking Tobacco	212.00	230.00	471.60	489.60
(4) Chinese Prepared Tobacco	45.50	50.00	121.40	125.90

Appendix F(2)

(i) VEHICLE AND DRIVING LICENCE FEES

	<u>Existing fees (\$)</u>	<u>Proposed fees (\$)</u>
<u>1. Driving Licences</u>		
Full	190 p.a.	205 p.a.
Driving instructor's	580 p.a.	625 p.a.
Learner's	390 p.a.	420 p.a.
Temporary	190	205
Driving test	390	420
Driving instructor's test	390	420
International driving permit	60 p.a.	65 p.a.
Duplicate licence	85	90
Duplicate international driving permit	60	65
Record of convictions	45	50
Certificate of no recorded conviction	45	50
<u>2. Vehicle Licences</u>		
<u>Goods Vehicle and Special Purpose Vehicle</u>		
not exceeding 1.9 tonnes	900	970
exceeding 1.9 tonnes but not exceeding 5.5 tonnes	1,750	1,890
exceeding 5.5 tonnes	3,500	3,780
<u>Taxi</u>	2,330	2,515
<u>Private Car</u>		
not exceeding 1,500 cc	2,915	3,150
exceeding 1,500 cc but not exceeding 2,500 cc	4,345	4,690
exceeding 2,500 cc but not exceeding 3,500 cc	5,775	6,235
exceeding 3,500 cc but not exceeding 4,500 cc	7,210	7,785
exceeding 4,500 cc	8,585	9,270
additional fee for private car using diesel fuel	1,115	1,205
<u>Electrically powered passenger vehicles</u>		
not exceeding 1 tonne	340	365
for each additional 250 kg	70	75
<u>Motor Cycle</u>	920	990
<u>Motor Tricycle</u>	920	990

## Appendix F(2) (cont'd)

(i) VEHICLE AND DRIVING LICENCE FEES (cont'd)

	<u>Existing</u> <u>fees</u> (\$)	<u>Proposed</u> <u>fees</u> (\$)
<u>Public Light Bus</u>	6,360	6,870
<u>Private Light Bus</u>	2,015	2,175
<u>Public Bus</u>		
for the driver	17	20
additional fee for each seat	39	40
<u>Private Bus</u>		
for the driver	17	20
additional fee for each seat	34	35
<u>Trailer</u>		
for each 250 kg or part thereof	22	25
<u>Invalid Carriage</u>	10	10

## Appendix F(2)(cont'd)

(ii) DEPOSIT-TAKING COMPANY LICENCE AND REGISTRATION FEES

	<u>Existing fee (\$)</u>	<u>Proposed fee (\$)</u>
1. Registration fee (section 23(1))	54,000	62,100
2. Renewal of registration fee (section 23(2))	54,000	62,100
3. Deposit-taking licence fee (section 26(1))	183,600	211,140
4. Renewal of deposit-taking licence fee (section 26(2))	183,600	211,140
5. Fee for the establishment of a local branch of a deposit-taking company (section 45(1))	9,180	10,500
6. Annual fee for maintaining a local branch of a deposit-taking company (section 45(1) and (2))	9,180	10,500
7. Fee for the establishment of an overseas branch of a deposit-taking company (section 51(1))	18,360	21,100
8. Annual fee for maintaining an overseas branch of a deposit-taking company (section 51(1) and (2))	18,360	21,100
9. Fee for the establishment of an overseas representative office of a deposit-taking company (section 51(1))	9,180	10,500
10. Annual fee for maintaining an overseas representative office of a deposit-taking company (section 51(1) and (2))	9,180	10,500

## Appendix F(3)

(1) BROAD EFFECT OF THE INCREASE IN BASIC PERSONAL ALLOWANCE  
ON SINGLE AND MARRIED TAXPAYERS IN 1989-90

	<u>Single Persons</u>	<u>Married Couples</u>	<u>Total</u>
(a) Number of taxpayers who will receive:			
<b>Full Benefit</b> - no tax liability	41,000	19,000	60,000
<b>Partial Benefit</b> - reduced tax liability	467,000	205,500	672,500
(b) Number of taxpayers who will receive <b>no benefit</b> from the increase in personal allowance but the <b>full benefit</b> of the reduction in the standard rate of tax	18,000	39,500	57,500
Total	<u>526,000</u>	<u>264,000</u>	<u>790,000</u>

Appendix F(3) (Cont'd)

(ii) A Projection of the distribution of Single and Married Taxpayers by different income groups in 1989-90

<u>Single</u>	<u>No. of taxpayers</u>
Low Income Group (ie.those with income below \$90,000)	386 500
Middle Income Group (ie.those with income between \$90,000 and \$160,000)	72 500
High Income Group (ie.those with income in excess of \$160,000)	26 000
 <u>Married</u>	
Low Income Group (ie.those with income below \$130,000)	73 300
Middle Income Group (ie.those with income between \$130,000 and \$260,000)	110 700
High Income Group (ie.those with income in excess of \$260,000)	61 000
<b>Total after Budget concessions</b>	<b>730 000</b>
 <u>Add:</u>	
No. of Taxpayers estimated to fall out and be kept out of the tax net [on account of the budget concessions but liable to pay 1988-89 final tax in 1989-90]	60 000
<b>Total no. of Taxpayers estimated to pay tax in 1989-90</b>	<b>790 000</b>

Appendix B.3.3 (Cont'd)

(1.1) EXAMPLES OF THE EFFECT THE PROPOSED INCREASE IN BASIC PERSONAL ALLOWANCE AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Single person

Annual income (\$)	Present tax payable (Exemption level: \$36,000)		Proposed tax payable (Exemption level: \$39,000)		Effective rate (%)	Tax Saving (A) - (B) (\$)	Remarks	
	Amount (A) (\$)	Effective rate (%)	Amount (B) (\$)	Effective rate (%)				
37,000	33	0.1	-	-	-	33	This group will <u>not</u> be required to pay tax as a result of the increase in basic personal allowance.	
39,000	99	0.3	-	-	-	99		
42,000	198	0.5	99	0.2	0.2	99	This group will have <u>reduced</u> tax liabilities as a result of the increase in basic personal allowance.	
48,000	492	1.0	297	0.6	0.6	195		
60,000	1,476	2.5	1,179	2.0	2.0	297		
72,000	2,952	4.1	2,556	3.6	3.6	396		
84,000	5,004	6.0	4,425	5.3	5.3	579		
96,000	7,560	7.9	6,867	7.2	7.2	693		
106,000	10,150	9.6	9,325	8.8	8.1	825		
109,000	10,900	10.0	10,150	9.3	6.9	750		
120,000	13,650	11.4	12,900	10.8	5.5	750		
132,000	16,650	12.6	15,900	12.0	4.5	750		
144,000	19,650	13.6	18,900	13.1	3.8	750		
168,000	25,650	15.3	24,900	14.8	2.9	750		
(171,000)	26,400	15.4	25,650	15.0	2.8	750		Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.
(172,105)	26,676	15.5	25,815	15.0	3.2	861		

## Appendix F (3) (Cont'd)

## (iv) EXAMPLES OF THE EFFECT THE PROPOSED INCREASES IN BASIC PERSONAL AND DEPENDENT PARENT ALLOWANCES AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Single person, with two dependent parents

Annual income	Present tax payable (Exemption level: \$54,182)		Proposed tax payable (Exemption level: \$59,000)		Effective rate	Amount (B)	Effective rate	Tax Saving (A) - (B)	Remarks
	Amount (A)	Effective rate (%)	Amount (B)	Effective rate (%)					
	(\$)	(%)	(\$)	(%)				(\$)	(%)
56,000	60	0.1	-	-	-	-	-	60	100.0
59,000	159	0.3	-	-	-	-	-	159	100.0
60,000	192	0.3	33	0.1	0.1	33	159	159	82.8
72,000	876	1.2	558	0.8	0.8	558	318	318	36.3
84,000	2,136	2.5	1,575	1.9	1.9	1,575	561	561	26.3
96,000	3,900	4.1	3,105	3.2	3.2	3,105	795	795	20.4
106,000	5,760	5.4	4,806	4.5	4.5	4,806	954	954	16.6
109,000	6,300	5.8	5,400	5.0	5.0	5,400	900	900	14.3
120,000	8,650	7.2	7,560	6.3	6.3	7,560	1,090	1,090	12.6
132,000	11,650	8.8	10,400	7.9	7.9	10,400	1,250	1,250	10.7
144,000	14,650	10.2	13,400	9.3	9.3	13,400	1,250	1,250	8.5
156,000	17,650	11.3	16,400	10.5	10.5	16,400	1,250	1,250	7.1
168,000	20,650	12.3	19,400	11.5	11.5	19,400	1,250	1,250	6.1
180,000	23,650	13.1	22,400	12.4	12.4	22,400	1,250	1,250	5.3
192,000	26,650	13.9	25,400	13.2	13.2	25,400	1,250	1,250	4.7
204,000	29,650	14.5	28,400	13.9	13.9	28,400	1,250	1,250	4.2
(224,737)	34,834	15.5	33,584	14.9	14.9	33,584	1,250	1,250	3.6
(226,000)	35,030	15.5	33,900	15.0	15.0	33,900	1,130	1,130	3.2

This group will not be required to pay tax as a result of the increases in basic personal and dependent parent allowances.

This group will have reduced tax liabilities as a result of the increases in basic personal and dependent parent allowances.

Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.

Appendix 1 (3) (Cont'd)

(v) EXAMPLES OF THE EFFECT THE PROPOSED INCREASES IN BASIC PERSONAL AND CHILD ALLOWANCES, INTRODUCTION OF A SINGLE PARENT ALLOWANCE OF \$20,000 AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Single person, with one child

Annual income	Present tax payable (Exemption level: \$46,909)		Proposed tax payable (Exemption level: \$69,000)		Effective rate	Amount (B)	Effective rate	Tax Saving (A) - (B)	Remarks
	Amount (A)	Effective rate (%)	Amount (B)	Effective rate (%)					
	(\$)	(%)	(\$)	(%)				(\$)	(%)
50,000	102	0.2	-	-	-	-	-	102	100.0
60,000	564	0.9	-	-	-	-	564	564	100.0
69,000	1,287	1.9	-	-	-	-	1,287	1,287	100.0
72,000	1,584	2.2	99	0.1	0.1	99	1,485	1,485	93.8
84,000	3,120	3.7	690	0.8	0.8	690	2,430	2,430	77.9
96,000	5,220	5.4	1,773	1.8	1.8	1,773	3,447	3,447	66.0
106,000	7,350	6.9	3,105	2.9	2.9	3,105	4,245	4,245	57.8
109,000	7,980	7.3	3,600	3.3	3.3	3,600	4,380	4,380	54.9
120,000	10,650	8.9	5,400	4.5	4.5	5,400	5,250	5,250	49.3
132,000	13,650	10.3	7,770	5.9	5.9	7,770	5,880	5,880	43.1
144,000	16,650	11.6	10,650	7.4	7.4	10,650	6,000	6,000	36.0
156,000	19,650	12.6	13,650	8.8	8.8	13,650	6,000	6,000	30.5
168,000	22,650	13.5	16,650	9.9	9.9	16,650	6,000	6,000	26.5
180,000	25,650	14.3	19,650	10.9	10.9	19,650	6,000	6,000	23.4
192,000	28,650	14.9	22,650	11.8	11.8	22,650	6,000	6,000	20.9
(203,684)	31,571	15.5	25,571	12.6	12.6	25,571	6,000	6,000	19.0
(253,500)	39,292	15.5	38,025	15.0	15.0	38,025	1,267	1,267	3.2

This group will not be required to pay tax as a result of the increases in basic personal and child allowances and the introduction of a single parent allowance.

This group will have reduced tax liabilities as a result of the increases in basic personal and child allowances and the introduction of a single parent allowance.

Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.



Appendix B (Cont'd)

(vii) EXAMPLES OF THE EFFECT THE PROPOSED INCREASES IN BASIC PERSONAL AND CHILD ALLOWANCES AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Married person, with two children

Annual income	Present tax payable (Exemption level: \$92,636)		Proposed tax payable (Exemption level: \$100,000)		Effective rate	Tax Saving (A) - (B)	Remarks
	Amount (A)	Effective rate (%)	Amount (B)	Effective rate (%)			
	(\$)	(%)	(\$)	(%)		(\$)	(%)
94,000	45	0.1	-	-	-	45	100.0
96,000	111	0.1	-	-	-	111	100.0
100,000	243	0.2	-	-	-	243	100.0
108,000	714	0.7	264	0.2	0.2	450	63.0
120,000	1,812	1.5	1,080	0.9	0.9	732	40.4
132,000	3,495	2.6	2,424	1.8	1.8	1,071	30.6
144,000	5,670	3.9	4,260	3.0	3.0	1,410	24.9
156,000	8,337	5.3	6,636	4.3	4.3	1,701	20.4
168,000	11,625	6.9	9,600	5.7	5.7	2,025	17.4
180,000	14,925	8.3	12,900	7.2	7.2	2,025	13.6
192,000	18,225	9.5	16,200	8.4	8.4	2,025	11.1
204,000	21,525	10.6	19,500	9.6	9.6	2,025	9.4
214,000	24,275	11.3	22,250	10.4	10.4	2,025	8.3
220,000	25,775	11.7	23,900	10.9	10.9	1,875	7.3
228,000	27,775	12.2	25,900	11.4	11.4	1,875	6.8
240,000	30,775	12.8	28,900	12.0	12.0	1,875	6.1
252,000	33,775	13.4	31,900	12.7	12.7	1,875	5.6
288,000	42,775	14.9	40,900	14.2	14.2	1,875	4.4
(307,631)	47,682	15.5	45,807	14.9	14.9	1,875	3.9
(311,000)	48,205	15.5	46,650	15.0	15.0	1,555	3.2

This group will not be required to pay tax as a result of the increases in basic personal and child allowances.

This group will have reduced tax liabilities as a result of the increases in basic personal and child allowances.

Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.

Appendix F (3)(Cont'd)

## (viii) EXAMPLES OF THE EFFECT THE PROPOSED INCREASES IN BASIC PERSONAL, CHILD AND DEPENDENT PARENT ALLOWANCES AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Married person, with two children and two dependent parents

Annual income	Present tax payable (Exemption level: \$110,818)		Proposed tax payable (Exemption level: \$120,000)		Tax Saving (A) - (B)	Remarks
	Amount (A)	Effective rate (%)	Amount (B)	Effective rate (%)		
	(\$)	(%)	(\$)	(%)	(\$)	(%)
112,000	39	0.1	-	-	39	100.0
116,000	171	0.1	-	-	171	100.0
120,000	306	0.3	-	-	306	100.0
132,000	1,197	0.9	492	0.4	705	58.9
144,000	2,580	1.8	1,476	1.0	1,104	42.8
156,000	4,455	2.9	2,952	1.9	1,503	33.7
168,000	6,909	4.1	5,004	3.0	1,905	27.6
180,000	9,925	5.5	7,560	4.2	2,365	23.8
192,000	13,225	6.9	10,700	5.6	2,525	19.1
204,000	16,525	8.1	14,000	6.9	2,525	15.3
214,000	19,275	9.0	16,750	7.8	2,525	13.1
220,000	20,775	9.4	18,400	8.4	2,375	11.4
228,000	22,775	10.0	20,400	8.9	2,375	10.4
240,000	25,775	10.7	23,400	9.8	2,375	9.2
252,000	28,775	11.4	26,400	10.5	2,375	8.3
288,000	37,775	13.1	35,400	12.3	2,375	6.3
324,000	46,775	14.4	44,400	13.7	2,375	5.1
(360,263)	55,840	15.5	53,465	14.8	2,375	4.3
(366,000)	56,730	15.5	54,900	15.0	1,830	3.2

This group will not be required to pay tax as a result of the increases in basic personal, child and dependent parent allowances.

This group will have reduced tax liabilities as a result of the increases in basic personal, child and dependent parent allowances.

Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.

Appendix B, Pt. 3 (cont'd)

(15.) EXAMPLES OF THE EFFECT THE PROPOSED INCREASES IN BASIC PERSONAL, CHILD AND DEPENDENT PARENT ALLOWANCES AND REDUCTION IN THE STANDARD RATE WILL HAVE ON SALARIES TAX AT VARIOUS INCOME LEVELS

Married person, with two children, two dependent parents and working wife allowance\*

Annual income	Present tax payable (Exemption level: \$124,455)		Proposed tax payable (Exemption level: \$133,636)		Tax Saving (A) - (B)	Remarks	
	Amount (A)	Effective rate	Amount (B)	Effective rate			
(\$)	(\$)	(%)	(\$)	(%)	(\$)	(%)	
132,000	249	0.2	-	-	249	100.0	This group will <u>not</u> be required to pay tax as a result of the increases in basic personal, child and dependent parent allowances.
144,000	1,035	0.7	384	0.3	651	62.9	
156,000	2,364	1.5	1,314	0.8	1,050	44.4	This group will have <u>reduced</u> tax liabilities as a result of the increases in basic personal, child and dependent parent allowances.
168,000	4,185	2.5	2,736	1.6	1,449	34.6	
180,000	6,531	3.6	4,680	2.6	1,851	28.3	
192,000	9,475	4.9	7,182	3.7	2,293	24.2	
204,000	12,775	6.3	10,250	5.0	2,525	19.8	
214,000	15,525	7.3	13,000	6.1	2,525	16.3	
220,000	17,025	7.7	14,650	6.7	2,375	14.0	
228,000	19,025	8.3	16,650	7.3	2,375	12.5	
240,000	22,025	9.2	19,650	8.2	2,375	10.8	
252,000	25,025	9.9	22,650	9.0	2,375	9.5	
288,000	34,025	11.8	31,650	11.0	2,375	7.0	
324,000	43,025	13.3	40,650	12.5	2,375	5.5	
( 399,737)	61,959	15.5	59,584	14.9	2,375	3.8	Standard Rate taxpayers will have reduced tax liabilities as a result of the reduction in the standard rate of tax.
( 403,500)	62,542	15.5	60,525	15.0	2,017	3.2	

\* The examples shown above are calculated on the basis that the wife's income is in excess of the Working Wife Allowance of \$15,000

Appendix F(3)(Cont'd)

(x) INCOME LEVELS BELOW WHICH SALARIES TAXPAYERS  
ARE NOT REQUIRED TO PAY TAX

	Present		Proposed	
	Without working wife allowance	With working * wife allowance	Without working wife allowance	With working * wife allowance
	(\$)	(\$)	(\$)	(\$)
<u>No dependent parent</u>				
Single	36,001	-	39,001	-
Married	74,001	87,637	80,001	93,637
Married + 1 child	84,910	98,546	91,819	105,456
Married + 2 children	92,637	106,274	100,001	113,637
Married + 3 children	95,365	109,001	102,728	116,365
<u>Including two dependent parents</u>				
Single	54,183	-	59,001	-
Married	92,183	105,819	100,001	113,637
Married + 1 child	103,092	116,728	111,819	125,456
Married + 2 children	110,819	124,456	120,001	133,637
Married + 3 children	113,546	127,183	122,728	136,365
<u>Including two dependent parents with additional allowance</u>				
Single	59,637	-	64,456	-
Married	97,637	111,274	105,456	119,092
Married + 1 child	108,546	122,183	117,274	130,910
Married + 2 children	116,274	129,910	125,456	139,092
Married + 3 children	119,001	132,637	128,183	141,819

\* The examples above are calculated on the basis that the wife's income is in excess of the working wife allowance of \$15,000.

## Appendix F(3)(Cont'd)

(xi) INCOME LEVELS ABOVE WHICH SALARIES TAXPAYERS BEGIN  
TO PAY TAX AT THE MAXIMUM 25% MARGINAL RATE

	Present		Proposed	
	Without working wife allowance	With working * wife allowance	Without working wife allowance	With working * wife allowance
	(\$)	(\$)	(\$)	(\$)
<u>No dependent parent</u>				
Single	99,636	-	102,636	-
Married	137,636	151,273	143,636	157,273
Married + 1 child	148,545	162,182	155,455	169,091
Married + 2 children	156,273	169,909	163,636	177,273
Married + 3 children	159,000	172,636	166,364	180,000
<u>Including two dependent parents</u>				
Single	119,000	-	124,000	-
Married	155,818	169,455	163,636	177,273
Married + 1 child	166,727	180,364	175,455	189,091
Married + 2 children	174,455	188,091	183,636	197,273
Married + 3 children	177,182	190,818	186,364	200,000
<u>Including two dependent parents with additional allowance</u>				
Single	125,000	-	130,000	-
Married	161,273	174,909	169,091	182,727
Married + 1 child	172,182	185,818	180,909	194,545
Married + 2 children	179,909	193,545	189,091	202,727
Married + 3 children	182,636	196,273	191,818	205,455

\* The examples above are calculated on the basis that the wife's income is in excess of the **working wife allowance** of \$15,000.

## Appendix F (3)(Cont'd)

(xii) INCOME LEVELS AT WHICH SALARIES TAXPAYERS  
ENTER THE STANDARD RATE ZONE

	Present		Proposed	
	Without working wife allowance	With working * wife allowance	Without working wife allowance	With working * wife allowance
	(\$)	(\$)	(\$)	(\$)
<u>No dependent parent</u>				
Single	172,105	-	171,000	-
Married	253,684	293,158	256,000	293,500
Married + 1 child	285,263	324,737	288,500	326,000
Married + 2 children	307,631	347,105	311,000	348,500
Married + 3 children	315,526	355,000	318,500	356,000
<u>Including two dependent parents</u>				
Single	224,737	-	226,000	-
Married	306,315	345,789	311,000	348,500
Married + 1 child	337,895	377,368	343,500	381,000
Married + 2 children	360,263	399,737	366,000	403,500
Married + 3 children	368,158	407,631	373,500	411,000
<u>Including two dependent parents with additional allowance</u>				
Single	240,526	-	241,000	-
Married	322,105	361,579	326,000	363,500
Married + 1 child	353,684	393,158	358,500	396,000
Married + 2 children	376,053	415,526	381,000	418,500
Married + 3 children	383,947	423,421	388,500	426,000

\* The examples above are calculated on the basis that the wife's income is in excess of the **working wife allowance** of \$15,000.

## Appendix F(3)(Cont'd)

(xiii) ANALYSIS OF ESTIMATED SALARIES TAX YIELD (AFTER  
BUDGET CONCESSIONS) BY INCOME GROUP IN 1989-90

Assessable income group per annum (\$)	No. of taxpayers	Percentage of total taxpayers (%)	Tax yield (\$M)	Percentage of total yield (%)
50,000 & under	175 000	22.1	30	0.3
50,001 - 100,000	300 000	38.0	670	6.9
100,001 - 240,000	236 000	29.9	2,520	25.9
240,001 - 300,000	24 000	3.0	1,030	10.6
300,001 - 500,000	34 500	4.4	2,400	24.6
500,001 & over	20 500	2.6	3,090	31.7
<u>Total</u>	<u>790 000</u>	<u>100.0</u>	<u>9,740</u>	<u>100.0</u>

Of 790,000 taxpayers only 57,500 (or 7.3%) are estimated to pay tax at the standard rate of 15% in 1989-90. This small group of taxpayers, however, will contribute about \$5.5 billion or 56% of the total tax yield and is composed of -

18,000	single persons with annual incomes of \$171,000 or more;
16,700	married couples with annual incomes of \$256,000 or more; and
22,800	married couples with one or more children and/or dependent parents and with annual incomes of \$288,500 or more.