THE 2013-14 BUDGET

Speech by the Financial Secretary, the Hon John C Tsang moving the Second Reading of the Appropriation Bill 2013

Wednesday, 27 February 2013

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This speech, together with the supplement and appendices relating to the 2013-14 Budget, is available at www.budget.gov.hk.

Mr President,

I move that the Appropriation Bill 2013 be read a second time.

Introduction

2. Last month, the Chief Executive announced a series of new policies worth $60 billion in the first Policy Address of the current-term Government. I shall provide financial resources to fully support these initiatives. In this Budget, I am going to introduce proposals in four areas, namely developing the economy, optimising human resources, investing in infrastructure and caring for people's livelihood. I shall also share my thinking about future challenges posed by an ageing population. The package of measures in this Budget will have a stimulus effect of 1.3 percentage points. I hope that with these measures, we shall not only promote economic growth and invest in the future, but also improve employment opportunities and people's livelihood in a bid to address the aspirations of different sectors of the community.

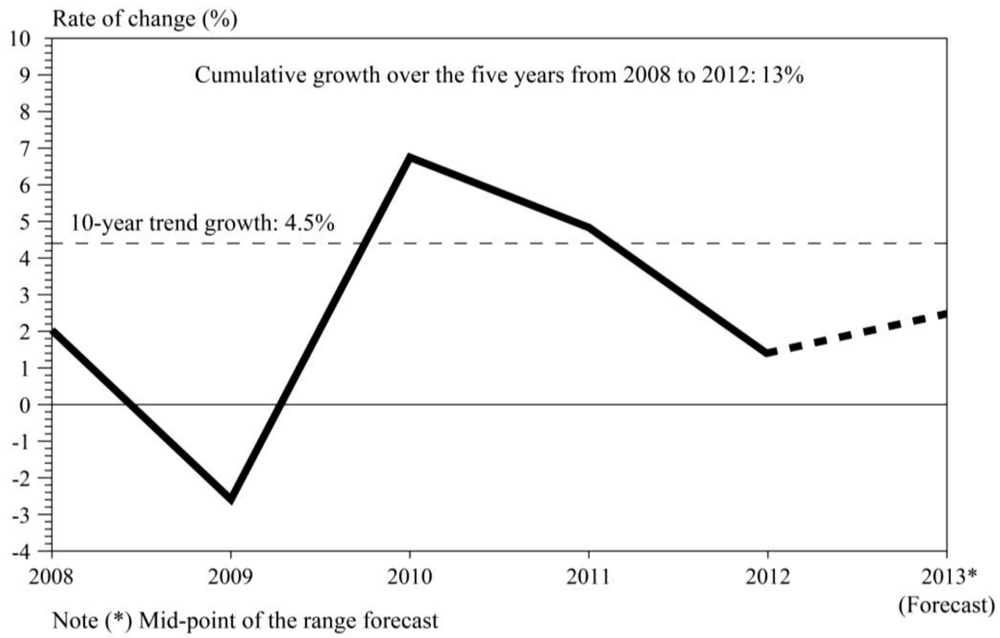
3. This is my sixth year as Financial Secretary. Looking back, the Hong Kong economy survived a number of major challenges that threatened to bring our external trade and economic growth to a standstill, take unemployment to an all-time high and see investor confidence fall to an all-time low. I am honoured to have contributed to and steered through the economic rebound and consolidation, shoulder to shoulder with the Hong Kong community. But the road ahead remains bumpy. Challenges to Hong Kong's economic growth, commerce and trading, public finance, financial services, land and development matters abound. With resolve and commitment to serve for the coming five years, I shall continue to do my level best to nurture and grow our economy, to keep Hong Kong a land of opportunities, a place that values fair and just opportunities while caring for the less privileged: a place we truly call home.

Economic Performance in 2012

4. The external environment was unfavourable in 2012. In general, there were setbacks in external trade over the year, but domestic demand was stable. Due to weak demand from the advanced economies, the overall economy saw sub-trend growth throughout the year. GDP growth for 2012 as a whole was only 1.4 per cent, much lower than the average of 4.5 per cent over the past ten years.

Chart 1

Real Gross Domestic Product



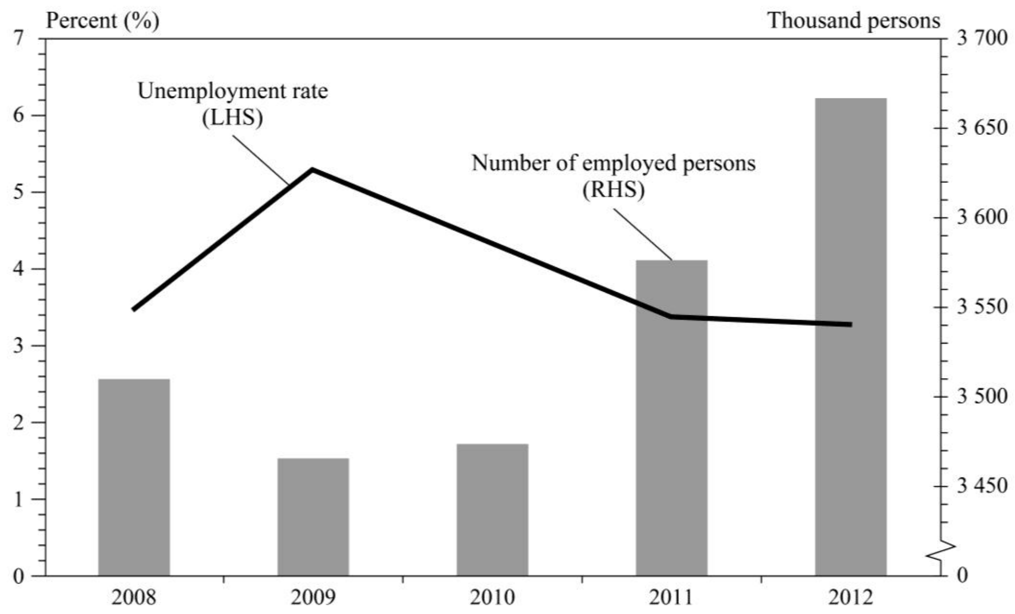
5. The weak fundamentals of the European and US economies weighed on the trade flows in Asia. Hong Kong's exports of goods declined in the second quarter of 2011, the export performance remained weak in the first half of 2012 and improved slightly in the second half. For 2012, exports of goods saw moderate growth by only 1.3 per cent in real terms. Exports of services were also dragged down by the unfavourable external environment and grew by only 1.2 per cent in real terms in 2012.

6. The domestic sector maintained stable growth in 2012. Thanks to high employment and improved income, private consumption grew by four per cent in real terms for the year. Despite rather cautious business sentiments, building and construction activities as well as machinery and equipment acquisition remained buoyant, further driving up overall investment spending by 9.1 per cent last year.

7. Realising that our economy was facing a huge downward risk, I introduced a package of measures in my Budget last year which stimulated a GDP growth of 1.5 percentage points. These measures were mainly to support small and medium enterprises (SMEs), help our people, preserve employment and lessen the impact of the economic slowdown. The labour market remained stable in 2012. Despite a slight rebound in the unemployment rate from its low of 3.2 per cent in mid-year to the latest 3.4 per cent, the labour market was still in a state of full employment.

Chart 2

Number of Employed Persons and Unemployment Rate

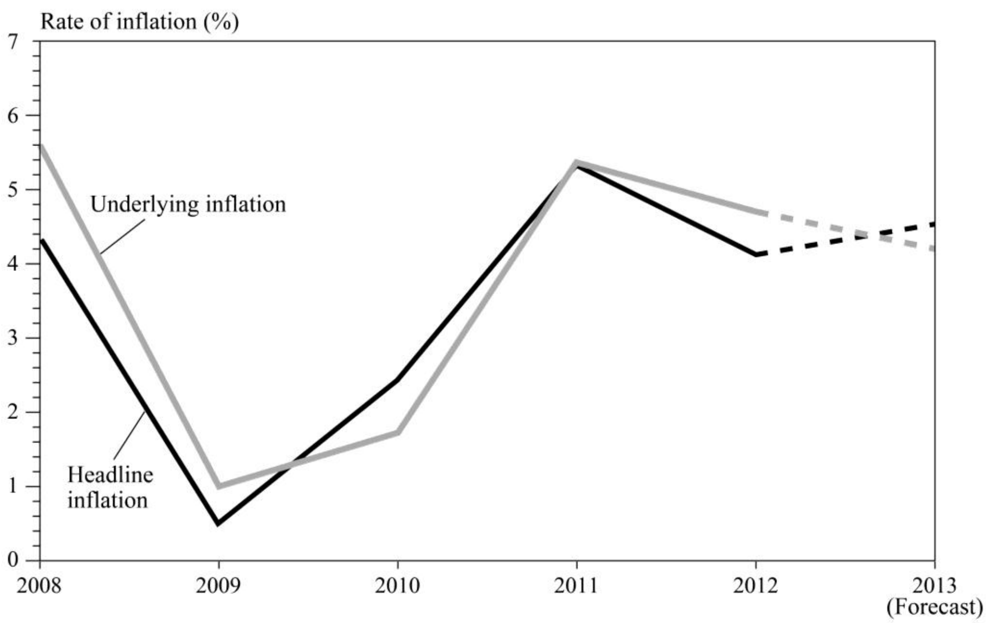


8. There was a real increase in pay in 2012, even though economic growth was slow and the impact of Minimum Wage has faded. Averaged over the previous year, the pay and wage in the first three quarters of 2012 rose by 6.7 per cent and 5.9 per cent respectively, representing increases of 2.5 per cent and 1.9 per cent in real terms after discounting inflation.

9. Inflation has dropped continuously since early last year. This is partly attributed to the reduction in imported inflation due to the retreat of international food and commodity prices and easing inflation in our major import sources. Another contributing factor is the slight reduction in local costs as a result of economic slowdown. The headline inflation rate dropped from a peak of 6.4 per cent in the third quarter of 2011 to 3.8 per cent in the fourth quarter of 2012, averaging 4.1 per cent for 2012 as a whole. Netting out the effects of the Government’s one-off relief measures, the underlying inflation rate fell from 6.4 per cent in the fourth quarter of 2011 to 3.8 per cent in the fourth quarter of 2012, averaging 4.7 per cent for 2012 as a whole.

Chart 3

Composite Consumer Price Index



Economic Outlook for 2013

10. 2013 will be a challenging year. While the US has made some progress in tackling its fiscal problems, the pace of its economic recovery remains slow. Though the European debt crisis has temporarily stabilised, the economies there have already plunged into recession. Japan is beset by high debts, and it is difficult to tell whether the Japanese government's stimulus measures will help renew economic growth. Taking a macro perspective of the world's economy, continued modest growth is expected amid downside risks. The quantitative easing programmes launched by the advanced economies facing a prolonged economic downturn will lead to fluctuations in the markets, ultra-abundant liquidity with unpredictable fund flows, and potentially give rise to stronger protectionist sentiments. This, combined with various geopolitical factors, will cast a negative outlook for global trade.

11. The intricate external environment will remain unstable in the year ahead. The whole world will have to face wars on three fronts, namely "currency", "trade" and "geopolitics". As a highly open and small economy, Hong Kong will be impacted by the development of these wars to a certain extent.

12. Fundamentals in Asia remain strong and the Mainland economy regained its growth momentum in the fourth quarter of last year. Barring an abrupt deterioration in the demand from the advanced economies, Hong Kong's external trade should see some improvement. On the domestic front, buoyed by the largely stable labour market, local consumption is expected to sustain modest growth. The pick-up in construction works and vibrant inbound tourism will remain the driving force of domestic demand this year. I expect a modest improvement in our economy this year and forecast Gross Domestic Product (GDP) growth of 1.5 to 3.5 per cent for the year. This growth rate is still lower than the average over the past decade and there may be some upward pressure on the unemployment rate.

13. The inflationary trend will be affected by the internal and external environments as well as overall demand. On the external front, we must not overlook the risk of increasing international commodity and asset prices arising from excessive global liquidity. Moreover, new rounds of quantitative easing in Europe, the US and Japan may trigger another round of imported inflation. Locally, slow economic growth has eased the pressure on wages. However, given the upcoming upward adjustment to the Minimum Wage in the middle of this year coupled with the persistently high rental levels, inflation will face upward pressure. The average headline inflation rate for 2013 is estimated at 4.5 per cent, with the underlying inflation at 4.2 per cent.

Developing the Economy and Increasing Employment

14. As the world's economic balance shifts to Asia, Hong Kong should ride the wave of the new order by capitalising on our unique advantages and exploring new business opportunities to take Hong Kong's economy to new heights.

15. During the Budget consultation, many people mentioned the role of the Government in the development of a market economy, and the general consensus was that the free and open mode of economic development which had been the key to Hong Kong's success should be maintained. We maintain a simple and low tax regime while prudently controlling government expenditure to leave most of the wealth to the market and the public. Entrepreneurs, investors and members of the public are free to make their own decisions on business, investment and employment issues, making it possible to use the limited resources more effectively.

16. This does not mean that the Government is merely reactive. In fact, the Government has been playing a pivotal role in the market economy, especially in times of market failure when it takes steps to restore the market balance to ensure that the community can share the fruits of economic growth. The Government acts as provider of public service, mediator in the allocation of public resources as well as negotiator in discussions with other governments. As I see it, government participation and market operation are complementary concepts. What matters is how to make the two work together, and how to strike a balance between social costs and benefits.

17. The current-term Government will continue to count on market forces and act in a rational and pragmatic manner in collaborating with the market to grasp development opportunities and create a better business environment to foster robust economic growth underpinned by our established strengths and foundations. The ultimate objective of economic policies is not about chasing after statistics. It is about expanding the scale of Hong Kong's economy, promoting the holistic development of our society and creating more business and job opportunities so that our people can realise their aspirations and improve their living standards. At the same time, the Government will distribute social resources effectively through appropriate policies and measures so that the needy can be provided with appropriate relief and become self-reliant.

18. To promote future economic development, we must work on two areas. First, we must foster our economic integration with the Mainland to take advantage of its market development. We know the huge Mainland market well. The Government will make good use of all Government-to-Government (G2G) platforms to help Hong Kong enterprises expand their Mainland business, channel overseas capital to the Mainland market, and support Mainland enterprises in "going global". More importantly, we must at the same time preserve Hong Kong's characteristics as an international city. We must recognise our biggest advantages - a sound legal system, a level-playing field and an excellent business environment. We treasure our core values of individual freedoms, the rule of law and a clean government, which align us with the international system. We shall support our enterprises by strengthening opportunities in traditional markets, exploring new areas of growth and opening up more new markets.

19. The Economic Development Commission established by the Chief Executive will provide a new platform for the Government to work with the market in the promotion of economic development. It will develop ideas, advise on strategies and policies, examine the structure of different industries, and explore measures for their development.

20. Second, we must expand and strengthen our pillar industries to maintain our competitiveness. We must also support the development of new industries, build a more diversified and solid economic base, and provide more career choices for our younger generation to realise their potential.

21. Traditional pillar industries have been the major driving forces behind Hong Kong’s economic development. They have clear advantages internationally and are highly competitive. Currently, the four pillar industries - trading and logistics, tourism, financial services and business and professional services employ 1.7 million people, or 48 per cent of the total labour force. These pillar industries contribute to 59 per cent of our GDP. With a large economic base, they serve as a powerful driver for related sectors and the job market as well. I shall now introduce measures to further promote these industries.

Consolidating Trading and Logistics Industry

22. The trading and logistics industry consolidates different economic and production activities, and creates numerous jobs with different requirements for academic qualifications, skills and experience. The industry currently employs 770 000 workers and contributes to one quarter of GDP, the highest among the four pillar industries.

Modern Logistics Services

23. Due to changes in market demand, the industry is moving towards the provision of high value-added logistics services. Hong Kong is developing into a regional distribution centre for high-value goods, which differs from its conventional role in transporting components, semi-finished products and finished products.

24. With an efficient intermodal transport network, the status of a free port and a sound legal system to protect intellectual property, Hong Kong has an edge in handling and distributing high-value goods to markets in the region. Our responsive and efficient logistics enterprises can provide high value-added and "tailor-made" services to cater for the different needs of customers in respect of supply chain management. Our logistics industry has potential to further expand its regional services, thereby strengthening Hong Kong's position as a logistics hub.

25. We need to build dedicated facilities to help the development of high value-added logistics services which will help shorten operating time and reduce logistics and inventory costs. We have reserved a logistics site with an area of about two hectares at Tsing Yi which will be put on the market in the first half of this year. We also plan to designate about ten hectares of land at Tuen Mun West for the development of logistics facilities. This will facilitate clustering of companies involved in various operations and services for the industry. Tuen Mun West is an ideal site for this. Upon completion of the Tuen Mun-Chek Lap Kok Link in 2018, it will only take ten minutes to travel from Tuen Mun West to the Airport. We shall conduct a feasibility study on the proposed development and shall release the logistics sites in Tuen Mun West in phases.

26. Upon completion of the logistics facilities at Tsing Yi and Tuen Mun West, more than 300 000 square metres of floor area and 7 500 new jobs in various trades will be provided, yielding over $3 billion worth of economic benefits annually.

Facilitating the Flow of Goods

27. After the 911 incident in the US, various countries enhanced their air cargo security requirements. It is imperative that our freight and logistics operators make early moves to gain greater international recognition in cargo safety and management. This will facilitate the customs clearance of our export overseas, and maintain Hong Kong's competitive advantage as a logistics hub.

28. The Customs and Excise Department (C&ED) launched the Hong Kong Authorised Economic Operator Programme last April. The Programme accredits local companies with sound internal safety and management systems in accordance with international criteria, giving their consignments customs facilitation, including prioritised clearance and simpler inspection procedures. The C&ED has liaised with other customs authorities to seek mutual recognition of similar programmes, so that locally-accredited companies can enjoy corresponding preferential treatment outside Hong Kong. The C&ED will allocate additional resources to boost companies' participation in the Programme and promote mutual recognition.

Transport Infrastructure

29. To enhance the external connectivity of our transport network, we shall continue to push ahead with the planning and implementation of, sea, land and air transport infrastructure projects.

30. Regarding the proposal of constructing Container Terminal 10 at Southwest Tsing Yi, we are conducting a study to examine the technical feasibility and assess the environmental impact of the proposal. The Study on the Strategic Development Plan for Hong Kong Port 2030 is also under way to update port cargo growth forecasts and explore how to make better use of the existing port facilities to support future development. Both studies are scheduled for completion in the first half of this year. In deciding on the need to construct Container Terminal 10, we shall take into account, among other things, the studies' results and the economic situation and the views of stakeholders.

31. On land transport, the local projects of the Hong Kong-Zhuhai-Macao Bridge are scheduled for completion in 2016 to tie in with the opening of the main bridge. This bridge connection will become part of a strategic road network linking Hong Kong, Zhuhai, Macao and Shenzhen. The Western Pearl River Delta (PRD) will fall within a three-hour commute from Hong Kong. The airport and container ports in Hong Kong can be used for transporting goods from the Western PRD, Guangxi Province and nearby countries such as Vietnam and Thailand. This will strengthen Hong Kong's position as a trade, logistics and aviation hub.

32. On air transport, the Airport Authority Hong Kong (AA) has commenced an environmental impact assessment and other planning for the three-runway system, which is expected to cope with air traffic demand up to at least 2030. The Government will decide on the development of the three-runway system when all relevant information is available.

Emerging Markets

33. Supporting local enterprises to tap new markets, facilitating trade flows and promoting economic development are important roles of the Government. The Government's work in this area is of particular importance to the development of the modern trading and logistics industry. With our country's strong support, Hong Kong has submitted to the Association of Southeast Asian Nations (ASEAN) a request to join the China-ASEAN Free Trade Area to assist our traders to further tap into the emerging Southeast Asian market. ASEAN member states are currently considering our proposed accession, and conducting internal consultations and studies. We shall continue our lobbying work, and collaborate with the Hong Kong Trade Development Council (HKTDC) and local trade associations to organise more business missions and discussion forums to enhance interaction between Hong Kong and ASEAN businesses.

34. Our efforts to tap emerging markets have started to deliver results. Over the past five years, with more frequent communication through G2G platforms, the trade in goods between Hong Kong and the BRICS countries grew substantially by over 40 per cent in value. Amongst the BRICS countries, our bilateral trade with India registered cumulative growth of over 90 per cent while that with Russia even increased by 1.5 times. To further diversify Hong Kong's export network, we shall continue our efforts to promote Hong Kong in and strengthen trade links with emerging markets.

Promoting Tourism Industry

35. Tourism is another mainstay of our economy, employing some 230 000 people and accounting for 4.5 per cent of GDP. In 2012, there were over 48 million visitors to Hong Kong, an increase of 16 per cent over 2011. Despite the gloomy global economic outlook, total spending associated with inbound tourism increased 16.5 per cent to exceed $300 billion.

36. Buoyant tourism will undoubtedly put pressure on our control points, hotels, tourist attractions and shopping centres. To sustain the healthy development of the tourism industry, we need to devote more efforts to enhancing tourism infrastructure, hotel supply, market promotion, service support, etc.

37. Last year, I announced that the Government would look into the further development of Ocean Park and Hong Kong Disneyland. Ocean Park is the winner of the prestigious 2012 Applause Award, the first-ever Asian attraction to be recognised as the best theme park in the world. To further enhance its facilities, Ocean Park will build an all-weather Water World at Tai Shue Wan. The Government will offer a $2.3 billion loan to Ocean Park to spur early commencement of the project. We shall submit a funding proposal to the Finance Committee in the next few months. In the coming few years, Hong Kong Disneyland will launch a new night-time parade and put in place a themed area featuring “Marvel heroes”, the first of its kind in the world. These new projects will be funded by the Disneyland’s operating surplus. Meanwhile, the two theme parks are actively pursuing new hotel projects to provide better complementary services for tourists.

38. The terminal building and the first berth of the Kai Tak Cruise Terminal will be commissioned in the middle of this year. Preparations are in full swing for the Terminal to receive its first liner, Mariner of the Seas with a capacity of 3 840 passengers, on 12 June. Meanwhile, we are actively working with the Hong Kong Tourism Board to promote cruise tourism, and collaborate with the travel trade and neighbouring ports on itinerary development and regional co-operation. We aim to exploit the potential of cruise tourism in Asia Pacific and attract more high-spending cruise trip visitors to Hong Kong, so as to reinforce our position as a regional cruise hub.

39. Increasing the supply of hotels will help enhance receiving capacity and service quality. Currently, there are over 210 hotels in Hong Kong, providing more than 67 000 rooms. The Government has been working to make available more hotel rooms through various measures, including providing "hotel only" sites. As at end-2012, 13 applications for redevelopment or wholesale conversion of industrial buildings into hotels were approved by the Lands Department. It is estimated that some 10 000 new hotel rooms will be provided this year and next year.

40. Following my proposal to extend the operation of the Mega Events Fund last year, we sponsored several major international events, including the Hong Kong Dragon Boat Carnival and the Hong Kong Open Championship (golf tournament). We shall continue to sponsor more international mega events to be held in Hong Kong through the Fund, and use the existing mechanism to subsidise mega events hosted by local non-profit-making organisations. In recent years, our neighbouring cities have organised mega events, such as the Formula 1 Races and overseas NBA games. We shall take the initiative to seek to host more mega events.

41. In the coming few years, large-scale tourist facilities will come on stream, and there will be major events funded by the Mega Events Fund or hosted in other forms. I believe that the tourism industry will continue to flourish and spur growth in other service sectors, including food and beverage, retail and transport, creating many employment opportunities.

Developing Financial Services Industry

42. Hong Kong is an international financial centre, and the financial services industry underpins our economy. The industry employs 230 000 people, or six per cent of the total workforce. It is a high value-added industry that contributes 16 per cent to GDP. It is also a major client of professional services and drives growth in other consumer industries. Maintaining the competitive edge of our financial services industry is crucial to economic development. The focus of developing the industry is the diversification of its business and products.

Fund and Asset Management Business

43. The total value of fund assets under management in Hong Kong is more than $9 trillion, ranking second in Asia. As the global economic balance shifts more towards the East, Asia is experiencing some of the fastest wealth growth in the world. We shall seize this opportunity to further develop our fund and asset management business.

44. To strengthen its position as a premier international asset management centre, Hong Kong will provide relevant legal and regulatory frameworks, and a clear and competitive tax environment with a view to attracting more funds of various types to base in Hong Kong to broaden the variety and scope of our fund business. Hong Kong-domiciled funds will drive demand for professional services such as fund management and investment advice as well as legal and accounting services.

45. To attract more private equity funds to domicile in Hong Kong, we propose to extend the profits tax exemption for offshore funds to include transactions in private companies which are incorporated or registered outside Hong Kong and do not hold any Hong Kong properties nor carry out any business in Hong Kong. This will allow private equity funds to enjoy the same tax exemption as offshore funds. We shall conduct consultation on the amendments to relevant tax legislation and detailed proposals.

46. At present, investment funds established in Hong Kong can only take the form of trusts. As an international financial centre, Hong Kong should provide a more flexible business environment for the industry to meet market demand. To attract more traditional mutual funds and hedge funds to domicile in Hong Kong, we are considering legislative amendments to introduce the Open-ended Investment Company, an increasingly popular form used in the fund industry. We are discussing the relevant legal and regulatory frameworks with regulators. The public will be consulted once a proposal is drawn up.

47. To expand the distribution network of Hong Kong's fund industry, the Securities and Futures Commission is studying with the Mainland authorities an arrangement for mutual recognition of funds. The arrangement will attract more funds to establish in Hong Kong and foster the development of those professional sectors engaged in the registration, investment management and sales of funds.

48. In addition, the Government has introduced two bills into this Council, with a view to enhancing Hong Kong's competitiveness in the development of Islamic finance and facilitating the development of trusts services industry in Hong Kong.

49. As the Mainland experiences rapid growth in wealth and a steady opening of its capital account, the Qualified Domestic Institutional Investor (QDII) Scheme, which allows investment of Mainland capital in offshore financial markets, is expected to be further relaxed. This will help the growth of the private wealth management business in Hong Kong. The number of private banks in Hong Kong has increased from 27 at end-2007 to 41 now. To tie in with the development of private wealth management, the Government and the regulators will continue to support the work of the sector in setting up a trade association, taking forward programmes relating to the accreditation and enhancing the training of practitioners.

Insurance Business

50. The Government is seeking to introduce a bill into this Council within this year to establish an independent Insurance Authority to align the insurance regulatory regime in the local insurance industry with international practices. This will facilitate the development of the industry and protect the interests of policyholders.

51. Many large enterprises in Asia are keen to run their own captive insurance companies to insure against their business risks. To attract more enterprises to form captive insurance companies in Hong Kong, I propose to reduce the profits tax on the offshore insurance business of captive insurance companies, such that they will enjoy the same tax concessions as those currently applicable to reinsurance companies. Attracting a cluster of large-scale captive insurers in Hong Kong will promote the development of other related businesses, including reinsurance, making Hong Kong’s risk management services more diversified.

Offshore Renminbi Business Centre

52. Hong Kong is now the world's largest and most efficient offshore RMB business hub, with the world's largest offshore pool of RMB. Total RMB deposits and outstanding RMB certificates of deposits stood at RMB 720 billion at end-2012.

53. Hong Kong also serves as a platform for enterprises and financial institutions all over the world to carry out various financial activities such as RMB payments, financing and investments. RMB trade settlement conducted through Hong Kong banks in 2012 exceeded RMB 2,600 billion, a year-on-year increase of 37 per cent and representing over 90 per cent of the Mainland's cross-border trade settled in RMB. The RMB bond market also showed continuous growth. At end-2012, outstanding RMB bonds issued in Hong Kong exceeded RMB 230 billion, an increase of 62 per cent over end-2011.

54. Since the launch of the RMB Qualified Foreign Institutional Investors (RQFII) Scheme at end-2011, the range of offshore RMB investment products has been broadened. Among them, Exchange Traded Funds tracking the A-share indices have been well received by the market. We shall continue our dialogue with the relevant Mainland authorities to expedite the next stage of RQFII's expansion, which will include extending the pilot scheme to qualified Hong Kong financial institutions. These measures will promote the circulation of RMB funds and diversify the development of RMB investment products. We shall continue to strengthen our market infrastructure, and stay connected with other financial centres in the world with a view to further enhancing the use of RMB for trade settlement, financing and investment at the international level, consolidating Hong Kong's position as an offshore RMB business centre.

Basel III

55. The Basel Committee on Banking Supervision announced in early January the details of the revised regulatory liquidity standards of Basel III to be implemented progressively between 2015 and 2019. The Hong Kong Monetary Authority (HKMA) is assessing the impact of the revision on the local banking sector to draw up a corresponding implementation plan for industry consultation. We shall devise regulatory rules that suit our financial markets and business environment to promote the stability of our banking system.

Government Bond Programme

56. Since the launch of the Government Bond Programme in 2009, the systematic offering of bonds has attracted local and overseas investors to the Hong Kong bond market and expanded the investment base. As at early February this year, outstanding bonds issued under the Programme totalled about $70 billion.

57. Given the situation of global financial markets, there has been a sustained growth in the demand from investors and financial institutions in Asia and other emerging markets for high quality public debt papers, including Hong Kong Dollar government debt. I hope that the Government Bond Programme can be expanded to meet the criteria of certain global benchmark bond indices to attract more investors. To further promote the sustainable development of our bond market, I propose to expand the size of the Government Bond Programme from the current $100 billion to $200 billion to provide adequate room for the Programme to continue in the next five years. We shall move in due course an amendment resolution in this Council to raise the maximum amount of borrowings under the Government Bond Programme.

58. The Government also issued two sets of inflation-linked retail bonds (iBond) under the Government Bond Programme. Both the total amount of applications and the total application amounts for the iBond issued last year set a new record for local retail bonds, reflecting the investing public's greater awareness of, and interest in, retail bonds. To maintain this growth momentum, I propose launching a further iBond issue of up to $10 billion under the Government Bond Programme. The iBond, with a maturity of three years, will target Hong Kong residents. Interest will be paid to bond holders once every six months at a rate linked to the inflation rates of the last half-year period. The HKMA will announce the details in due course. I have to point out that the further issuance of iBond is a measure to address the current low-interest rate environment. It is a non-recurrent measure. In the long run, the Government will not confine bond issuance to a particular type of bonds. We shall develop different types of bonds for a more diversified bond market in Hong Kong.

Stored Value Facilities and Retail Payment Systems

59. Over the past ten years, the number of local internet banking accounts has increased at an average annual rate of 22 per cent to over eight million at present, with an average transaction volume of around $4 trillion per month. Shopping and bill paying on innovative online and electronic payment platforms are becoming increasingly popular. The development of electronic payment instruments and retail payment systems can make payment processing more efficient for companies, especially those in the retail industry. Such development will encourage local enterprises to extend their global sales networks, and stimulate the growth of other ancillary trades, including electronic transaction services and computer system developments. We are considering possible amendments to the legislation to introduce a licensing regime for stored value electronic money and to empower the HKMA to supervise the relevant retail payment systems, which will help establish a sound regulatory regime for Hong Kong.

60. Given the rapid developments in the global financial markets, the Government needs to tap advice from market experts. The Chief Executive has announced the establishment of the Financial Services Development Council, a high-level, cross-sector advisory body, to offer views and suggestions to the Government on developing and promoting our financial services industry as well as reinforcing our position as an international financial centre.

Expanding Business and Professional Services

61. With some 470 000 employees and accounting for 12 per cent of GDP, business support and professional services are another pillar industry of the Hong Kong economy. They comprise a wide range of professional and supporting services for business activities, such as legal, accounting, architecture, engineering, planning, surveying, human resources, management consultancy, technical testing, product development and distribution, market research, conference and exhibition, and information technology.

62. Apart from serving local enterprises, Hong Kong’s business and professional services are also exported to the Mainland and other areas in Asia. We shall continue to assist these service industries through relevant G2G platforms. Under the National 12th Five-Year Plan, the Mainland will devote greater efforts to developing modern service industries to lift the share of the service industries in the economy by four percentage points by 2015. Such scale of expansion far exceeds Hong Kong’s GDP in one year. This will present vast business opportunities to the sectors concerned in Hong Kong. For continuous enhancement of the CEPA mechanism, the Chief Executive has announced that the HKSAR Government and the Ministry of Commerce will set up a joint working group to assist the sectors concerned to solve problems they encounter in gaining access to the Mainland market under CEPA.

Nurturing Emerging Industries

63. Apart from building on our traditional strengths, we also give strong support for the development of emerging industries to further diversify our economy, so that Hong Kong can better respond to the world's ever-changing economic environment. Over the past couple of years, the Government has promoted six industries where Hong Kong enjoys clear advantages. These industries employ 420 000 people, or 12 per cent of the total workforce, and contribute to 8.5 per cent of GDP. The Government will keep an eye on the development of new industries and proactively provide appropriate support for emerging industries with the potential to flourish.

64. On nurturing emerging industries, the efforts of the Government and the industries concerned have borne fruit. Among the emerging industries, the cultural and creative industries, employing 190 000 persons, have been taking up an increasing share of GDP, which now approaches five per cent. To the credit of these practitioners, they have won numerous international awards and accolades. Apart from the film industry, other industries in the sector also made impressive achievements. Despite the global economic slowdown over the past few years, our design and architecture sectors have, during the five years leading up to 2011, achieved an average annual growth rate of 20 per cent in terms of value added and five per cent in terms of the number of practitioners. Another notable achievement is that local advertising companies scooped a total of 60 awards in three different international advertising competitions. In 2011, local enterprises spent more than $35 billion on advertising, an increase of 16 per cent over the previous year. The local advertising industry continues to boom, employing 18 000 people and bringing $6.8 billion worth of economic benefits. With the huge domestic demand in the Mainland as a result of sustained economic growth, our cultural and creative industries have great development potential. We shall continue to provide strong support for the industries with a view to opening up more business opportunities and markets.

65. In recent years, Hong Kong has played host to a number of art fairs which have attracted many well-established art galleries from different corners of the world. We shall host a number of world-class art fairs again this year, including Art Basel - Hong Kong, inaugural show in Asia. These major events will help pool overseas and local art-related participants and foster interaction and exchanges among them. Successful art fairs will also facilitate art and cultural development in Hong Kong, and highlight our potential as an international art metropolis.

66. To foster the development of visual arts and nurture local talent in the field, we are converting the club house of the former Royal Hong Kong Yacht Club in Oil Street, North Point into a visual arts exhibition and activity centre. I also propose additional funding of $50 million for the Leisure and Cultural Services Department to acquire local visual artists' outstanding artworks, and to commission works for exhibition under public art schemes. These are set to promote the profile of local artists and bring their works to the attention of the art market.

67. Today, many internationally renowned scholars work in local universities to conduct research. Their efforts contribute to the development of Hong Kong's research and development (R&D) capabilities. Top researchers working in our universities and enterprises have won numerous awards. Last year, 56 Hong Kong scientists were approved by the State Ministry of Science and Technology for inclusion in the National Science and Technology Programmes Expert Database. They are now qualified to participate in the compilation of the application guide and in project assessment for national science and technology programmes. Internationally, the "Interactive Intention-Driven Upper-Limb Training Robotic System", a project under the Innovation and Technology Fund (ITF), was awarded the "Grand Prix Du Salon International Des Inventions De Genève" in the 40th International Exhibition of Inventions of Geneva in 2012, making it the first invention from Hong Kong to receive the grand prize.

68. In my view, if we can transform technology research outcomes into products with market potential, coupled with industrial production, our technological development can make an even greater contribution to Hong Kong's economy. To facilitate technology transfers and the realisation of R&D results, six local universities have set up their own technology transfer offices to deal with the complicated process of commercialising R&D results. I propose that these six universities be each provided with a subvention of up to $12 million through the ITF for a period of three years from 2013-14 onwards to support the work of their technology transfer offices.

69. Technology and product R&D will stimulate the development of intellectual property trading. Hong Kong has a sound regime for the protection of intellectual property rights, and is well-equipped to develop into a regional intellectual property trading hub. The Secretary for Commerce and Economic Development will lead a working group to study the overall strategy for promoting Hong Kong as a hub for intellectual property trading.

Supporting Small and Medium Enterprises

70. SMEs are an important pillar of Hong Kong's economy and employment market. They form the majority of enterprises in Hong Kong and employ over 1.2 million people or half the private-sector workforce. In the face of persistently weak export markets and a challenging external environment, we shall assist SMEs in six areas to help them raise capital and tap new markets:

(a) I propose to extend the application period for the special concessionary measures under the SME Financing Guarantee Scheme for one year to the end of February 2014. Last year, the Government provided a total guarantee commitment of $100 billion for the Hong Kong Mortgage Corporation Limited to introduce special time-limited concessionary measures to offer guarantees with a higher guarantee ratio of 80 per cent at a concessionary fee rate. Introduced in May 2012, the measures have been well received by the trade. Up to end-January, over 5 400 applications have been approved, benefiting more than 4 000 enterprises with total loan guarantee of more than $24 billion.

(b) We shall continue to make use of the $1 billion BUD Fund set up last June to assist Hong Kong enterprises to enhance their competitiveness in the Mainland through upgrading and restructuring, developing brands and promoting domestic sales in the Mainland. The Fund has since received more than 500 applications.

(c) The HKTDC will set up more Design Galleries in Mainland cities other than Beijing and Guangzhou to offer platforms for Hong Kong enterprises, especially SMEs, to showcase their products. This will help Hong Kong enterprises gain access to the Mainland market and build up greater awareness of Hong Kong brands there.

(d) I propose to increase the cumulative amount of the grant for SMEs under the SME Export Marketing Fund from $150,000 to $200,000, subject to the meeting of relevant additional conditions. The Fund subsidises SMEs' export promotion activities, including trade fairs, exhibitions, business missions and advertising.

(e) On 1 March, the Hong Kong Export Credit Insurance Corporation (ECIC) will introduce a "Small Business Policy" (SBP) scheme for Hong Kong enterprises with an annual business turnover of less than $50 million, providing exporters with more flexibility in taking out insurance cover. Within a period of two years from 1 March 2013, SBP policyholders will enjoy waiver of the annual policy fee and up to 20 per cent premium discount.

(f) On 1 March this year, the ECIC will upgrade the ratings of Turkey and the Philippines following the rating upgrades countries including Russia, Indonesia and Peru last year. The ECIC will raise the insurance limits of these countries accordingly, and provide higher credit limits and lower premium rates for exporters to these countries.

71. I hope that these six support measures for SMEs will help keep their business running, create more employment and enhance our people's job security.

Investing in Education and Optimising Human Capital

72. The importance of education is beyond question. Investing in education enhances the knowledge of both individuals and the community at large. Through skills training, people can acquire the tools for self-reliance to improve their livelihood and realise their goals. For the community as a whole, a diverse pool of talent can promote social mobility and sharpen competitiveness, providing a long-term economic driver. I shall now put forward measures to invest in education and optimise Hong Kong's overall manpower structure.

Developing Human Capital

73. Estimated recurrent expenditure on education for 2013-14 is $63 billion, which is more than one-fifth of recurrent government expenditure. It is the biggest expenditure area amongst different policy area groups.

74. A quality teaching force is the key to the quality of education. I propose to inject an additional $480 million into the HKSAR Government Scholarship Fund (GSF) to set up scholarships for outstanding local students to take degree courses or teacher training programmes in prestigious overseas universities. I expect that about 20 scholarships will be awarded each year. Students who receive the awards must undertake to teach in Hong Kong upon graduation for at least two years or a period equivalent to the duration of receiving the scholarships.

75. Hong Kong is an international city. Our people should possess good language proficiency. The Language Fund set up in 1994 provides financial support for projects and activities aimed at promoting bi-literacy and tri-lingualism among our people, including programmes to support non-Chinese speaking students in learning Chinese. I propose to inject $5 billion into the Language Fund to facilitate its longer term planning.

76. In the 2011-12 academic year, nearly 500 students with special education needs (SEN) enrolled in local full-time accredited sub-degree and degree programmes. As compared with their peers, students with SEN encounter more difficulties in learning and have to apply themselves more diligently. I propose to make two separate injections of $20 million each, bringing the total to $40 million, into the GSF and Self-financing Post-secondary Education Fund to establish scholarships to give recognition to deserving tertiary students with SEN in the pursuit of academic and other excellence. I expect that about 100 students will be awarded scholarships every year. I also propose to allocate $12 million to the Vocational Training Council each year to purchase equipment and learning aids for students with SEN, providing them with psychological and student counselling services, and enhancing the support for teaching and learning.

Promoting Career Progression

77. Vocational and academic qualifications are equally important for personal development. The Government launched the Qualifications Framework (QF) in 2008, embracing qualifications in the academic, vocational and continuing education sectors and establishing flexible learning pathways with multiple entry and exit points. Industry Training Advisory Committees (ITACs) are set up under the QF to develop the Specifications of Competency Standards (SCSs), and to promote and implement the QF within the industry. The QF also provides a platform to facilitate the development of diverse pathways for career progression, and practitioners can receive recognition at various levels based on their prior practice and experience.

78. To further enhance the knowledge and skills of workers in the industries, and their competitiveness in the labour market, I propose to allocate $10 million per year to support ITACs to launch new initiatives. These include:

(a) introducing award schemes for outstanding practitioners to engage in learning activities in different places around the world;

(b) designing SCS-based training programmes and package that meet the needs of the industries; and

(c) stepping up promotion and publicity of the QF for its wider acceptance among all sectors.

So far, 19 industries have set up their ITACs, covering 46 per cent of the local workforce.

Enhancing Vocational Training

79. The sustained development of all sectors hinges on quality workers. Some sectors, including the construction, retail and catering industries, have experienced labour shortage in recent years. Members of these sectors have urged the Government to follow other countries' example and allow large-scale labour importation. In my opinion, the shortage problem facing some sectors is caused by the surge in labour demand arising from their rapid development, coupled with the fact that a labour mismatch does exist in the labour market.

80. Hong Kong's economic growth has been driven by economic upgrading and restructuring for many decades. We have a flexible labour market where the quality of labour keeps improving to meet the needs of a changing economic structure. We should first consider how to provide more suitable training programmes and complementary measures to channel more workers to these sectors. This is to make good use of local labour to enhance the productivity of the whole community. No doubt, local workers should be given priority for quality employment opportunities in all sectors. However, I understand that there may be transitional labour shortages for some jobs in certain sectors, or even longer-term shortages in a number of obnoxious trades. The Government will follow its existing policy and mechanisms in dealing with labour importation.

81. A long-term labour shortage will hinder the development of industries, affect the employment market and even dampen our economic vibrancy. We must find the right match between the industries and the workforce. Trade associations and stakeholders of some industries have been forthcoming with proposals to improve training and labour supply for their respective industries. A feasible option for attracting new blood into the industries is to develop structured training programmes that link up enrolment of trainees, vocational training, job attachment and job matching. Such training programmes should be coupled with appropriate subsidies as incentives, and effective publicity. These will allow more young people and their families to have a better understanding of the industries concerned.

82. Take the construction industry as an example. The efforts on training made by the industry in recent years have begun to produce results. The industry's co-ordinating body, the Construction Industry Council (CIC) has all along been striving to enhance training for the construction workforce. I allocated a total of $320 million in 2010 and 2012 to support the CIC's labour training, which includes granting subsidies to contractors to employ trainees on a "first-hire-then-train" basis to enable them to gain actual work experience on construction sites. Training allowances are provided for those trades facing labour shortages to attract new entrants. More than 2 000 training places have been provided by the CIC so far, and about 60 per cent of the trainees are aged below 35. We shall also step up our promotion efforts to attract ethnic minorities to join the industry.

83. Thanks to the systematic labour training provided by the CIC and the rollout of major infrastructure projects in the past decade, the employment situation of the construction industry has improved notably. The unemployment rate dropped substantially from the post-financial tsunami 12.8 per cent to the latest 5.1 per cent, and the average median monthly income has increased steadily to $13,000. Some of the trades have even seen an appreciable increase in the income of their workers. I encourage other industries in keen demand for labour to follow the example of the construction industry in launching systematic training plans and initiatives to bring in more new recruits.

84. As elaborated by the Chief Executive in his Policy Address, further enhancing Hong Kong's status as an international shipping centre is one of the Government's priorities. The shipping industry offers plenty of quality job opportunities with promising prospects. The shipping companies registered in Hong Kong own and manage a total of about 2 000 merchant ships, which make up ten per cent of the world's merchant fleet. There are about 700 shipping-related companies in Hong Kong, offering a wide range of services such as shipping management, agency, finance, legal services and arbitration, and a large number of jobs. At present, the Hong Kong International Airport offers more than 60 000 jobs.

85. To support training for the local shipping and aviation industry, I propose to designate $100 million to establish a training fund for maritime and aviation transport, so as to sustain and expand various schemes and scholarships, and to implement other new initiatives. This will help attract young people to enrol in related skills training and degree programmes and join the industry upon graduation, providing a wealth of vibrant and competitive talent for the industry.

86. The retail industry accounts for about four per cent of GDP and employs over 300 000 people. While the robust development of tourism should mean more business opportunities, the retail industry suffers from an increasing shortage of labour, with the current vacancy rate standing at over three per cent. Difficulties in retaining and recruiting quality people have an imminent impact on the service quality of the industry, and may adversely affect economic development. To facilitate its healthy growth in the long term, I shall set up a task force on labour development in the retail industry. Led by the Commerce and Economic Development Bureau, the task force will pool the efforts of the Government, the industry and relevant organisations. It will study the economic outlook of the industry and its labour demand and supply. The task force will complete its work within this year and put forward appropriate and concrete recommendations.

Funding the Employees Retraining Board

87. Over the years, the Employees Retraining Board (ERB) has strived to improve the employability of local workers. Through a variety of courses under the Manpower Development Scheme, the ERB offers placement-tied courses for the unemployed and job seekers, and courses which assist employees to enhance their skills, making it easier for them to move up the job ladder in various trades. In 2013-14, the ERB will offer 130 000 training places. Resources have also been reserved to provide an additional 40 000 places to meet the demand from training providers for increasing or redeploying places.

88. Levy on employers of foreign domestic helpers is the major financial source of the ERB. In his Policy Address, the Chief Executive announced the abolition of the levy. We have to provide sustained and stable financial support for the ERB so that it can continue to enhance the productivity of local workers. I propose to inject $15 billion into the ERB to provide it with long-term support.

Investing in Infrastructure

89. To foster economic development and enhance the quality of life of our people, we shall continue to plan and take forward infrastructure projects. The estimated capital works expenditure for 2013-14 exceeds $70 billion. By late March 2013, our total commitments for capital projects are expected to be over $310 billion.

90. As for traffic infrastructure, the construction of five new railway lines is now under way. Our railway network will extend to Sai Ying Pun and Kennedy Town in 2014, and further to Wong Chuk Hang and Ap Lei Chau, as well as Ho Man Tin and Whampoa in 2015. The construction of the Shatin to Central Link, a railway that traverses the territory, has commenced and will be completed in phases in 2018 and 2020. Upon completion, our railway network will cover an area within which over 70 per cent of Hong Kong's population lives.

91. Major road projects include the Central-Wan Chai Bypass and Island Eastern Corridor Link. Upon completion in 2017, the existing traffic congestion from Central to Wan Chai and the adjoining areas will be alleviated. We shall seek funding approval for the detailed design of a second tunnel linking Tseung Kwan O and urban Kowloon. We also plan to commence construction of the Tuen Mun-Chek Lap Kok Link within this year. The Southern Connection will be commissioned first to tie in with the opening of the Hong Kong-Zhuhai-Macao Bridge in 2016, followed by the Northern Connection.

92. As for healthcare, the construction of the North Lantau Hospital was completed in late 2012 and the hospital will come into operation in phases this year. The expansion of Tseung Kwan O Hospital and the phase two redevelopment of Caritas Medical Centre will also be completed in 2013 and 2014 respectively. We are preparing for the redevelopment of Queen Mary Hospital, Kwong Wah Hospital and United Christian Hospital. The estimated costs will be as high as $25 billion. In addition, we plan to use $20 billion for the construction and refurbishment of several public hospitals and clinics, including the construction of Tin Shui Wai Hospital and the Centre of Excellence in Paediatrics, the refurbishment of Hong Kong Buddhist Hospital as well as the reprovisioning of the Yau Ma Tei Specialist Clinic.

93. The Government will continue to provide various sports facilities for the public. The new indoor heated pool complex at Victoria Park is expected to come into operation in the third quarter of this year. We shall seek funding approval for the construction of an indoor stadium with a heated pool in Tsing Yi. Upon completion of the project, there will be 25 heated pools for public use in Hong Kong.

94. Construction works of the velodrome in Tseung Kwan O will be completed in the second half of this year. We are also taking forward in phases the development of a cycle track network connecting the East and West New Territories. The construction of the Ma On Shan-Sheung Shui section is expected to complete by end-2013. We plan to seek funding approval this year to construct part of the Sheung Shui-Yuen Long section.

95. We shall continue to invest in environmental infrastructure to improve our environment. On water quality, we have completed the Harbour Area Treatment Scheme Stage 1, and there has been significant improvement in the overall water quality of Victoria Harbour. Stage 2A of the Scheme, a $17.6 billion project, is scheduled for completion in 2014. To further reduce waste at source, we are pressing ahead with the first phase development of the organic waste treatment facilities in Siu Ho Wan, Lantau. Scheduled for commissioning in 2016, the facilities will convert food waste into energy and compost products. We have also earmarked $500 million to set up waste electrical and electronic equipment processing facilities as well as five community green stations to encourage public participation in waste reduction and recycling.

96. Fresh water resources in the Mainland are limited, and the demand for Dongjiang water in Guangdong Province is on the rise. In face of scarce resources, we must encourage our people through public education to save water, and explore new water sources so as to ensure sustainable supply for Hong Kong amid climate change and population growth.

97. Last year, we started a detailed planning and investigation study, including an assessment of the feasibility and cost-effectiveness, for the construction of a desalination plant on a reserved site in Tseung Kwan O, with a view to tapping sea water as a water source. Although the anticipated output capacity of the desalination plant will only account for five to ten per cent of Hong Kong's total water consumption, we hope that as technology advances and costs go down in the future, seawater desalination can serve as another water supply source and help reduce our reliance on other water sources in the long term.

98. With the major infrastructure projects entering their construction peaks, it is estimated that capital works expenditure will increase to over $70 billion for each of the next few years, far exceeding the average annual expenditure of about $40 billion in the past five years. These large infrastructure projects create a large number of jobs which are particularly crucial in times of uncertain economic outlook.

Stabilising Land Supply

99. The Chief Executive detailed in his Policy Address specific measures to increase land and housing supply. I shall continue with my co-ordination work to expand the land reserve as in the past two years. I shall also allocate additional resources to the relevant departments to increase their manpower in order to speed up land supply. I shall allocate $4.5 billion in the coming five years to carry out studies and design work and progressively roll out the land development projects relating to reclamation outside Victoria Harbour on an appropriate scale, opening up of new development areas and the development of caverns.

Increasing Residential Land

100. Regarding land supply for private housing, the Government's aim is to maintain on average the provision of land for building about 20 000 residential units each year. The Government will continue to increase land supply in the coming year. In the 2013-14 Land Sale Programme, we shall include 46 residential sites, which is capable of providing about 13 600 units in total. Amongst these sites, 28 are new sites. We shall continue the practice of announcing government-initiated land sale arrangements in advance on a quarterly basis, and exercise flexibility in supplying housing land in the light of market demand. In the coming year, all the major sources of land supply for private housing together, which include the Government's Land Sale Programme, railway property development projects, projects of the Urban Renewal Authority, and lease modifications/land exchanges or other private developments, will provide land capable of building some 25 800 private residential flats. The Secretary for Development will announce the Land Sale Programme for the coming year tomorrow.

101. On public housing, we have provided the Housing Authority with adequate land to build 79 000 public rental housing flats within five years from 2012-13, and about 17 000 Home Ownership Scheme flats within four years from 2016-17.

Supply of Private Residential Flats in Short Term

102. I announced two demand-side management measures last Friday in a bid to cool down the overheated property market. I will not repeat the details of the measures today. Increasing supply is the key to solving the housing problem. In the next three to four years, it is estimated that a total of 67 000 first-hand units would come onto the private residential property market, the highest since September 2007. These include 4 000 unsold units in completed projects, 48 000 unsold units under construction, and 15 000 units to be constructed on disposed sites.

103. As for the supply of private residential flats in 2013, I estimate that 24 000 first-hand units can be offered for sale this year, including 12 000 uncompleted units, for which we are speeding up the processing of their pre-sale consent applications, 8 000 uncompleted units ready for pre-sale and 4 000 unsold units in completed projects.

104. Developers usually adjust the pace of sales according to market appetite, and may not put all the 24 000 flats on the market this year. However, we are sure that the supply of first-hand units has seen a rebound. As the external economic environment remains volatile, I would like to remind people once again that interest rates are susceptible to various external factors and will resume an upturn cycle in the future. Before making a home purchase decision, people should assess their ability to afford the property, particularly whether family income can support mortgage payments if mortgage rates are to revert to a normal level.

Increasing Commercial Land

105. Apart from housing land, the Government is also committed to increasing the supply of commercial land to provide room for further development of different economic activities in Hong Kong. Rentals of Grade A offices started to drop last year. This had much to do with the external slowdown and uncertain outlook. The 2013-14 Land Sale Programme will include nine sites for commercial/business use and one "hotel only" site, providing a total floor area of about 330 000 square metres and some 300 hotel rooms respectively.

106. We shall expedite the development of the Kowloon East core business district. Upon completion, it will be able to provide an office floor area of four million square metres. In addition, we are considering speeding up the release of two clusters of government sites for commercial development in Kowloon East, including assessing the feasibility of relocating the government facilities there. The two clusters of sites will provide a floor area of 500 000 square metres. We shall also discuss with the AA ways to accelerate the development of the North Commercial District on Chek Lap Kok Airport Island.

107. There is a huge demand for office space in the Central Business District (CBD) in Central. We shall continue to relocate government departments from the CBD to release more office space to the market. The relocation of the Independent Commission Against Corruption to North Point has freed a prime site at Murray Road. Upon completion of the zoning procedures, the site can provide some 40 000 square metres of Grade A office space. The completion of the new Trade and Industry Tower at the Kai Tak Development Area by end-2014 will release more than 18 000 square metres of floor area in the Trade and Industry Department Tower in Mong Kok for commercial use.

108. The Department of Justice plans to relocate to the old Central Government Offices in 2015, vacating its offices in Queensway Government Offices for use by other government departments currently occupying commercial office premises in Central and Admiralty. This will release office space in the districts to the market. By then, the floor area of our leased office space in Central and Admiralty will reduce from the present level of over 2 700 square metres to less than 230 square metres.

109. We are now proceeding with the relocation of departments in the three government office buildings at the Wan Chai waterfront. This is a large-scale project, involving 29 departments and more than 10 000 staff. Upon the relocation in phases of government departments to the new government office buildings in West Kowloon, Kai Tak and Tseung Kwan O, we shall rent out the floor space released to increase the supply of Grade A offices in Wan Chai. We shall put up the three government office buildings in Wan Chai for sale in due course, which is expected to provide a floor area of 175 000 square metres.

Caring for People's Livelihood

110. Social welfare, education and medical services are the major spenders of public resources. In 2013-14, estimated recurrent expenditure in these three areas will approach $170 billion, or 60 per cent of recurrent government expenditure. This is an increase of $55.1 billion, or 50 per cent, compared with 2007-08. I have already covered the Government's plans to invest in education and optimise human capital. I shall now focus on the major initiatives in social welfare, healthcare services and environmental protection.

Enhancing Social Welfare

111. We have been investing heavily in regular welfare programmes and services, covering major areas such as the provision of social security assistance, support for the elderly, persons with disabilities, families, children and young people, and the promotion of women's interests. In 2013-14, our recurrent expenditure on social welfare is estimated to reach $56 billion, an increase of 31 per cent over that for last year.

Elderly Services

112. The elderly are the major beneficiaries of social security payments. To enhance the quality of life for elderly people aged 65 or above who are in need of financial support, we shall start making payments for the Old Age Living Allowance this April. The new allowance, involving an additional allocation of about $8.3 billion [Note 1] in 2013-14, is expected to benefit more than 400 000 elderly people.

[Note 1] The additional allocation covers the allowance payments from December last year to March this year.

113. On elderly care services, the five new or improved measures coming on stream in 2013-14 include:

(a) allocating $380 million from the Lotteries Fund to launch the first phase of the Pilot Scheme on Community Care Service Voucher for the Elderly this September. By adopting the "money follows the user" approach in the provision of assistance, eligible elderly people under the Pilot Scheme can choose the community care services that suit their individual needs;

(b) allocating additional recurrent funding of $9 million to add 100 day care places and extend the service hours of new day care centres and units for the elderly;

(c) increasing recurrent funding by $73 million for the additional provision of some 600 subsidised residential care places for the elderly through the construction of three contract residential care homes for the elderly (RCHEs), purchase of additional EA1 places under the Enhanced Bought Places Scheme and making better use of space in subvented homes. Together with those subsidised residential care places with funding earmarked earlier, 2 300 additional subsidised residential care places will be provided from 2012-13 to 2015-16;

(d) allocating additional recurrent funding of $164 million to increase the subvention for 7 000 residential care places with continuum of care by ten per cent, so that RCHEs can provide more targeted services for the elderly, and to upgrade 7 850 ordinary residential care places in subvented RCHEs to places with continuum of care; and

(e) allocating $160 million in the five-year period from 2013-14 for the Social Welfare Department to organise ten more classes of two-year full-time Enrolled Nurse Training Programmes for the welfare sector to cope with the expansion of residential care services. The Programmes will provide more than 1 200 training places to augment the enrolled nurses supply to meet manpower demand in the welfare sector.

Rehabilitation Services for Persons with Disabilities

114. Recurrent expenditure on rehabilitation services for persons with disabilities in the coming year will reach $4.4 billion. New services will be introduced in 2013-14 in the following five areas:

(a) allocating additional recurrent funding of $35.6 million to strengthen the care and training for persons with disabilities by providing 145 new places each for residential and day training services;

(b) allocating additional recurrent funding of $67.9 million to increase the manpower of residential care homes and day training centres for persons with disabilities to meet the needs of ageing service users;

(c) allocating additional recurrent funding of $203 million to regularise the home care service for persons with severe disabilities and extend the home-based care services to all districts to cover persons with severe disabilities who are living in the community, regardless of whether they are on the waiting lists for places in subsidised residential care homes;

(d) allocating additional recurrent funding of $4.8 million to enhance vocational rehabilitation services and employment support by increasing the job attachment allowance and wage subsidy under the "On the Job Training Programme for People with Disabilities" and the "Sunnyway - On the Job Training Programme for Young People with Disabilities"; and

(e) allocating an additional funding of $5.9 million to acquire six additional buses, thereby increasing the fleet size of Rehabus to 135, to better meet the special transport needs of persons with disabilities.

Supporting Poverty Alleviation

115. The Community Care Fund was established by the Government in early 2011. With the Government's $5 billion injection into the Fund and donations from the business sector, the Fund has launched a total of 18 programmes to offer appropriate time-limited assistance to over 100 000 people in need, including those not covered by the Government's safety net.

116. I propose to inject an additional $15 billion into the Fund. This, together with the original $5 billion government injection, is expected to generate an annual investment return of over $1 billion. I believe that the Commission on Poverty (CoP) will make effective use of this injection to renew its efforts to alleviate poverty by plugging the gaps in the existing system, and continue to implement and enhance those programmes that have proved to be effective but have yet to be incorporated into the Government's regular assistance and service programmes. It will also introduce new assistance programmes or pioneer projects.

Enhancing Mandatory Provident Fund System

117. The Mandatory Provident Fund (MPF), which has been in place for 12 years, is one of the three pillars of the existing retirement protection system. We we are now working with the Mandatory Provident Fund Schemes Authority (MPFA) on short, medium and long-term fee reduction measures. They include promoting electronic platforms, consolidating employees' accounts, and rationalising the types and numbers of MPF funds in order to reduce the administration costs. Meanwhile, we aim to cut down the fees and charges by maximising market forces. The MPFA is preparing proposals regarding the implementation of a cap on MPF fees that will be introduced in case of market failure. We intend to consult the public within this year.

118. In the past few months, there have been considerable discussions on retirement protection. The Social Security and Retirement Protection Task Force under the CoP will study this complicated issue in depth. I hope that the community will explore the issue in a rational, pragmatic and prudent manner and with due regard to the sustainability of public finances and the possible financial pressure on our future generations.

Reinforcing Healthcare Services

119. The recurrent expenditure on medical and health services for 2013-14 will reach $49 billion, an increase of $2.7 billion over 2012-13. The bulk of the additional funding is for new recurrent allocation to the Hospital Authority (HA) to enhance and expand appropriate public medical services.

120. To cope with the ever-increasing demand for medical services, the HA will add 290 acute patient beds and convalescent beds, and increase the quota at general out-patient clinics for patients with episodic diseases in the coming year. The HA will also refine the waiting list management of specialist out-patient clinics to shorten the waiting time for such services. On elderly medical services, the HA will strengthen the treatment of degenerative diseases to meet the service demands of an ageing population.

121. The Government is committed to promoting mental health and has in recent years introduced various initiatives to enhance community support for mental patients with a view to facilitating their rehabilitation and reintegration into the community. To enhance community support for patients with severe mental illness, the HA launched the Case Management Programme in April 2010, which now covers 12 districts. Since its launch, the Programme has provided intensive and personalised community support for over 11 000 mental patients. The HA will roll out the Programme to three more districts in 2013-14 and achieve full coverage in the coming two years. Additional funding of $12.5 million will be allocated to the Social Welfare Department to increase the staff resources of the Integrated Community Centres for Mental Wellness to dovetail with the HA's Programme. Also, we plan to use $8 billion to redevelop Kwai Chung Hospital to strengthen care and support for mental patients.

122. In the next financial year, we shall allocate an additional $44 million to include in the HA Drug Formulary two chemotherapeutic drugs for cancer treatment and expand the application of two special drugs for patients with advanced Parkinson's disease and cancer. Following the injection of $10 billion into the Samaritan Fund by the Government last year, the financial assessment criteria for drug subsidies were relaxed last September to benefit more patients in need.

Promoting Environmental Protection and Conservation

123. Environmental protection and conservation is one of the major policy areas in the Policy Address. Improving the environment is vital to the sustainable development of Hong Kong, for which we need the shared commitment of both the community and the Government. Our next priority will be to improve roadside air quality.

124. In his Policy Address, the Chief Executive proposed setting aside $10 billion as subsidies, coupled with regulatory measures, to progressively phase out heavily polluting pre-Euro IV diesel commercial vehicles. I have already earmarked resources for this proposal on which the Environment Bureau is now consulting this Council, the relevant transport trades and other stakeholders.

125. The Chief Executive also proposed in his Policy Address to inject $5 billion into the Environment and Conservation Fund to provide support for green projects initiated by the community. I have made a provision for the Fund to further enhance public awareness of environmental protection, conduct related scientific research, and encourage public participation in environmental protection activities.

Easing Pressure and Stimulating Economic Growth

126. During the Budget consultation, political parties and members of the public made many suggestions on relief and concessionary measures. They have diverse views on whether we should continue the one-off relief measures implemented in recent years. I understand that members of the public, especially the grass roots, hope that the Government will help ease the heavy burden and pressure on them. Some, however, opined that one-off hand-outs are undesirable as resources should be expended to implement appropriate policies to provide recurrent support to the needy. I must stress that the allocation of resources by the Government is based on the principle of "policy leads and financial resources follow". For one-off measures or otherwise, the use of all government expenditure should be strictly subject to the same principle of fiscal prudence. We must commit our resources only when justified and needed. Every dollar should be spent on appropriate measures, and not squandered.

127. One-off measures, from a micro perspective, can help ease the community's burden, and are counter-cyclical from a macro perspective for coping with short-term economic fluctuations, maintaining spending power and supporting the employment market. The measures I proposed in last year's Budget had a stimulus effect on GDP that helped maintain local economic growth and a low unemployment rate. In the year ahead, having regard to the uncertain external outlook and the risk of rising inflation caused by quantitative easing measures in various countries, I consider that we still have to introduce some stimulus measures.

128. I have also been listening to the voices of people from the middle class. They have expressed to me the heavy burden they have to bear in coping with expenses on rent, medical care, support for their parents, children's education, etc. They hope that I would consider specific tax measures for them. I agree that middle-class families should be given some support. However, as one may appreciate, it is impracticable for the Government to respond to each and every demand. The Government must take into account its overall financial commitments and the fairness of resource allocation. I am inclined to adopt a simple and direct approach through one-off tax reduction and increase in tax allowance as a response to the various aspirations of the middle class.

129. Many business chambers and SMEs have also told me that increase in rentals and other costs have posed difficulties to the operation of enterprises. They proposed that the Government should introduce relief measures, including lowering the profits tax rate for SMEs with profits below a particular level. I have given due consideration to their proposals. Profits tax revenue is now sourced from a handful of enterprises while nearly 90 per cent of companies do not have to pay tax. There will be practical difficulty in applying different tax rates to those tax-paying enterprises, and this will complicate our simple tax regime. The low profit-making enterprises will not benefit much as a result. Having regard to the implications of the tax proposals on individual enterprises, our tax base and tax revenue, I am inclined to adopt a simple and direct approach through one-off tax reduction to meet the aspirations of our business sector.

130. I propose the following one-off measures:

(a) waiving rates for 2013-14[Note 2], subject to a ceiling of $1,500 per quarter for each rateable property. It is estimated that around 75 per cent of properties will be subject to no rates in the year. This proposal will cost the Government $11.6 billion;

(b) reducing salaries tax and tax under personal assessment for 2012-13 by 75 per cent, subject to a ceiling of $10,000. The reduction, benefiting 1.53 million taxpayers in the territory, will be reflected in the taxpayers' final tax payable for 2012-13. This measure will cost the Government $8.4 billion;

(c) granting each residential electricity account a subsidy of $1,800. This will cost the Government $4.5 billion;

(d) providing an extra allowance to Comprehensive Social Security Assistance (CSSA) recipients, equal to one month of the standard rate CSSA payments; and an extra allowance to Old Age Allowance, Old Age Living Allowance and Disability Allowance recipients, equal to one month of the allowances. This will involve an additional expenditure of $2.7 billion;

[Note 2] Comprehensive Social Security Assistance recipients who do not have to bear rates and public housing rents will not obtain any pecuniary advantage from the two measures of waiving rates and paying rents for public housing tenants.

(e) paying two months' rent for public housing tenants[Note 3]. The Government will pay two months' base rent for tenants who are required to pay extra rent to the Hong Kong Housing Authority. For non-elderly tenants of the Hong Kong Housing Society's Group B estates, the Government will pay two-thirds of their rent for two months. This measure will involve an expenditure of $2.2 billion;

(f) I extended and improved short-term food assistance services through the additional funding of $100 million made in my last Budget. The Labour and Welfare Bureau will seek this Council's approval for the provision in the next financial year. When necessary, the Government will allocate another $100 million for the services; and

(g) giving all student loan borrowers who complete their studies in 2013 the option to start repaying their student loans one year after completion of studies. This will alleviate the financial burden of fresh graduates.

131. To alleviate people's burden in raising their children and to encourage self-education and lifelong learning, I propose:

(a) increasing the basic and additional child allowances from the current $63,000 to $70,000 for each child. After the adjustment, the allowance for babies born in 2013-14 will be $140,000 for the year. This measure will benefit 300 000 taxpayers, estimated to cost the Government $410 million a year; and

[Note 3] See Note 2.

(b) raising the deduction ceiling for self-education expenses from $60,000 to $80,000. This measure will benefit 6 000 taxpayers, estimated to cost the Government $10 million a year.

132. In the face of the unstable external economic environment and increasing operating costs, apart from the six support measures for SMEs that were mentioned earlier, I propose the following two one-off measures to help our enterprises:

(a) waiving the business registration fees for 2013-14 to benefit 1.2 million business operators. This proposal will cost the Government $2.1 billion; and

(b) reducing profits tax for 2012-13 by 75 per cent, subject to a ceiling of $10,000. The reduction will be reflected in the taxpayers' final tax payable for 2012-13. This proposal will benefit 119 000 taxpayers who are liable to profits tax, costing the Government $1 billion.

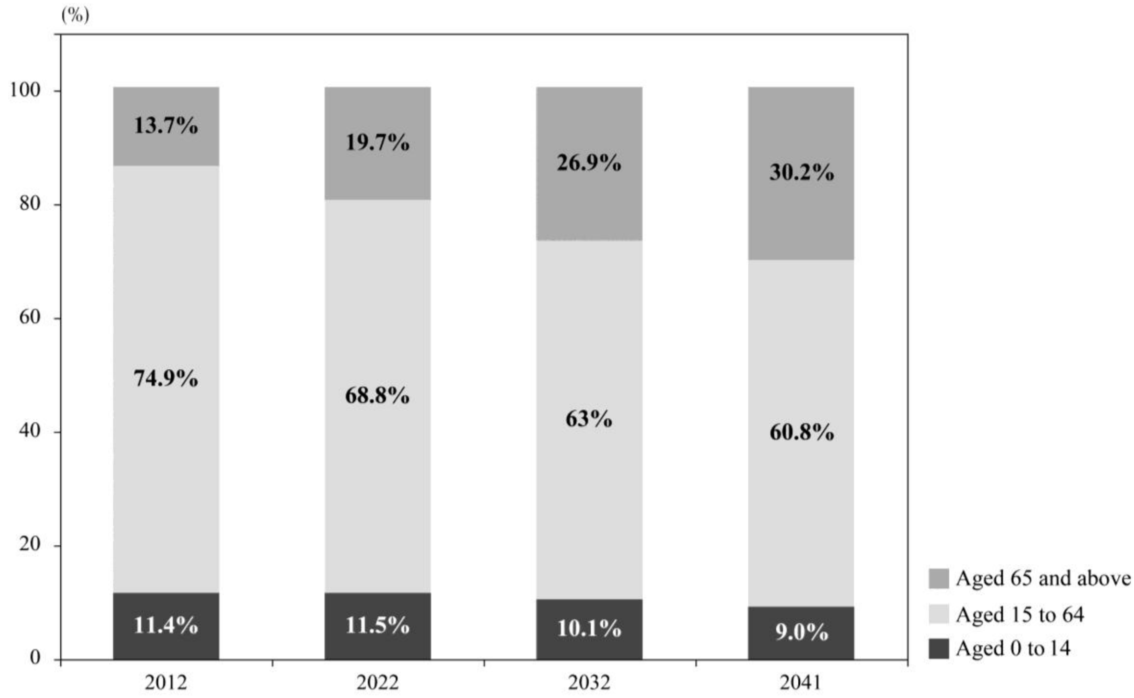
The above 11 relief measures, involving $33 billion, should be able to help ease the pressure on our middle class, grass roots and SMEs.

Embracing the Challenges Ahead

133. The average life expectancy of Hong Kong people is continuously increasing. We must not overlook the challenges posed by an ageing population.

Chart 4

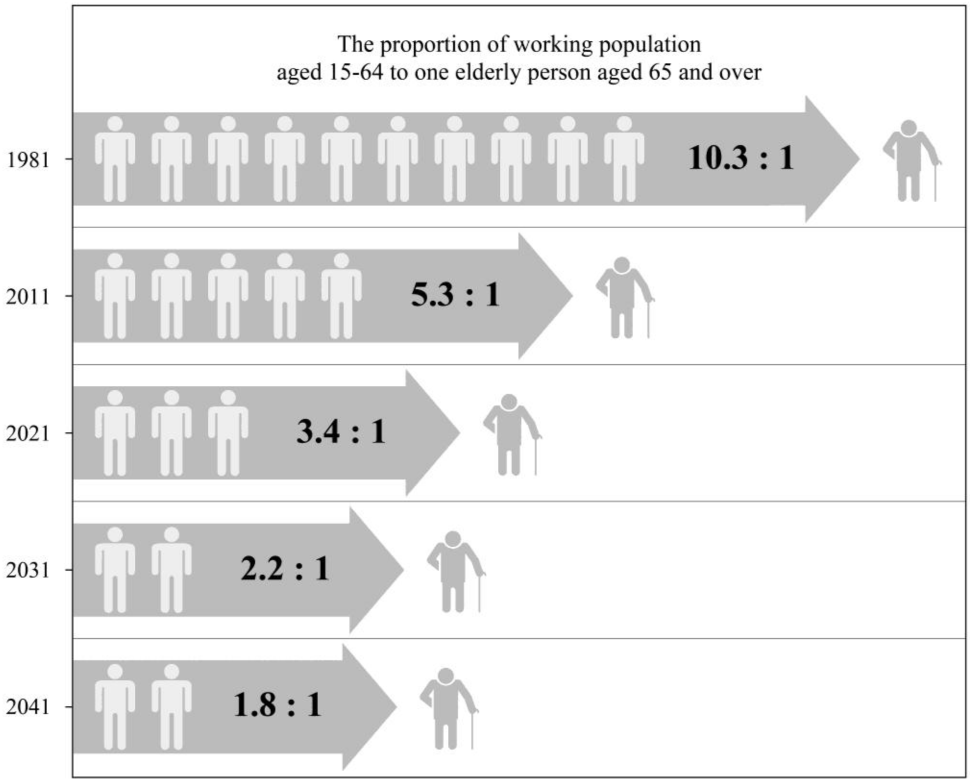
2012 to 2041 Population by age group



134. Last year, the number of elderly people aged 65 and over was 980 000, representing 14 per cent of our population. This proportion continues to rise. According to the latest projection, the number of elderly people will increase significantly to 2.56 million by 2041, representing 30 per cent of our population. As for the elderly dependency ratio in Hong Kong, ten persons of working age (i.e. people aged 15 to 64) supported one dependent elderly person financially in the early 1980s, but the ratio has dropped to five persons supporting one dependent elderly person now. After 20 years, the ratio will further drop to just two persons supporting one dependent elderly person.

Chart 5

Much Heavier Burden Imposed by Ageing Population



Note: Excluding foreign domestic helpers.
Source: Demographic Statistics Section, Census and Statistics Department.

135. The increase in the proportion of elderly population will result in a surge of expenditure on healthcare and welfare. Moreover, a fall in the proportion of working population will reduce economic vibrancy and slow down the momentum of economic growth. These developments will have profound implications for the sustainability of government revenue and public expenditure. Judging from the current demographic trends, our economic growth will certainly continue to taper off in the 2020s and the growth rate will be much lower than the trend growth rate of 4.5 per cent over the past ten years.

136. Our resource inputs in healthcare and social welfare represent 40 per cent of recurrent government expenditure at present. Take the spending on elderly care for 2012-13 as an example. The estimated expenditure in this area, including the provision of social security, elderly services and healthcare services, has reached $43.4 billion, accounting for 16 per cent of recurrent government expenditure. This spending will inevitably increase significantly with an ageing population because there will be a substantial rise in the demand for patient beds, residential care homes and community elderly care.

137. With an increase in the number of the elderly, a shrinking working population, reduction in the number of taxpayers and decelerated economic growth, I expect that the growth of government revenue will drop substantially if our tax regime remains unchanged. Meanwhile, expenditure on welfare and healthcare will soar. We may not be able to make ends meet. Some may think that the purpose of building up ample fiscal reserves is to provide a sufficient reserve capital for Hong Kong when our recurrent revenue is not sufficient to cover expenditure. I would say that this is not wrong but is a rather one-sided view. Of course, we can draw on our reserves to tackle short-term financial fluctuations. Yet fiscal reserves is not a regular revenue, it is all that we have at our disposal. The reserves can be exhausted. Prolonged depletion of the reserves to meet ever-increasing recurrent expenditure is not sustainable. Recurrent expenditure must be funded by sustainable revenue.

138. Apart from meeting our expenditure on public services, fiscal reserves also serve as a buffer in times of economic downturn. Take the five-year deficit between 1998 and 2004 as an example. Our fiscal reserves dropped from an amount equivalent to 28 months of government expenditure originally to a level of 13 months of expenditure in 2004.

139. Besides, we have not deducted the Government's known liabilities, commitments and various contingent liabilities from the fiscal reserve figure that is familiar to you. These include capital projects costing over $300 billion, guarantees of $100 billion and statutory pension with a present value of about $600 billion. Although we do not need to settle them in a lump sum within a short period of time, we must not overlook our liabilities and commitments behind the reserves when assessing the HKSAR's overall financial position.

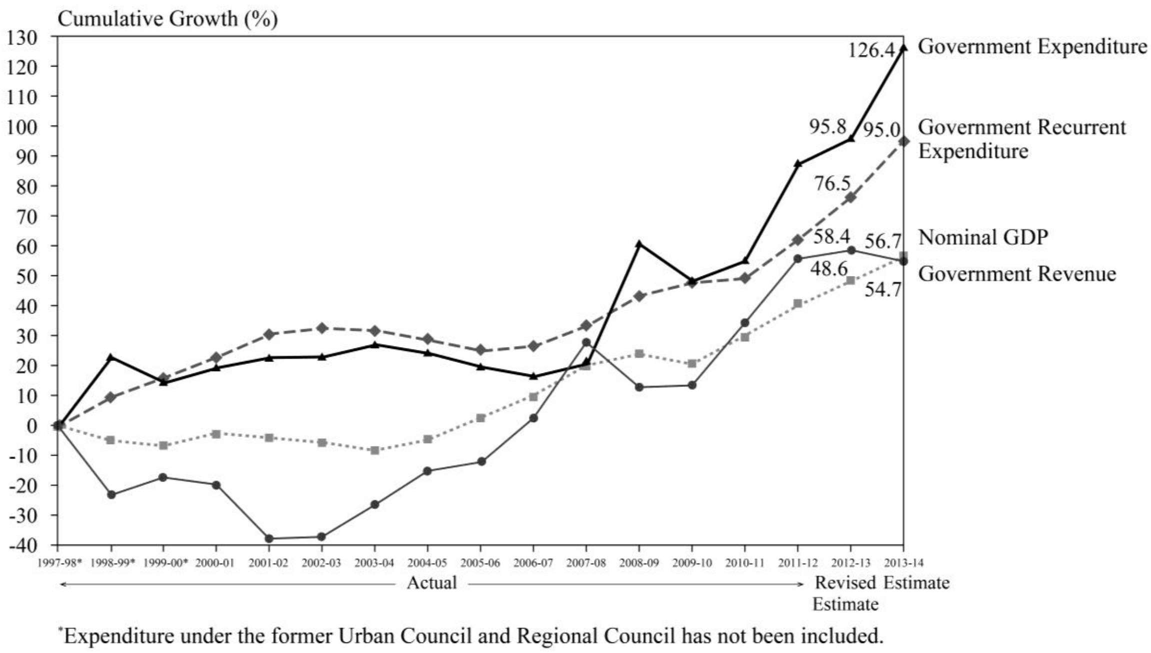
140. Looking globally, many economies are also facing the problem of soaring public expenditure in the long run. Some countries use the resources available to plan for the future through saving up part of their fiscal surplus or other receipts and assets. I shall set up a working group to be led by the Treasury Branch. Scholars and experts will be invited to join the working group to explore ways to make more comprehensive planning for our public finances to cope with the ageing population and the Government's other long-term commitments. The working group will report to me by the end of this year.

Adhering to Fiscal Discipline

141. Government expenditure has more than doubled from nearly $200 billion in 1997-98 to over $400 billion in 2013-14, while recurrent expenditure has almost doubled from $150 billion to over $290 billion. However, GDP has grown by only 60 per cent for the same period. The use of public resources has always been guided by the principle of pragmatism. Resources are allocated in accordance with actual needs and priorities, taking into account fiscal sustainability. When implementing new policies and measures, especially those involving long-term financial commitments, the Government must consider them thoroughly and conduct appropriate consultation in advance.

Chart 6

Growth of Government Revenue, Expenditure and Nominal GDP



*Expenditure under the former Urban Council and Regional Council has not been included.

142. Fiscal sustainability and prudent management of public finances require us to strictly contain the growth of government expenditure. We must not increase expenditure without good cause, or without regard to our low tax regime. Our revenue, now amounting to about 20 per cent of GDP, is unlikely to achieve significant growth. Our public expenditure, on the other hand, has stayed at around the same level in recent years. As we are obliged to uphold the principle of keeping expenditure within the limits of revenue, the Government would need to increase revenue if we want to increase expenditure. This would mean raising taxes or resorting to borrowing. Both options are controversial. Tax hikes will overhaul our simple and low tax regime which has been the key to our success, and undermine Hong Kong's overall competitiveness in the longer run. This will also adversely affect our community and businesses. We must carefully assess the pros and cons in considering any proposal to increase tax.

143. In the wake of the financial tsunami, many European countries and the US have fallen into financial difficulty. The major causes are the prolonged mismanagement of public finances by their governments and over-expanded welfare measures. Beset with huge debts from overspending, these countries eventually find themselves in a dire financial crisis, and have to cut the deficit through fiscal austerity. Hong Kong must draw a lesson from them. We must maintain effective fiscal management and fiscal discipline by adhering to the principles of keeping expenditure within the limits of revenues and allocating resources where they are required. Any indiscriminate increase in expenditure will only impose a heavy burden on our next generation.

Government Revenue

144. We need to ensure that the Government has a stable income by preserving tax revenue and adhering to the "user pays" principle. Tax revenue, accounting for more than 60 per cent of the total government revenue, exceeds $280 billion in 2013-14. Of this, two-thirds will come from direct taxes (i.e. profits tax, tax under personal assessment, property tax and salaries tax) and the remaining one-third from indirect taxes (e.g. rates, motor vehicles first registration tax and duty on dutiable commodities).

145. On the premise of maintaining the existing low and simple tax regime, we shall strive to prevent revenue losses on payable taxes. To this end, the Government will examine the tax information stated by taxpayers through an audit and investigation mechanism. Back tax is assessed and penalties are imposed on cases of understatement or omission. In 2011-12, the Inland Revenue Department (IRD) collected back tax and penalties of about $6.8 billion, which was 76 per cent higher than that of the previous year. The IRD will continue to combat tax evasion and avoidance, and strive for greater effectiveness by making better use of information technology, reinforcing staff training and adjusting investigation strategies.

146. Regarding indirect taxes, the annual revenue from tobacco duty and motor vehicles first registration tax is over $4 billion and $7 billion respectively. We notice that the main modus operandi of selling illicit cigarettes has recently changed from street peddling to telephone order, making law enforcement more difficult. On the other hand, some dealers provide false information on the selling prices of vehicles to evade motor vehicles first registration tax, which reduces our tax revenue. To protect the revenue from tobacco duty and motor vehicles first registration tax, the C&ED will deploy more resources to step up its efforts to combat tax evasion in the coming year.

147. The provision of government services is generally charged in accordance with the "user pays" principle. There are thousands of fees and charges, including all types of licence fees and other fees related to the issue of identity documents, registration, etc. The cost recovery rate for some items is as low as 30 per cent. The rate for more than 1 000 fees and charges has not been adjusted since reunification.

148. In 1997-98, government services with charges determined on a cost-recovery basis generated nearly $12 billion in revenue, equivalent to four per cent of government revenue. In 2011-12, revenue from this source dropped to only $10 billion, or a share of only two per cent of revenue.

149. To prevent cost recovery items being turned into heavily subsidised items, we need a systematic review. I shall ask all policy bureaux and departments to review their respective fees and charges, and submit plans for their revision for the coming one or two years. We shall first deal with fees that have not been revised for years and do not directly affect people's livelihood. Examples are fees for pesticide permits, riding establishment licences and temporary permits for exhibitions of animals and birds. We shall also deal with items which have low cost recovery rates such as fees for visas or licences for storage of dangerous goods. The Government will make appropriate fee revisions as and when necessary. There will not be substantial revisions at one go to avoid affecting people's livelihood. We shall also strictly control costs and reduce the need for increasing fees and charges as far as possible. I hope that the community will consider our proposals for fee revisions in a fair and objective manner.

Revised Estimates for 2012-13

150. When I prepared the 2012-13 Budget early last year, I made a prudent forecast for government revenue in view of the global economic downturn, sluggish export and local economic slowdown. One year on, my forecast about the economic conditions has proved to be accurate. However, our actual revenue from various items now exceeds the original estimate. Despite the economic fluctuations last year, local enterprises showed strong resilience. Revenue from earnings and profits tax is $24.8 billion higher than the original estimate. With the Government stepping up land sale to increase land supply, revenue from land premium has also increased by $9.1 billion compared to the original estimate. Given hectic trading in the property market in the first three quarters and a bullish stock market in the fourth quarter of this year, stamp duty revenue is $6 billion higher than the original estimate. Moreover, the dividend from the West Rail Property Development Limited is about $10 billion higher than the original estimate. Taking all these into account, the revised estimate for government revenue for 2012-13 is $445.5 billion, $55.2 billion higher than the original estimate. As for government expenditure, I forecast a revised estimate of $380.6 billion, three per cent or $13.1 billion less than the original estimate.

151. For 2012-13, I forecast a surplus of about $64.9 billion. By 31 March 2013, our fiscal reserves are expected to be $734 billion, equivalent to 36 per cent of GDP or 23 months of government expenditure.

Estimates for 2013-14

152. Operating expenditure for 2013-14 is estimated to be $352 billion and recurrent expenditure will be $291.3 billion, representing an increase of 15.5 per cent and 10.5 per cent respectively over the revised estimate for 2012-13. It is estimated that capital expenditure will be $88 billion, including $70.1 billion on capital works. I forecast that total government expenditure will reach $440 billion, an increase of 15.6 per cent compared with the revised estimate for 2012-13. Public expenditure will be equivalent to 21.7 per cent of GDP.

153. The increases in expenditure, both total and recurrent, for 2013-14 far exceed the estimated nominal GDP growth of 5.5 per cent in 2013. This clearly demonstrates that the current-term Government upholds the principle of committing resources as and when needed to provide appropriate services for the community.

154. Total government revenue for 2013-14 is estimated to be $435.1 billion. Earnings and profits tax, estimated at $189.4 billion, will be our major source of revenue. Land revenue is estimated at $69 billion.

155. Taking all these into account, it is expected that a small deficit of about $4.9 billion will be recorded in our accounts in the coming year, and we shall largely achieve fiscal balance. Fiscal reserves are estimated at $729.1 billion by end-March 2014, representing approximately 34 per cent of GDP or equivalent to 20 months of government expenditure.

Medium Range Forecast

156. For the medium term, the annual average growth rate will be four per cent in real terms for the four-year period between 2014 and 2017, while the underlying inflation rate will average 3.5 per cent. The Operating Account will see a surplus for the period between 2014-15 and 2017-18. With expenditure on infrastructure projects ever increasing, a deficit will arise in the Capital Account for the whole period. Fiscal reserves are estimated at $850.3 billion by end-March 2018, representing 31 per cent of GDP or 21 months of government expenditure.

Concluding Remarks

157. Mr President, since Hong Kong's return to the Motherland, Hong Kong has experienced several periods of ups and downs, including two shattering financial crises. Thanks to the sound institutional framework and stable economic foundations built up by generations of Hong Kong people over decades, we were able to ride out the storm. It was not by chance that we were immune from the big cuts in public expenditure that the US and most European countries have been forced to make because of their severe fiscal deficits.

158. By developing the economy and creating wealth, we can provide opportunities for everyone to realise his aspirations and live a better life. That is why the Government has always attached importance to economic development. Hong Kong is now a fairly mature economy. Compared with the rapid growth in the 1970s and 1980s, we are unavoidably slowing down. Nevertheless, in the face of keen global competition, we must still endeavour to look for new growth areas. Otherwise, we can only mark time rather than stride ahead, and will lag behind others.

159. When I was young, our living environment was inferior to that of today, and many families lived in squatter areas or resettlement areas. They might not even have gas, electricity or water supply at home. Family members used to sleep on make-shift plain planks or canvas beds. Every morning, they woke up, stretched their backs and went to school or work. Today, our living environment has improved considerably. We should not, of course, apply the standard in the past to judge the quality of life today.

160. Similarly, civil society has evolved rapidly and brought with it changes in our social values. Hong Kong people, especially our younger generation, aspire to live in a society which values equality and justice for all, with dignity and respect for each individual, and care for the disadvantaged. I am all for this. An ideal society hinges on having the right conditions and resolving the core question of where to get the resources required. A politician once said, "Keep your eyes on the stars, and your feet on the ground." This comes as a timely reminder for today's Hong Kong. Put simply: we must take the pragmatic way.

161. Wealth redistribution seems to be a quick fix to improve the livelihood of the grass roots. But the lesson in Europe in recent years tells us that welfarism is not sustainable. It has long been my steadfast belief that we can provide everyone opportunities to change his life through developing the economy, creating quality employment opportunities, investing vigorously in education and training to increase social mobility. I trust that this is also a common value for all of us.

162. In almost every movie and TV drama series featuring Hong Kong, you are likely to come across these scenes: queues of vehicles along roads and crowds of pedestrians jostling against each other amid the hustle and bustle of the city. You can feel a unique buzz. Call it hectic or even chaotic, in Hong Kong everyone is free to live his own way and make his own choice. While our seven million people may have seven million different lifestyles, seemingly unconnected to each other, we share the same vision and values that unite us and drive us to forge ahead. Hong Kong people of different generations and backgrounds are all positive, optimistic and resilient. We strive for continued improvement and never yield to fate. I believe we shall build a better and brighter future together.

163. Thank you, Mr President.

THE 2013-14 BUDGET

Speech by the Financial Secretary, the Hon John C Tsang
moving the Second Reading of the Appropriation Bill 2013

Supplement and Appendices

Wednesday, 27 February 2013

SUPPLEMENT

Please visit our web-site at www.budget.gov.hk/2013/eng/speech.html for all documents, appendices and statistics relating to the 2013–14 Budget. The Chinese version can be found at www.budget.gov.hk/2013/chi/speech.html.

Contents

EFFECT OF THE GENERAL REVALUATION OF RATES ON MAIN PROPERTY CLASSES

Property Type	*2013-14* Average Increase in Rateable Value[(6)] %	*2013-14* New Average Rates Payable[(7)] $ per month	*2013-14* Increase[(8)] $ per month
Small Domestic Premises[(1)] (Private)	+11	394	**+38**
Medium Domestic Premises[(1)] (Private)	+8	926	**+72**
Large Domestic Premises[(1)] (Private)	+6	2,257	**+120**
Public Domestic Premises[(2)]	+10	203	**+18**
All Domestic Premises[(3)]	+9	410	**+34**
Shops and Commercial Premises	+7	2,741	**+187**
Offices	+6	3,396	**+184**
Industrial Premises[(4)]	+8	1,000	**+72**
All Non-domestic Premises[(5)]	+7	2,645	**+175**
All Properties	+8	701	**+53**

(1) Domestic units are classified by saleable areas, as follows –

Small domestic	up to $69.9m^2$	(up to 752 sq. ft.)
Medium domestic	$70m^2$ to $99.9m^2$	(753 sq. ft. to 1 075 sq. ft.)
Large domestic	$100m^2$ and over	(1 076 sq. ft. and over)

(2) Including Housing Authority and Housing Society rental units.

(3) Including car parking spaces in domestic premises.

(4) Including factories and storage premises.

(5) Including miscellaneous premises such as hotels, cinemas, petrol filling stations, schools and car parking spaces in non-domestic premises.

(6) The rateable values for 2013-14 reflect changes in open market rental values between 1 October 2011 and 1 October 2012.

(7) The effect of the proposed rates concession in 2013-14 has not been taken into account.

(8) The effect of rates concession in 2012-13 has not been taken into account.

EFFECT OF THE GENERAL REVALUATION OF GOVERNMENT RENT ON MAIN PROPERTY CLASSES

Property Type	*2013-14* Average Increase in Rateable Value[6] %	New Average Rent Payable $ per month	Increase $ per month
Small Domestic Premises[1] (Private)	+11	223	**+21**
Medium Domestic Premises[1] (Private)	+8	522	**+38**
Large Domestic Premises[1] (Private)	+5	1,087	**+54**
Public Domestic Premises[2]	+10	120	**+11**
All Domestic Premises[3]	+9	217	**+18**
Shops and Commercial Premises	+7	1,530	**+98**
Offices	+4	3,609	**+138**
Industrial Premises[4]	+8	599	**+43**
All Non-domestic Premises[5]	+6	1,422	**+84**
All Properties	+8	347	**+26**

(1) Domestic units are classified by saleable areas, as follows –

Small domestic	up to 69.9m²	(up to 752 sq. ft.)
Medium domestic	70m² to 99.9m²	(753 sq. ft. to 1 075 sq. ft.)
Large domestic	100m² and over	(1 076 sq. ft. and over)

(2) Including Housing Authority and Housing Society rental units.

(3) Including car parking spaces in domestic premises.

(4) Including factories and storage premises.

(5) Including miscellaneous premises such as hotels, cinemas, petrol filling stations, schools and car parking spaces in non-domestic premises.

(6) The rateable values for 2013-14 reflect changes in open market rental values between 1 October 2011 and 1 October 2012.

SALARIES TAX

Changes to Allowances and Deductions

	Present ($)	*Proposed* ($)	*Increase* ($)	(%)
Personal Allowances:				
Basic	120,000	120,000	—	—
Married	240,000	240,000	—	—
Single Parent	120,000	120,000	—	—
Other Allowances:				
Child:				
1st to 9th child				
Year of birth	126,000	140,000	14,000	11.1
Other years	63,000	70,000	7,000	11.1
Dependent Parent/Grandparent:				
Aged 60 or above				
Basic	38,000	38,000	—	—
Additional allowance (for a dependant living with the taxpayer)	38,000	38,000	—	—
Aged 55 to 59				
Basic	19,000	19,000	—	—
Additional allowance (for a dependant living with the taxpayer)	19,000	19,000	—	—
Dependent Brother/Sister	33,000	33,000	—	—
Disabled Dependant	66,000	66,000	—	—
Deduction Ceiling:				
Self-Education Expenses	60,000	80,000	20,000	33.3
Home Loan Interest (Number of years of deduction)	100,000 (15 years of assessment)	100,000 (15 years of assessment)	—	—
Approved Charitable Donations	35% of income	35% of income	—	—
Elderly Residential Care Expenses	76,000	76,000	—	—
Contributions to Recognised Retirement Schemes	15,000	15,000	—	—

Effect of the proposed one-off reduction of salaries tax, tax under personal assessment and profits tax

Salaries tax and tax under personal assessment-
75% tax reduction subject to a cap at $10,000 per case

Income in 2012-13	No. of taxpayers	Average amount of tax reduction	Average % of tax reduced
$120,001 to $200,000	351 000	$670	75%
$200,001 to $300,000	367 000	$3,470	73%
$300,001 to $400,000	256 000	$6,040	53%
$400,001 to $600,000	279 000	$8,270	31%
$600,001 to $900,000	141 000	$9,840	16%
Above $900,000	136 000	$10,000	3%
Total	1 530 000	—	—

Profits tax-
75% tax reduction subject to a cap at $10,000 per case

Profits in 2012-13	No. of businesses	Average amount of tax reduction	Average % of tax reduced
$100,000 and below	39 000	$4,330	72%
$100,001 to $200,000	16 000	$10,000	41%
$200,001 to $300,000	9 000	$10,000	24%
$300,001 to $400,000	6 000	$10,000	17%
$400,001 to $600,000	9 000	$10,000	12%
$600,001 to $900,000	7 000	$10,000	8%
Above $900,000	33 000	$10,000	0.3%
Total	119 000	—	—

ECONOMIC PERFORMANCE IN 2012

1. Estimated rates of change in the Gross Domestic Product and its expenditure components and in the main price indicators in 2012:

		(%)
(a) Growth rates in real terms of:		
Private consumption expenditure		4.0
Government consumption expenditure		3.7
Gross domestic fixed capital formation		9.1
of which :		
Building and construction	12.3	
Machinery, equipment and intellectual property products	10.6	
Total exports of goods		1.3
Imports of goods		2.7
Exports of services		1.2
Imports of services		0.7
Gross Domestic Product (GDP)		**1.4**
Per capita GDP in real terms		0.3
Per capita GDP at current market prices	HK$285,100 (US$36,800)	
(b) Rates of change in:		
Composite Consumer Price Index		**4.1**
GDP Deflator		**3.9**
Government Consumption Expenditure Deflator		**6.1**
(c) **Growth rate of nominal GDP**		**5.4**

2. Annual growth rates in real terms of re-exports and domestic exports based on external trade quantum index numbers:

	Re-exports (%)	***Domestic exports*** (%)
2010	18	16
2011	3	-12
2012	0	-13
Share in the value of total exports of goods in 2012	*98*	*2*

3. Annual growth rates in real terms of retained imports by type:

	Retained imports					
	Total (%)	***Consumer goods*** (%)	***Foodstuffs*** (%)	***Capital goods*** (%)	***Raw materials and semi-manufactures*** (%)	***Fuels*** (%)
2010	20	22	12	16	31	14
2011	8	33	6	15	-4	-10
2012	4	6	2	22	-6	-7

4. Annual growth rates in real terms of retained imports of capital goods by type:

	Retained imports of capital goods				
	Total (%)	***Office equipment*** (%)	***Industrial machinery*** (%)	***Construction machinery*** (%)	***Telecommunications equipment*** (%)
2010	16	-6	12	18	27
2011	15	-20	-10	-14	126
2012	22	22	-26	-26	100

5. Annual growth rates in real terms of exports of services by type:

	Exports of services				
	Total (%)	***Trade-related services*** (%)	***Transportation services*** (%)	***Travel services*** (%)	***Finance, insurance, business and other services*** (%)
2010	15	12	8	26	17
2011	5	3	1	13	5
2012	1	1	-3	9	-1

6. Hong Kong's visible and invisible trade balance in 2012 reckoned on GDP basis *(Note 1)*:

		(HK$ billion)
Total exports of goods	3,580.8	
Imports of goods	4,116.4	
Visible trade balance		**-535.6**
Exports of services	985.8	
Imports of services	449.4	
Invisible trade balance		**536.4**
Combined visible and invisible trade balance		**0.8**

Note 1 Preliminary figures.

7. Annual averages of the unemployment and underemployment rates and growth in labour force and total employment:

	Unemployment rate (%)	***Underemployment rate*** (%)	***Growth in labour force*** (%)	***Growth in total employment*** (%)
2010	4.3	2.0	-0.8	0.2
2011	3.4	1.7	2.0	2.9
2012	3.3	1.5	2.4	2.5

8. Annual rates of change in the Consumer Price Indices:

	Composite CPI				
	Headline (%)	***Underlying*** (%)	***CPI(A)*** (%)	***CPI(B)*** (%)	***CPI(C)*** (%)
2010	2.4	1.7	2.7	2.3	2.1
2011	5.3	5.3	5.6	5.2	5.1
2012	4.1	4.7	3.6	4.3	4.1

ECONOMIC PROSPECTS FOR 2013

Forecast rates of change in the Gross Domestic Product and prices in 2013:

		(%)
Gross Domestic Product (GDP)		
Real GDP		**1.5 to 3.5**
Nominal GDP		4.5 to 6.5
Per capita GDP in real terms		0.7 to 2.7
Per capita GDP at current market prices	HK$295,600-301,300 (US$37,900-38,600)	
Composite Consumer Price Index		
Headline Composite Consumer Price Index		**4.5**
Underlying Composite Consumer Price Index		**4.2**
GDP Deflator		**3.0**

APPENDICES

APPENDICES

Note: Expenditure figures for 2012-13 and before have been adjusted to align with the definitions and policy area group classifications adopted in the 2013-14 estimate.

APPENDIX A

MEDIUM RANGE FORECAST

CONTENTS **Page**

SECTION I FORECASTING ASSUMPTIONS AND BUDGETARY CRITERIA

1 A wide range of assumptions on the factors affecting Government's revenue and expenditure are used to derive the Medium Range Forecast (MRF). Some assumptions are economic in nature (the general economic assumptions) while others deal with specific areas of Government's activities (the detailed assumptions).

General Economic Assumptions

Real Gross Domestic Product (real GDP)

2 GDP is forecast to increase by 1.5% to 3.5% in real terms in 2013. We have used the mid-point of this range forecast in deriving the MRF. For planning purposes, in the four-year period 2014 to 2017, the trend growth rate of the economy in real terms is assumed to be 4% per annum.

Price change

3 The GDP deflator, measuring overall price change in the economy, is forecast to increase by 3% in 2013. For the four-year period 2014 to 2017, the GDP deflator is assumed to increase at a trend rate of 2% per annum.

4 The Composite Consumer Price Index (CCPI), measuring inflation in the consumer domain, is forecast to increase by 4.5% in 2013. Netting out the effects of various one-off relief measures, the underlying CCPI is forecast to increase by 4.2% in 2013. For the ensuing period 2014 to 2017, the trend rate of increase for the underlying CCPI is assumed to be 3.5% per annum.

Nominal Gross Domestic Product (nominal GDP)

5 Given the assumptions on the rates of change in the real GDP and the GDP deflator, the GDP in nominal terms is forecast to increase by 4.5% to 6.5% in 2013, and the trend growth rate in nominal terms for the period 2014 to 2017 is assumed to be 6% per annum.

Detailed Assumptions

6 The MRF incorporates a wide range of detailed assumptions on expenditure and revenue patterns over the forecast period, taking the following, amongst other factors, into account –

— estimated cash flow of capital projects,
— forecast completion dates of these capital projects and their related recurrent consequences in terms of staffing and running costs,
— estimated cash flow arising from new commitments and policy initiatives,
— the expected pattern of demand for individual services,
— the trend in yield from individual revenue sources, and
— new initiatives in the 2013-14 Budget.

Budgetary Criteria

7 Article 107 of the Basic Law stipulates that "the Hong Kong Special Administrative Region shall follow the principle of keeping expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with the growth rate of its gross domestic product".

8 Article 108 of the Basic Law stipulates that "the Hong Kong Special Administrative Region shall, taking the low tax policy previously pursued in Hong Kong as reference, enact laws on its own concerning types of taxes, tax rates, tax reductions, allowances and exemptions, and other matters of taxation".

9 For the purpose of preparing the MRF, the following criteria are also relevant –

— *Budget surplus/deficit*

The Government aims to achieve a balance in the consolidated and operating accounts. The Government needs, over time, to achieve an operating surplus to partially finance capital expenditure.

— *Expenditure policy*

The general principle is that, over time, expenditure growth should not exceed the growth of the economy. The Government aims to keep public expenditure at or below 20% of GDP.

— *Revenue policy*

The Government aims to maintain, over time, the real yield from revenue.

— *Fiscal reserves*

The Government aims to maintain adequate reserves in the long run.

SECTION II MEDIUM RANGE FORECAST

10 The current MRF *(Note (a))* is summarised in the following table which indicates the forecast financial position of the Government –

Table 1

($ million)	2012–13 Revised Estimate	2013–14 Estimate	2014–15 Forecast	2015–16 Forecast	2016–17 Forecast	2017-18 Forecast
Operating Account						
Operating revenue *(Note (b))*	347,935	349,460	392,889	431,592	449,051	476,102
Less: Operating expenditure *(Note (c))*	304,828	352,000	321,100	390,400	360,800	382,400
Operating surplus/(deficit)	**43,107**	**(2,540)**	**71,789**	**41,192**	**88,251**	**93,702**
Capital Account						
Capital revenue *(Note (d))*	97,571	85,598	55,226	61,332	61,006	65,472
Less: Capital expenditure *(Note (e))*	75,787	87,983	103,318	101,068	102,815	99,732
Capital surplus/(deficit)	**21,784**	**(2,385)**	**(48,092)**	**(39,736)**	**(41,809)**	**(34,260)**
Consolidated Account						
Government revenue	445,506	435,058	448,115	492,924	510,057	541,574
Less: Government expenditure	380,615	439,983	424,418	491,468	463,615	482,132
Consolidated surplus/(deficit) before repayment of bonds and notes	**64,891**	**(4,925)**	**23,697**	**1,456**	**46,442**	**59,442**
Less: Repayment of bonds and notes *(Note (f))*	-	-	9,750	-	-	-
Consolidated surplus/(deficit) after repayment of bonds and notes	**64,891**	**(4,925)**	**13,947**	**1,456**	**46,442**	**59,442**
Fiscal reserves at 31 March	**733,979**	**729,054**	**743,001**	**744,457**	**790,899**	**850,341**
In terms of number of months of government expenditure	23	20	21	18	20	21
In terms of percentage of GDP	36.0%	33.9%	32.6%	30.8%	30.9%	31.3%

Notes –

(a) Accounting policies

(i) The MRF is prepared on a cash basis and reflects forecast receipts and payments, whether they relate to operating or capital transactions.

(ii) The MRF includes the General Revenue Account and eight Funds (Capital Investment Fund, Capital Works Reserve Fund, Civil Service Pension Reserve Fund, Disaster Relief Fund, Innovation and Technology Fund, Land Fund, Loan Fund and Lotteries Fund). It does not include the Bond Fund which is managed separately and the balance of which does not form part of the fiscal reserves.

(b) Operating revenue

(i) The operating revenue takes into account the revenue measures proposed in the 2013-14 Budget, and is made up of –

($ million)	2012–13 Revised Estimate	2013–14 Estimate	2014–15 Forecast	2015–16 Forecast	2016–17 Forecast	2017-18 Forecast
Operating revenue before investment income	316,755	319,632	369,494	390,268	412,651	437,189
Investment income	31,180	29,828	23,395	41,324	36,400	38,913
Total	347,935	349,460	392,889	431,592	449,051	476,102

(ii) Investment income under the Operating Account includes investment income of the General Revenue Account which is credited to revenue head Properties and Investments, and investment income of the Land Fund. The rate of investment return for 2013 is 5.0% and for 2014 to 2017 is assumed to be in the range of 3.7% to 6.2% a year.

(c) Operating expenditure

This represents expenditure charged to the Operating Account of the General Revenue Account. The levels of operating expenditure in 2013-14 to 2017-18 represent the expenditure guideline for these years. The sum for 2015-16 has included $50 billion for supporting healthcare reform.

(d) Capital revenue

(i) The breakdown of capital revenue is –

($ million)	2012–13 Revised Estimate	2013–14 Estimate	2014–15 Forecast	2015–16 Forecast	2016–17 Forecast	2017-18 Forecast
General Revenue Account	16,532	5,365	1,487	5,078	2,677	3,636
Capital Investment Fund	1,299	1,211	999	984	1,048	972
Capital Works Reserve Fund	69,189	69,131	45,400	48,138	51,040	54,377
Innovation and Technology Fund	49	14	-	-	-	-
Loan Fund	2,246	2,303	2,447	2,445	2,449	2,503
Lotteries Fund	1,145	1,165	1,192	1,221	1,250	1,279
Capital revenue before asset sales and investment income	90,460	79,189	51,525	57,866	58,464	62,767
Asset sales	266	237	298	298	298	298
Investment income	6,845	6,172	3,403	3,168	2,244	2,407
Total	97,571	85,598	55,226	61,332	61,006	65,472

(ii) Land premium included under the Capital Works Reserve Fund for 2013-14 is assumed to stay at around the same level as that for 2012-13. For 2014-15 onwards, it is assumed to be 2% of GDP.

(iii) Investment income under the Capital Account includes investment income of the Capital Investment Fund, Capital Works Reserve Fund, Civil Service Pension Reserve Fund, Disaster Relief Fund, Innovation and Technology Fund, Loan Fund and Lotteries Fund.

(e) *Capital expenditure*

The breakdown of capital expenditure is –

($ million)	2012–13 Revised Estimate	2013–14 Estimate	2014–15 Forecast	2015–16 Forecast	2016–17 Forecast	2017-18 Forecast
General Revenue Account	3,170	3,397	3,970	3,970	3,970	3,970
Capital Investment Fund	779	865	628	268	268	268
Capital Works Reserve Fund	67,336	77,839	90,660	89,989	92,846	90,347
Disaster Relief Fund	55	-	-	-	-	-
Innovation and Technology Fund	742	785	884	980	1,016	1,048
Loan Fund	2,735	3,808	5,209	4,030	3,010	2,895
Lotteries Fund	970	1,289	1,967	1,831	1,705	1,204
Total	75,787	87,983	103,318	101,068	102,815	99,732

(f) *Repayment of bonds and notes*

Repayment of bonds and notes is only in respect of the global bond issue in 2004. Outstanding principal as at 31 March 2018 is estimated at $1,500 million.

SECTION III RELATIONSHIP BETWEEN GOVERNMENT EXPENDITURE/PUBLIC EXPENDITURE AND GDP IN THE MEDIUM RANGE FORECAST

11 For monitoring purposes, expenditure of the Trading Funds and the Housing Authority (collectively referred to as "other public bodies" in this Appendix) is added to government expenditure in order to compare public expenditure with GDP.

Government Expenditure and Public Expenditure in the Context of the Economy

Table 2

($ million)	2012–13 Revised Estimate	2013–14 Estimate	2014–15 Forecast	2015–16 Forecast	2016–17 Forecast	2017-18 Forecast
Operating expenditure	304,828	352,000	321,100	390,400	360,800	382,400
Capital expenditure	75,787	87,983	103,318	101,068	102,815	99,732
Government expenditure	380,615	439,983	424,418	491,468	463,615	482,132
Other public bodies expenditure	24,912	27,085	28,615	30,212	31,508	32,740
Public expenditure *(Note (a))*	405,527	467,068	453,033	521,680	495,123	514,872
Gross Domestic Product (calendar year)	2,040,104	2,152,300	2,281,400	2,418,300	2,563,400	2,717,200
Nominal growth in GDP *(Note (b))*	5.4%	5.5%	6.0%	6.0%	6.0%	6.0%
Growth in government expenditure *(Note (c))*	4.6%	15.6%	-3.5%	15.8%	-5.7%	4.0%
Growth in public expenditure *(Note (c))*	5.2%	15.2%	-3.0%	15.2%	-5.1%	4.0%
Public expenditure in terms of percentage of GDP	19.9%	21.7%	19.9%	21.6%	19.3%	18.9%

Notes –

(a) Public expenditure comprises government expenditure and expenditure by other public bodies. It does not include expenditure by those organisations, including statutory organisations in which the Government has only an equity position, such as the Airport Authority and the MTR Corporation Limited.

(b) For 2013-14, the nominal GDP growth of 5.5% represents the mid-point of the range forecast of 4.5% to 6.5% for the calendar year 2013.

(c) The growth rates refer to year-on-year change. For example, the rates for 2012-13 refer to the change between revised estimate for 2012-13 and actual expenditure in 2011-12. The rates for 2013-14 refer to the change between the 2013-14 estimate and the 2012-13 revised estimate, and so forth.

12 Table 3 shows the relationship amongst the sum to be appropriated in the 2013-14 Budget, government expenditure and public expenditure.

Relationship between Government Expenditure and Public Expenditure in 2013-14

Table 3

($ million)	Appropriation	Government expenditure and revenue			Public expenditure
		Operating	Capital	Total	
Expenditure					
General Revenue Account					
Operating					
Recurrent	291,282	291,282	-	291,282	291,282
Non-recurrent	60,718	60,718	-	60,718	60,718
Capital					
Plant, equipment and works	2,033	-	2,033	2,033	2,033
Subventions	1,364	-	1,364	1,364	1,364
	355,397	352,000	3,397	355,397	355,397
Transfer to Funds	743	-	-	-	-
Capital Investment Fund	-	-	865	865	865
Capital Works Reserve Fund	-	-	77,839	77,839	77,839
Innovation and Technology Fund	-	-	785	785	785
Loan Fund	-	-	3,808	3,808	3,808
Lotteries Fund	-	-	1,289	1,289	1,289
Trading Funds	-	-	-	-	5,152
Housing Authority	-	-	-	-	21,933
	356,140	352,000	87,983	439,983	467,068
Revenue					
General Revenue Account					
Taxation		285,679	70	285,749	
Other revenue		53,318	5,295	58,613	
		338,997	5,365	344,362	
Land Fund		10,463	-	10,463	
		349,460	5,365	354,825	
Capital Investment Fund		-	1,287	1,287	
Capital Works Reserve Fund		-	73,249	73,249	
Civil Service Pension Reserve Fund		-	1,287	1,287	
Disaster Relief Fund		-	2	2	
Innovation and Technology Fund		-	119	119	
Loan Fund		-	2,624	2,624	
Lotteries Fund		-	1,665	1,665	
		349,460	85,598	435,058	
Deficit		(2,540)	(2,385)	(4,925)	

SECTION IV CONTINGENT AND MAJOR UNFUNDED LIABILITIES

13 The Government's contingent liabilities as at 31 March 2012, 31 March 2013 and 31 March 2014, are provided below as supplementary information to the MRF –

($ million)	2012 Actual	At 31 March 2013 Estimate	2014 Estimate
Guarantees provided under the Special Loan Guarantee Scheme	62,751	50,350	46,888
Guarantee to the Hong Kong Export Credit Insurance Corporation for liabilities under contracts of insurance	23,751	28,725	30,500
Guarantees provided under the SME Financing Guarantee Scheme – Special Concessionary Measures	-	24,954	24,155
Guarantees provided under the SME Loan Guarantee Scheme	7,012	7,844	9,128
Possible capital subscriptions to the Asian Development Bank	6,607	6,543	6,543
Guarantees provided under a commercial loan of the Ocean Park Corporation	1,388	1,388	1,388
Litigation	3,168	3,497	168
Guarantees provided under a special finance scheme for small and medium enterprises	16	16	16
Total	104,693	123,317	118,786

14 The Government's major unfunded liabilities as at 31 March 2012 were as follows –

($ million)	
Present value of statutory pension obligations	641,371
Untaken leave *(Note (a))*	23,586
Government bonds and notes issued in 2004 *(Note (b))*	11,250

Notes –

(a) The estimate for 'untaken leave' gives an indication of the overall value of leave earned but not yet taken by serving public officers.

(b) Based on US$1 = HK$7.8

APPENDIX B

ANALYSIS OF EXPENDITURE AND REVENUE

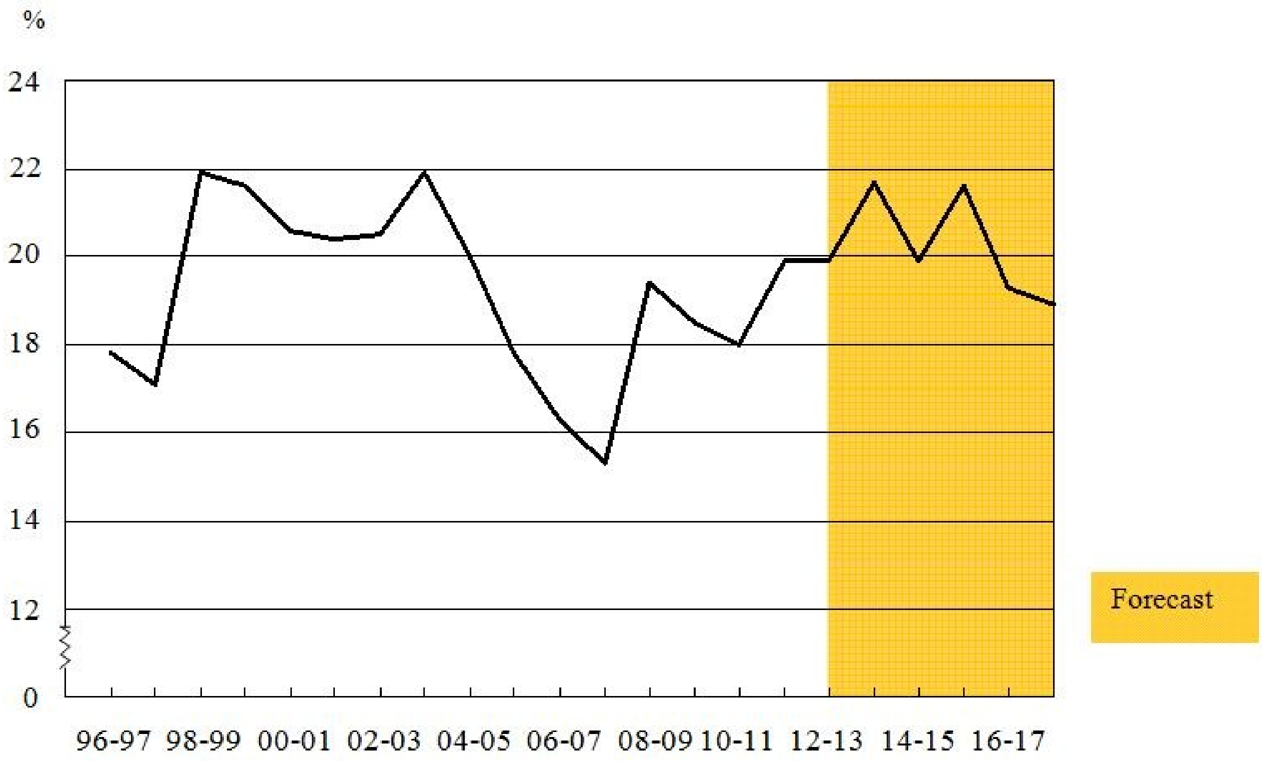
CONTENTS **Page**

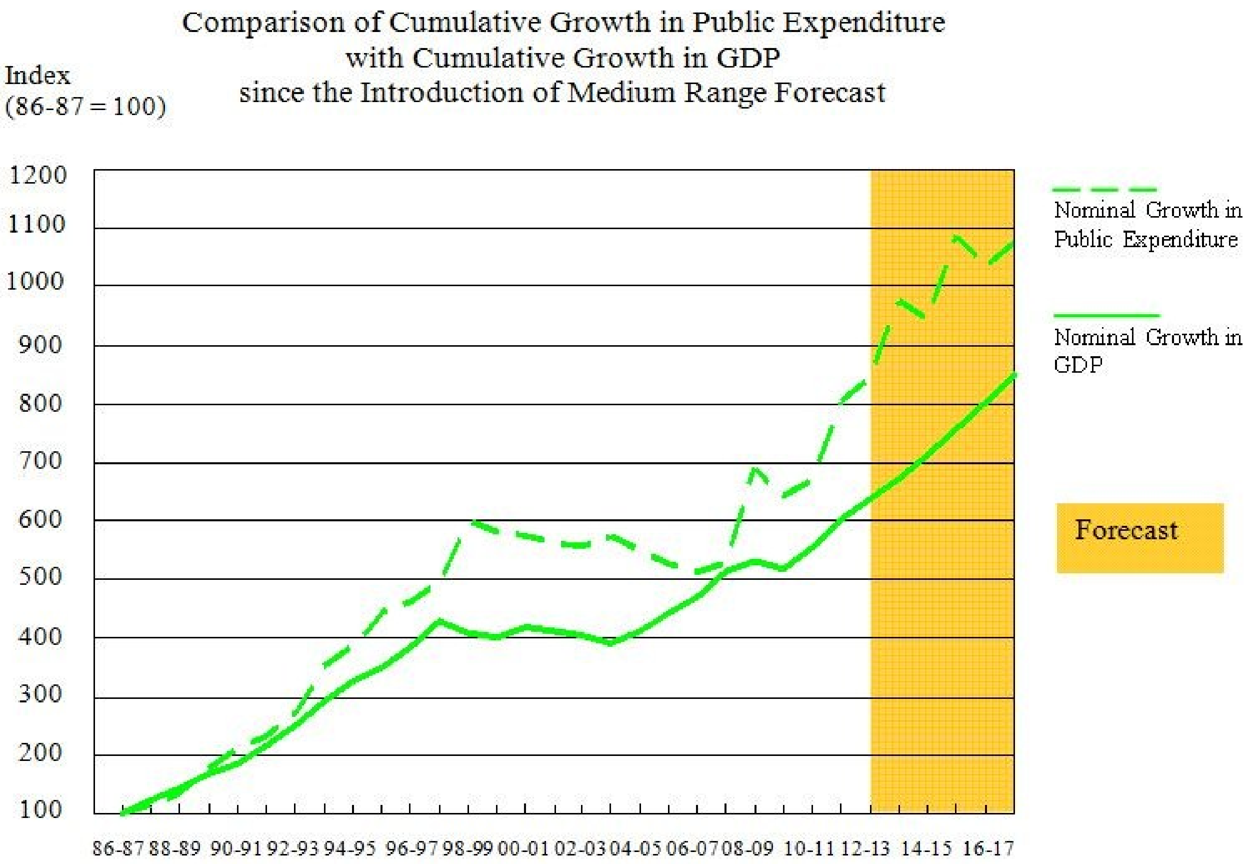
SECTION I THE ESTIMATES IN THE CONTEXT OF THE ECONOMY

Relationship between Government Expenditure, Public Expenditure and GDP

	2013–14 Estimate $m
General Revenue Account	
Operating	352,000
Capital	3,397
	355,397
Capital Investment Fund	865
Capital Works Reserve Fund	77,839
Innovation and Technology Fund	785
Loan Fund	3,808
Lotteries Fund	1,289
Government Expenditure	439,983
Trading Funds	5,152
Housing Authority	21,933
Public Expenditure	467,068
GDP	2,152,300
Public Expenditure in terms of percentage of GDP	21.7%

Public Expenditure in terms of Percentage of GDP





Comparison of Cumulative Growth in Public Expenditure
with Cumulative Growth in GDP
since the Introduction of Medium Range Forecast
Index
(86-87 = 100)
1200
1100
1000
900
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700
600
500
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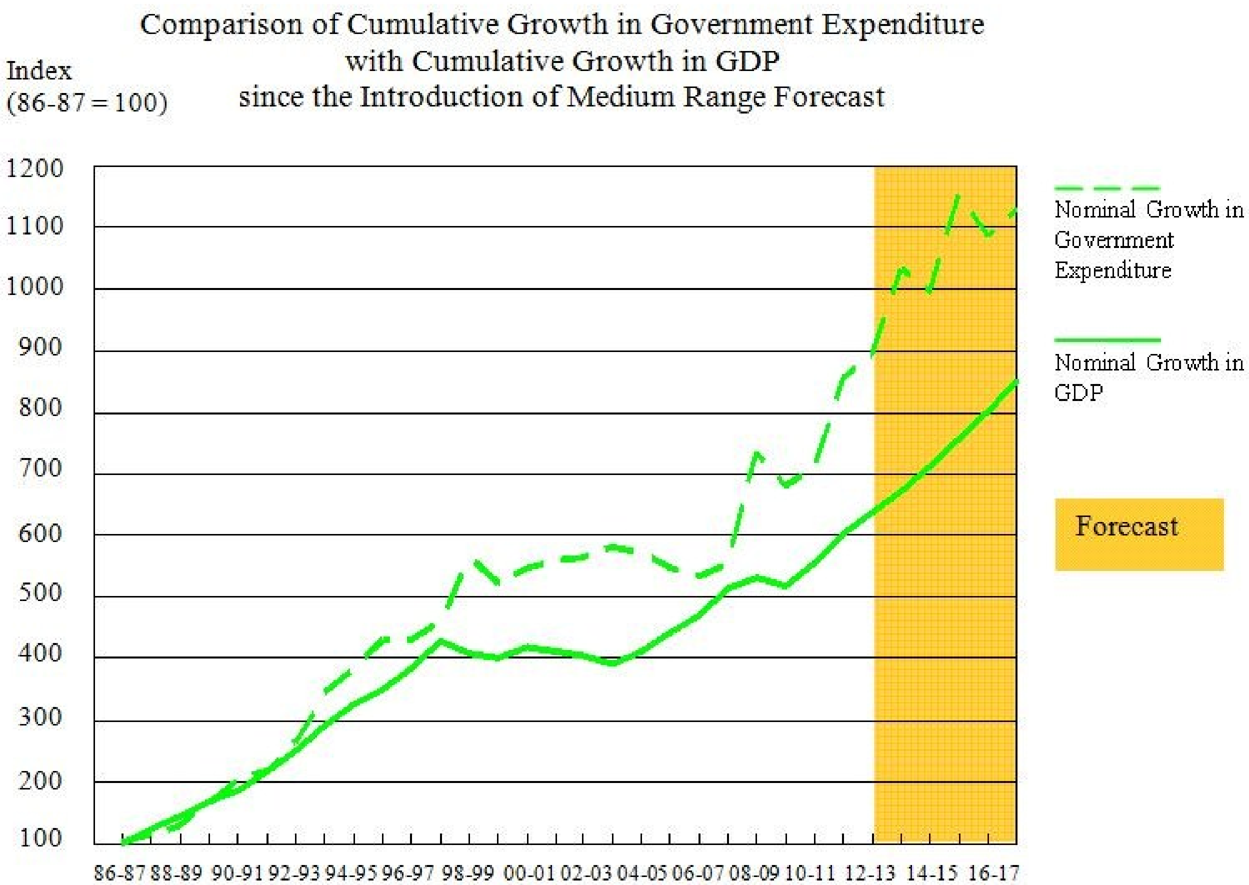
100
86-87 88-89 90-91 92-93 94-95 96-97 98-99 00-01 02-03 04-05 06-07 08-09 10-11 12-13 14-15 16-17
Nominal Growth in Public Expenditure
Nominal Growth in GDP
Forecast



Comparison of Cumulative Growth in Government Expenditure
with Cumulative Growth in GDP
since the Introduction of Medium Range Forecast
Index
(86-87 = 100)
1200
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86-87 88-89 90-91 92-93 94-95 96-97 98-99 00-01 02-03 04-05 06-07 08-09 10-11 12-13 14-15 16-17
Nominal Growth in Government Expenditure
Nominal Growth in GDP
Forecast

SECTION II ANALYSIS OF RECURRENT PUBLIC/GOVERNMENT EXPENDITURE BY POLICY AREA GROUP

Recurrent Public Expenditure : Year-on-Year Change

	2011–12 Actual $m	2012–13 Revised Estimate $m	**2013–14 Estimate $m**	**Increase/Decrease over 2012–13 Revised Estimate in Nominal Terms %**	**in Real Terms %**
Education	55,526	60,692	**62,953**	**3.7**	**2.9**
Social Welfare	40,333	42,694	**55,699**	**30.5**	**26.8**
Health	41,491	46,121	**48,765**	**5.7**	**4.9**
Security	29,341	31,184	**32,441**	**4.0**	**3.4**
Infrastructure	16,202	17,232	**18,049**	**4.7**	**2.5**
Economic	12,727	13,385	**14,345**	**7.2**	**4.9**
Housing	10,096	11,637	**12,362**	**6.2**	**2.3**
Environment and Food	10,422	11,144	**11,884**	**6.6**	**4.9**
Community and External Affairs	8,572	9,181	**9,728**	**6.0**	**4.1**
Support	32,442	36,591	**42,036**	**14.9**	**12.9**
	257,152	279,861	**308,262**	**10.1**	**8.4**

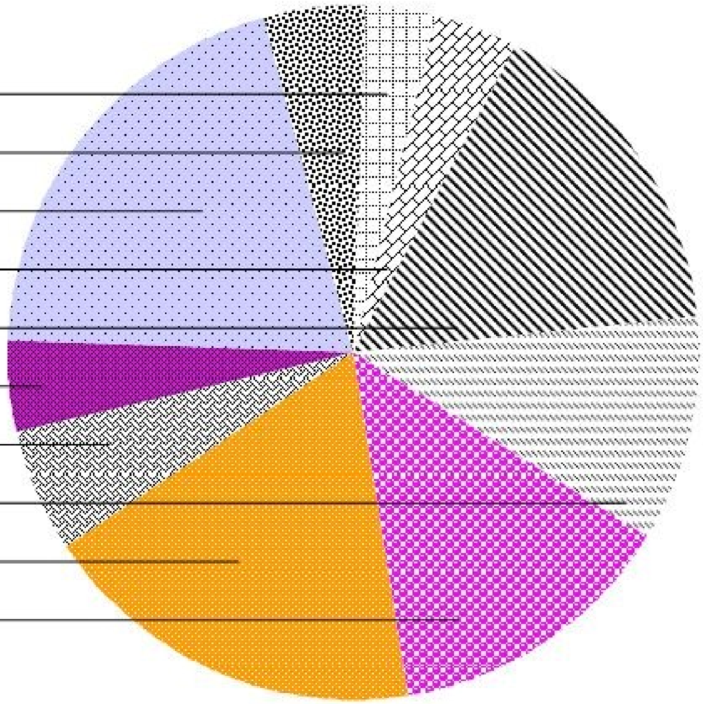
SECTION II ANALYSIS OF RECURRENT PUBLIC/GOVERNMENT EXPENDITURE BY POLICY AREA GROUP

Recurrent Government Expenditure : Year-on-Year Change

	2011–12 Actual $m	2012–13 Revised Estimate $m	**2013–14 Estimate $m**	**Increase/Decrease over 2012–13 Revised Estimate in Nominal Terms %**	**Increase/Decrease over 2012–13 Revised Estimate in Real Terms %**
Education	55,526	60,692	**62,953**	**3.7**	**2.9**
Social Welfare	40,333	42,694	**55,699**	**30.5**	**26.8**
Health	41,491	46,121	**48,765**	**5.7**	**4.9**
Security	29,341	31,184	**32,441**	**4.0**	**3.4**
Infrastructure	16,012	17,057	**17,856**	**4.7**	**2.5**
Economic	8,137	8,762	**9,632**	**9.9**	**8.5**
Housing	220	251	**288**	**14.7**	**14.5**
Environment and Food	10,422	11,144	**11,884**	**6.6**	**4.9**
Community and External Affairs	8,572	9,181	**9,728**	**6.0**	**4.1**
Support	32,442	36,591	**42,036**	**14.9**	**12.9**
	242,496	263,677	**291,282**	**10.5**	**8.9**

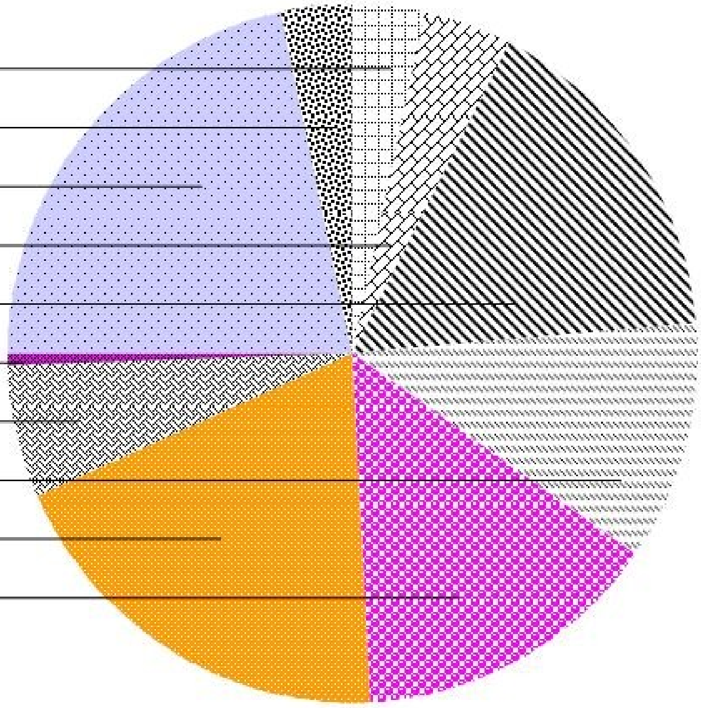
Percentage Share of Expenditure by Policy Area Group
Recurrent Public Expenditure : 2013-14 Estimate

Community and External Affairs	3.2%
Economic	4.7%
Education	20.4%
Environment and Food	3.9%
Health	15.8%
Housing	4.0%
Infrastructure	5.8%
Security	10.5%
Social Welfare	18.1%
Support	13.6%
	100.0%



Percentage Share of Expenditure by Policy Area Group
Recurrent Government Expenditure : 2013-14 Estimate

Community and External Affairs	3.4%
Economic	3.3%
Education	21.6%
Environment and Food	4.1%
Health	16.7%
Housing	0.1%
Infrastructure	6.1%
Security	11.1%
Social Welfare	19.1%
Support	14.5%
	100.0%



SECTION III ANALYSIS OF TOTAL PUBLIC/GOVERNMENT EXPENDITURE BY POLICY AREA GROUP

Total Public Expenditure : Year-on-Year Change

	2011–12 Actual $m	2012–13 Revised Estimate $m	**2013–14 Estimate $m**	**Increase/Decrease over 2012–13 Revised Estimate in Nominal Terms %**	**Increase/Decrease over 2012–13 Revised Estimate in Real Terms %**
Education	67,891	77,799	**76,884**	**-1.2**	**-2.2**
Social Welfare	43,346	45,940	**61,186**	**33.2**	**29.6**
Health	45,297	59,491	**53,732**	**-9.7**	**-10.6**
Security	31,522	33,732	**36,586**	**8.5**	**7.4**
Infrastructure	52,545	62,261	**76,144**	**22.3**	**16.7**
Economic	47,302	33,577	**40,106**	**19.4**	**17.8**
Housing	18,918	22,117	**24,501**	**10.8**	**6.2**
Environment and Food	17,733	19,206	**25,007**	**30.2**	**27.2**
Community and External Affairs	26,033	13,315	**28,451**	**113.7**	**111.1**
Support	35,054	38,089	**44,471**	**16.8**	**14.6**
	385,641	405,527	**467,068**	**15.2**	**12.7**

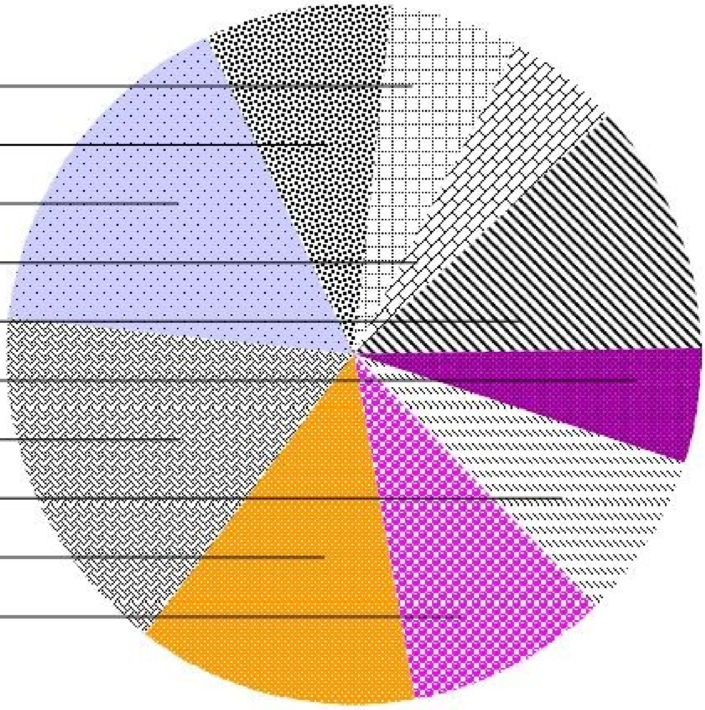
SECTION III ANALYSIS OF TOTAL PUBLIC/GOVERNMENT EXPENDITURE BY POLICY AREA GROUP

Total Government Expenditure : Year-on-Year Change

	2011–12 Actual $m	2012–13 Revised Estimate $m	**2013–14 Estimate $m**	**Increase/Decrease over 2012–13 Revised Estimate in Nominal Terms %**	**in Real Terms %**
Education	67,891	77,799	**76,884**	**-1.2**	**-2.2**
Social Welfare	43,346	45,940	**61,186**	**33.2**	**29.6**
Health	45,297	59,491	**53,732**	**-9.7**	**-10.6**
Security	31,522	33,732	**36,586**	**8.5**	**7.4**
Infrastructure	52,350	62,072	**75,930**	**22.3**	**16.7**
Economic	42,671	28,803	**35,168**	**22.1**	**20.8**
Housing	2,140	2,168	**2,568**	**18.5**	**18.4**
Environment and Food	17,733	19,206	**25,007**	**30.2**	**27.2**
Community and External Affairs	26,033	13,315	**28,451**	**113.7**	**111.1**
Support	35,054	38,089	**44,471**	**16.8**	**14.6**
	364,037	380,615	**439,983**	**15.6**	**13.2**

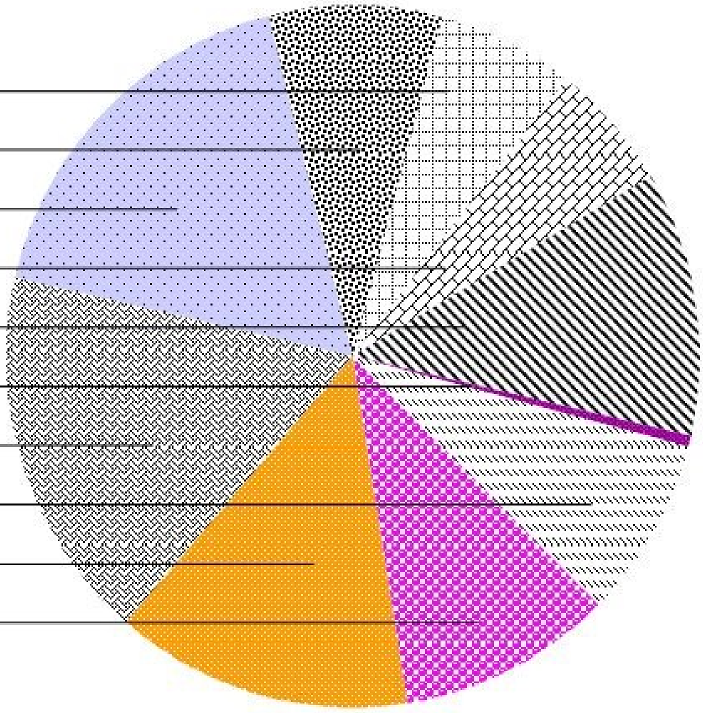
Percentage Share of Expenditure by Policy Area Group
Total Public Expenditure : 2013-14 Estimate

Community and External Affairs	6.1%
Economic	8.6%
Education	16.5%
Environment and Food	5.4%
Health	11.5%
Housing	5.2%
Infrastructure	16.3%
Security	7.8%
Social Welfare	13.1%
Support	9.5%
	100.0%



Percentage Share of Expenditure by Policy Area Group
Total Government Expenditure : 2013-14 Estimate

Community and External Affairs	6.5%
Economic	8.0%
Education	17.5%
Environment and Food	5.7%
Health	12.2%
Housing	0.6%
Infrastructure	17.2%
Security	8.3%
Social Welfare	13.9%
Support	10.1%
	100.0%



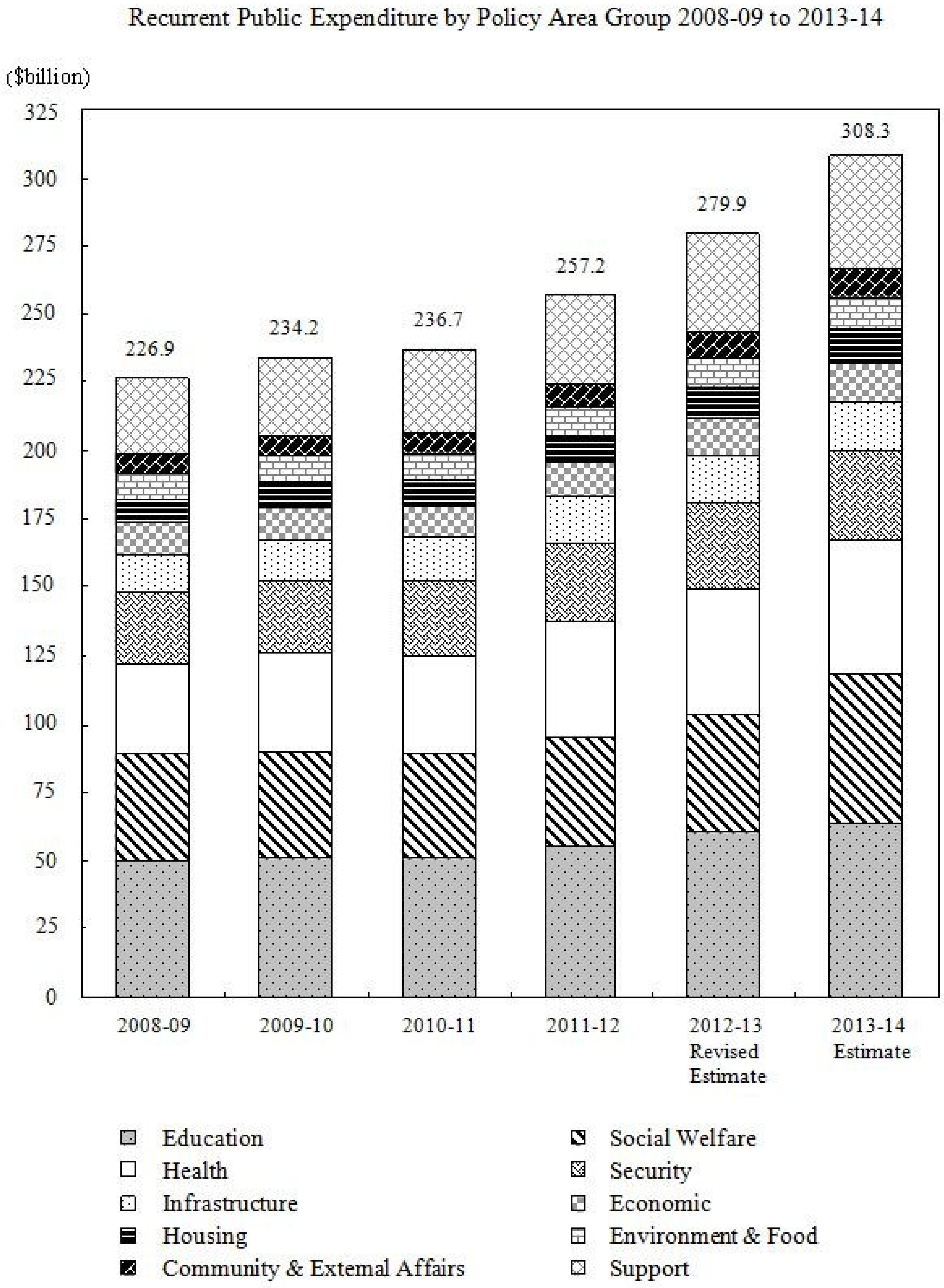
SECTION IV MAJOR CAPITAL PROJECTS ESTIMATED TO BEGIN IN 2013-14

Major capital projects estimated to begin in 2013-14 include –

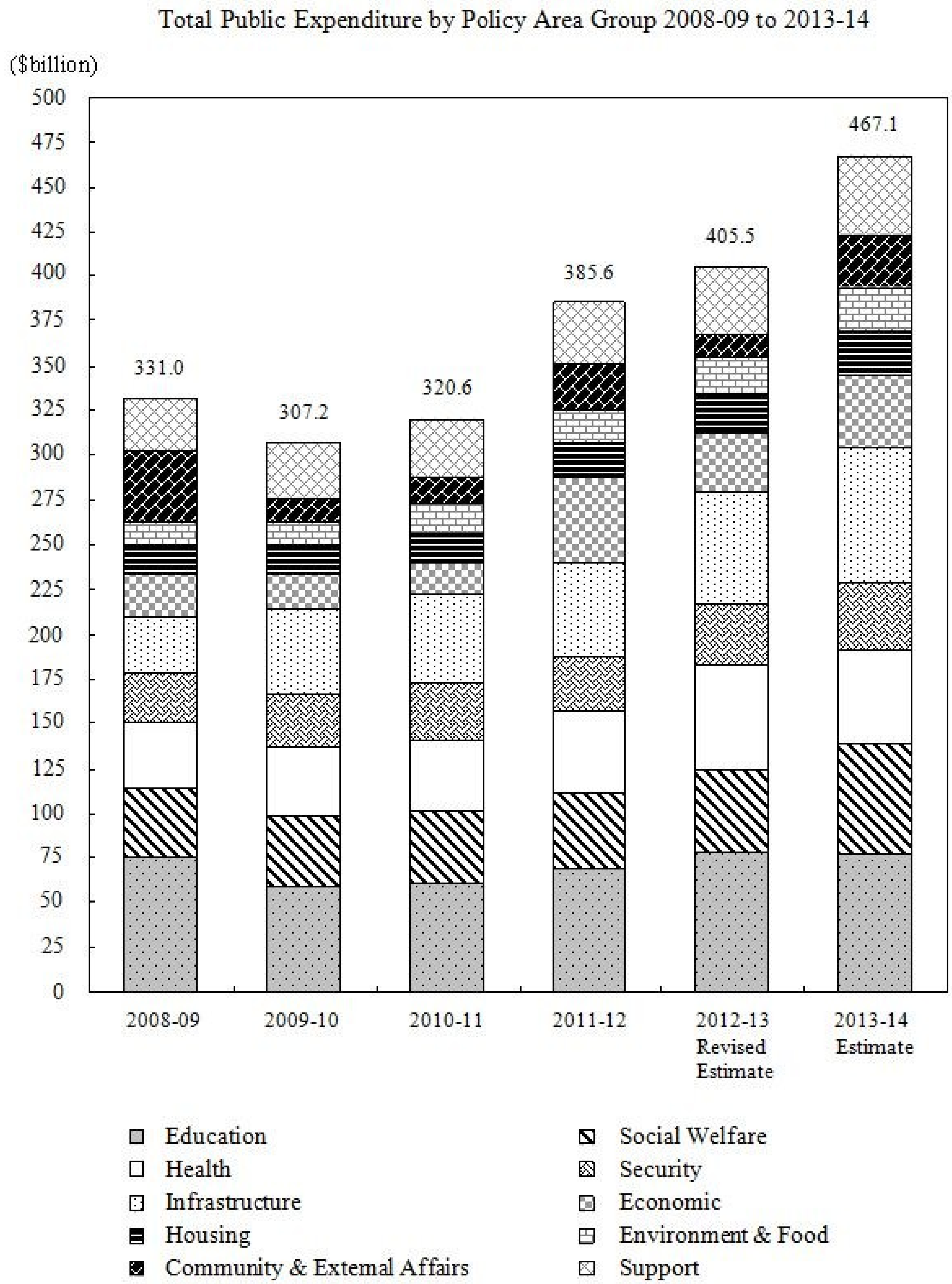
	Project Estimates $ million
Infrastructure	**54,570**
— Construction of additional floors on Central Piers Nos. 4, 5 and 6	
— Improvement of fresh water supply to Cheung Chau	
— Infrastructure works for housing sites adjacent to Lung Ping Road at Tai Wo Ping, Shek Kip Mei	
— Kai Tak development—stages 3A and 4 infrastructure at north apron area of Kai Tak Airport	
— Kwun Tong Town Centre redevelopment—provision of grade-separated pedestrian linkages (Yuet Wah Street Pedestrian Linkage)	
— Liantang/Heung Yuen Wai Boundary Control Point and associated works—regulation of Shenzhen River stage 4	
— Public transport interchange at Area 13, Hung Shui Kiu	
— Reconstruction and rehabilitation of Kai Tak nullah from Tung Kwong Road to Prince Edward Road East	
— Site formation and associated infrastructural works for development of columbarium, crematorium and related facilities at Sandy Ridge Cemetery—detailed design and site investigation	
— Tseung Kwan O–Lam Tin Tunnel—detailed design and site investigation	
— Tuen Mun–Chek Lap Kok Link—construction works	
— Water supply to Pak Shek Kok reclamation area, Tai Po—stage 2	
— Widening of Tolo Highway/Fanling Highway between Island House Interchange and Fanling—stage 2	
Health	**16,104**
— Establishment of Centre of Excellence in Paediatrics	
— Government, Institution or Community facilities in the Kwun Tong Town Centre redevelopment—additional medical and health facilities	
— Refurbishment of Hong Kong Buddhist Hospital	
— Reprovisioning of Yaumatei Specialist Clinic at Queen Elizabeth Hospital	
— Ward renovation in Kwai Chung Hospital	
Security	**2,535**
— Relocation of part of the offices of the Department of Justice to the Main and East Wings of the Former Central Government Offices	
— Relocation of the Court of Final Appeal and the Development Office of the Judiciary to No. 8 Jackson Road	
— Reprovisioning of Yau Ma Tei Police Station	
Education	**1,672**
— A 30-classroom primary school at Site 1A-3, Kai Tak Development, Kowloon	
— A 30-classroom primary school at Site 1A-4, Kai Tak Development, Kowloon	
— Development of the Vocational Training Council International Culinary College	
— Redevelopment of Tung Wah Group of Hospitals Wong Fut Nam College at Oxford Road, Kowloon	

	Project Estimates $ million
Community and External Affairs	**1,661**
— Cycle tracks connecting North West New Territories with North East New Territories—Tuen Mun to Sheung Shui section (Stage 1)	
— Improvement works at Mui Wo, phase 1	
— Lei Yue Mun Waterfront Enhancement Project—construction of a public landing facility	
— Lei Yue Mun Waterfront Enhancement Project—development of a waterfront promenade and related improvement works	
— Reprovisioning of Shanghai Street refuse collection point and street sleepers' services units to the site at Hau Cheung Street, Yau Ma Tei for the phase II development of the Yau Ma Tei Theatre project	
— Sports centre in Area 4, Tsing Yi	
Environment and Food	**1,169**
— Outlying Islands sewerage, stage 2—Lamma village sewerage phase 2, package 1	
— Outlying Islands sewerage, stage 2—Peng Chau village sewerage phase 2	
— Sewerage in Nam Wa Po and Wai Tau	
— Tolo Harbour sewerage of unsewered areas, stage 2—phase 1	
— West New Territories landfill extension—consultants' fees and investigations	
Economic	**488**
— Providing sufficient water depth for Kwai Tsing Container Basin and its approach channel	
Support	**370**
— Relocation of the printing workshop of Government Logistics Department	

SECTION V TRENDS IN PUBLIC EXPENDITURE : 2008-09 TO 2013-14

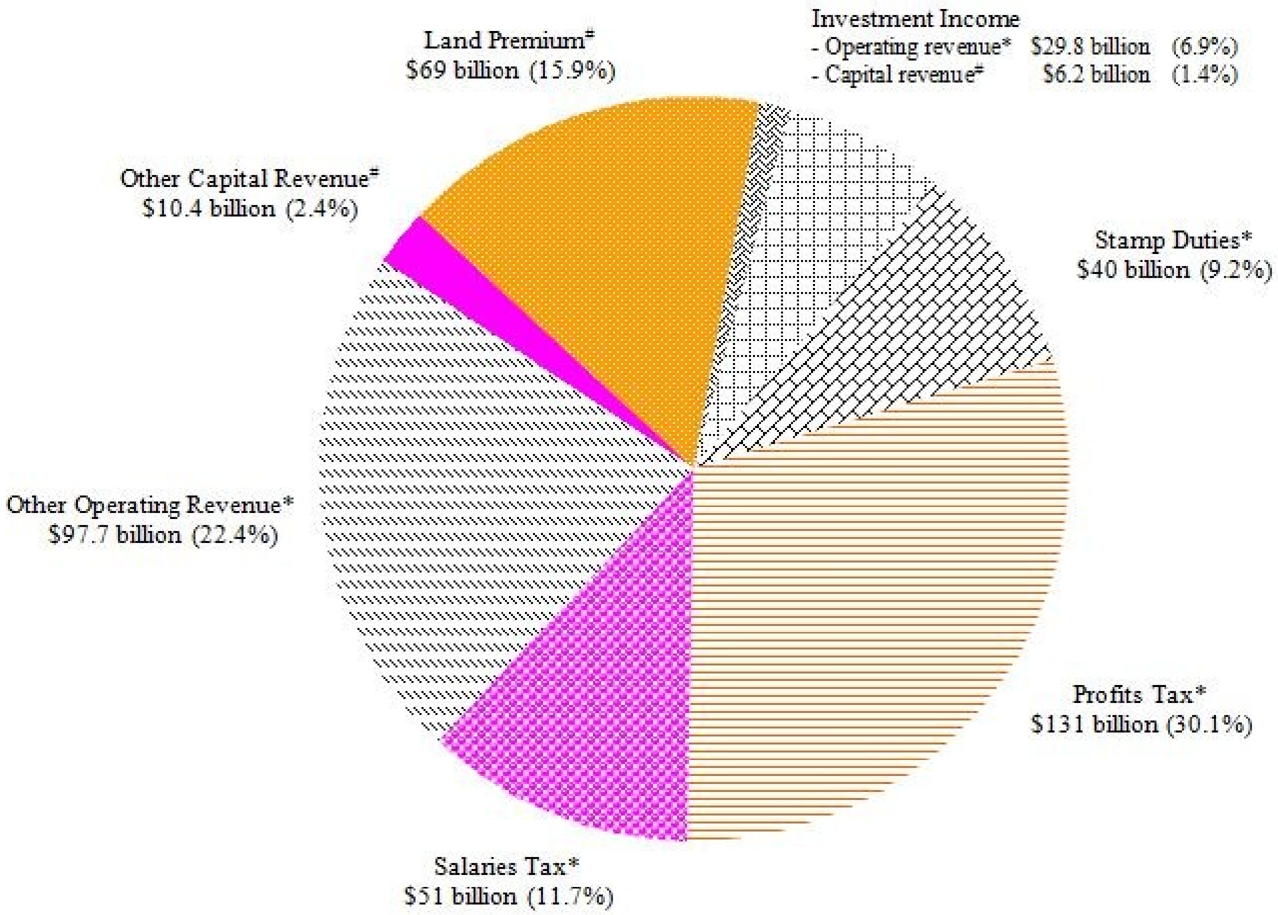


SECTION V TRENDS IN PUBLIC EXPENDITURE : 2008-09 TO 2013-14



SECTION VI ANALYSIS OF GOVERNMENT REVENUE

2013-14 Estimate ($435.1 billion)



*	Operating Revenue	$349.5 billion	(80.3%)
#	Capital Revenue	$85.6 billion	(19.7%)

SECTION VII CLASSIFICATION OF EXPENDITURE BY POLICY AREA GROUP

Policy Area Group	**Policy Area** (*Note*)	
Community and External Affairs	19	District and Community Relations
	18	Recreation, Culture, Amenities and Entertainment Licensing
Economic	3	Air and Sea Communications and Logistics Development
	6	Commerce and Industry
	8	Employment and Labour
	1	Financial Services
	17	Information Technology and Broadcasting
	34	Manpower Development
	4	Posts, Competition Policy and Consumer Protection
	7	Public Safety
	5	Travel and Tourism
Education	16	Education
Environment and Food	2	Agriculture, Fisheries and Food Safety
	32	Environmental Hygiene
	23	Environmental Protection, Conservation, Power and Sustainable Development
Health	15	Health
Housing	31	Housing
Infrastructure	22	Buildings, Lands, Planning, Heritage Conservation, Greening and Landscape
	21	Land and Waterborne Transport
	24	Water Supply, Drainage and Slope Safety
Security	12	Administration of Justice
	13	Anti-corruption
	10	Immigration Control
	9	Internal Security
	11	Legal Administration
	20	Legal Aid
Social Welfare	14	Social Welfare
	33	Women's Interests
Support	26	Central Management of the Civil Service
	30	Complaints Against Maladministration
	28	Constitutional and Mainland Affairs
	27	Intra-Governmental Services
	25	Revenue Collection and Financial Control
	29	Support for Members of the Legislative Council

Note: Details of individual heads of expenditure contributing to a particular policy area are provided in an index in Volume I of the 2013-14 Estimates. The index further provides details, by head of expenditure, of individual programmes which contribute to a policy area.

APPENDIX C

GLOSSARY OF TERMS

GLOSSARY OF TERMS

Note: Terms shown in ***bold italic*** are defined elsewhere in the glossary.

Capital expenditure. This comprises all expenditure charged to the Capital Account of the General Revenue Account, Capital Investment Fund, Capital Works Reserve Fund (including interest on government bonds and notes but excluding repayment of the bonds and notes), Disaster Relief Fund, Innovation and Technology Fund, Loan Fund and Lotteries Fund. Major items are highlighted below –

General Revenue Account

equipment, works and capital subventions of a minor nature

Capital Investment Fund

advances and equity investments

Capital Works Reserve Fund

acquisition of land
capital subventions
computerisation
interest and other expenses on government bonds and notes issued in 2004
major systems and equipment
Public Works Programme expenditure

Disaster Relief Fund

relief to disasters that occur outside Hong Kong

Innovation and Technology Fund

projects promoting innovation and technology upgrading in manufacturing and service industries

Loan Fund

loans made under various development schemes supported by the Government
loans to schools, teachers, students, and housing loans to civil servants, etc.

Lotteries Fund

grants, loans and advances for social welfare services

Capital surplus/deficit. The difference between ***capital revenue*** and ***capital expenditure***.

Capital revenue. This comprises certain revenue items in the General Revenue Account and all receipts credited to seven Funds, as highlighted below –

General Revenue Account

disposal proceeds of government quarters and other assets
estate duty
loan repayments received
recovery from Housing Authority

Capital Investment Fund

dividends from investments
interest on loans
investment income
loan repayments received
proceeds from sale of investments

Capital Works Reserve Fund

investment income
land premium
recovery from MTR Corporation Limited

Civil Service Pension Reserve Fund

investment income

Disaster Relief Fund

investment income

Innovation and Technology Fund

investment income
loan repayments received
proceeds from sale of investments

Loan Fund

interest on loans
investment income
loan repayments received
proceeds from sale of loans

Lotteries Fund

auctions of vehicle registration numbers
investment income
loan repayments received
share of proceeds from the Mark Six Lottery

Consolidated surplus/deficit before repayment of bonds and notes. The difference between ***government revenue*** and ***government expenditure***.

Fiscal reserves. The accumulated balances of the General Revenue Account, Capital Investment Fund, Capital Works Reserve Fund, Civil Service Pension Reserve Fund, Disaster Relief Fund, Innovation and Technology Fund, Land Fund, Loan Fund and Lotteries Fund.

Government expenditure. The aggregate of ***operating expenditure*** and ***capital expenditure***. Unlike ***public expenditure***, it excludes expenditure by the Trading Funds and the Housing Authority.

Government revenue. The aggregate of ***operating revenue*** and ***capital revenue.***

Operating expenditure. All expenditure charged to the Operating Account of the General Revenue Account.

Operating revenue. This comprises all revenue credited to the General Revenue Account (except those items which are treated as ***capital revenue***) and the Land Fund, as highlighted below –

General Revenue Account

duties
fines, forfeitures and penalties
investment income
rents and rates
royalties and concessions
taxes
utilities, fees and charges

Land Fund

investment income

Operating surplus/deficit. The difference between ***operating revenue*** and ***operating expenditure***.

Public expenditure. ***Government expenditure*** plus expenditure (operating and capital) by the Trading Funds and the Housing Authority.

Transfer to Funds. Transfers between the General Revenue Account and the eight Funds (Capital Investment Fund, Capital Works Reserve Fund, Civil Service Pension Reserve Fund, Disaster Relief Fund, Innovation and Technology Fund, Land Fund, Loan Fund and Lotteries Fund) are not counted as government revenue and expenditure as these are merely internal transfers within Government's accounts.