Research Brief

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The 2024-2025 Budget

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Hong Kong's fiscal deficit is forecast to reduce by more than half to HK$48.1 billion in 2024-2025 due to a restrained increase in budgeted government expenditure, along with introduction of several targeted new tax initiatives and an increase in bond issuance to bolster government coffers.

The 2024-2025 Budget further pledges fiscal consolidation to progressively restore fiscal balance in a few years' time. Many developed places, such as the United Kingdom, Canada and Singapore, have been implementing similar initiatives on a wider scope: (a) on the expenditure side, they are seeking efficiency savings in the public sector, re-prioritizing and enabling more focused government spending, as well as explicitly capping government debts/borrowings and/or welfare spending; and (b) on revenue enhancement, they are promoting economic growth to boost tax revenue, introducing new taxes (e.g. "wealth tax") to expand the revenue base, and/or raising the tax rates on existing taxes.

Another key highlight of this year's Budget is the further expansion in bond issuance to fund green/sustainable and infrastructure projects. Hong Kong's comparatively low government debt-to-Gross Domestic Product ratio should afford the fiscal leeway facilitating this initiative.

Land premium used to be a major revenue source for the Government before the COVID-19 pandemic. The lower revenue from land premium forecast in this year's Budget as well as realized in the previous financial year, along with the prevailing uncertainties in the property market, have recently reignited the discussions about broadening Hong Kong's tax base. Nevertheless, each proposed tax option comes with its own trade-offs that warrant thorough consideration when introducing a new tax.

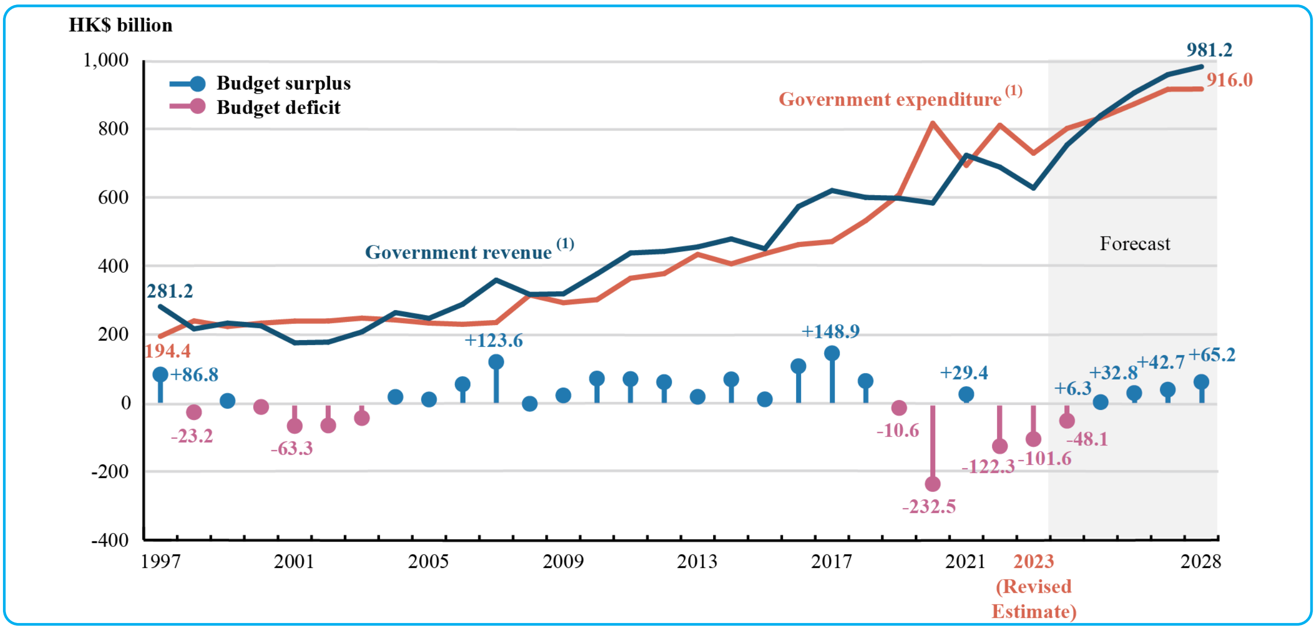
The Legislative Council will resume the Second Reading debate on the Appropriation Bill 2024 at its meeting of 24 April 2024.

1. Introduction

1.1 The Financial Secretary delivered the second Budget of the current-term Government on 28 February 2024. The revised estimate of fiscal deficit for 2023-2024 was HK$101.6 billion (**Figure 1**), which was equivalent to 3.4% of the Gross Domestic Product ("GDP") and substantially higher than the HK$54.4 billion forecast put forward in February 2023. The larger-than-expected fiscal deficit was mostly due to a marked shortfall in total government revenue, which more than offset the savings from the retrenchment of government expenditure after the COVID-19 pandemic.[1] In 2023-2024, total government revenue only amounted to HK$554.6 billion, which was 13.7% lower than the original estimate of HK$642.4 billion. While the revenue from salaries and profits taxes generally met expectations, there was a noticeable deficiency in revenue from land premium and stamp duties. The revised estimate on the combined revenue from the latter two for 2023-2024 (at HK$69.4 billion) was more than HK$100 billion below the forecast made in February last year (HK$170.0 billion).

[1] Revised estimate of total government expenditure for 2023-2024 amounted to HK$727.9 billion, which was 4.3% lower than the original estimate and 10.2% less than the figure for 2022-2023. For total public expenditure, which includes expenditure by the Housing Authority and the Trading Funds, the figure for 2023-2024 was HK$770.4 billion, 4.9% lower than the original estimate and 9.1% less than the preceding financial year.

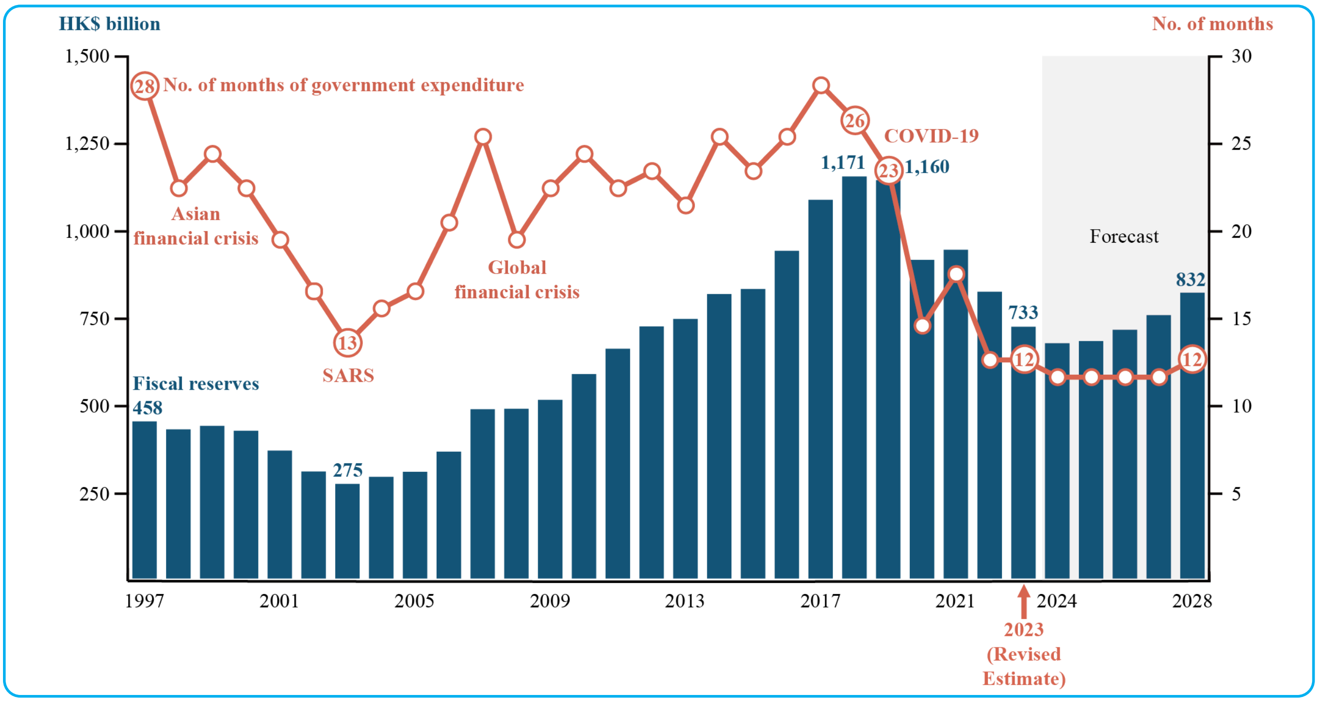
Figure 1 – Government's fiscal position, 1997-1998 to 2028-2029



Note: (1) Including issuance/repayment of government bonds and notes.
Sources: Budget speech (various years) and Financial Services and the Treasury Bureau.

1.2 Hong Kong has now seen deficits in four of the five financial years since 2019-2020, with a surplus of HK$29.4 billion in 2021-2022 being the lone exception. This setback has resulted in a significant depletion of fiscal reserves from the peak of HK$1.171 trillion at end-March 2019 to HK$733.2 billion at end-March 2024 (**Figure 2**), amounting to some 37.4% decrease or HK$437.7 billion over the same period. Mirroring this trend, the fiscal reserves when measured in terms of the number of months of government expenditure also declined from 26 months to 12 months.

Figure 2 – Fiscal reserves of the Government, 1997-1998 to 2028-2029



Sources: Budget speech (various years) and Financial Services and the Treasury Bureau.

1.3 In the face of pressure on public finances, the 2024-2025 Budget holds back from offering generous tax concessions and handouts that characterized recent years' Budgets. This year's Budget also introduces a number of policy initiatives designed to boost Hong Kong's economic strength and fiscal stability. Key among these initiatives include (a) a fiscal consolidation strategy aimed at achieving fiscal balance in a few years' time; (b) the issuance of bonds to finance green/sustainable and infrastructure projects; and (c) the removal of all demand-side management measures for residential properties. This Research Brief will study these policy initiatives in detail after reviewing the Government's fiscal position for 2024-2025.

2. Government revenue and expenditure initiatives for 2024-2025

2.1 While the 2024-2025 Budget remains expansionary, the Financial Secretary forecasts a more than halving of the fiscal deficit to HK$48.1 billion (1.5% of GDP), from the estimated HK$101.6 billion (3.4%) for 2023-2024. This fiscal consolidation reflects the Government's effort to identify new revenue and funding sources (including the issuance of bonds) while controlling the growth of total government expenditure.

<u>Revenue initiatives</u>

2.2 Total government revenue is expected to increase by 14.1% in 2024-2025 to HK$633.0 billion, reversing the decline of 10.9% in 2023-2024 (**Figure 3**). The Government's revenue projection is based on continued significant contributions from salaries tax, profits tax, investment income and stamp duties to the government coffers, which will together account for 67.7% of total government revenue in 2024-2025. Individually, profits tax will contribute the most at 28.5%, followed by investment income (14.2%), salaries tax (13.8%) and stamp duties (11.2%).[2] Previously a major revenue source[3], land premium is now projected to contribute a mere HK$33.0 billion, or 5.2%, to total government revenue in 2024-2025, probably reflecting the Government's latest views regarding the composition of its key revenue sources.

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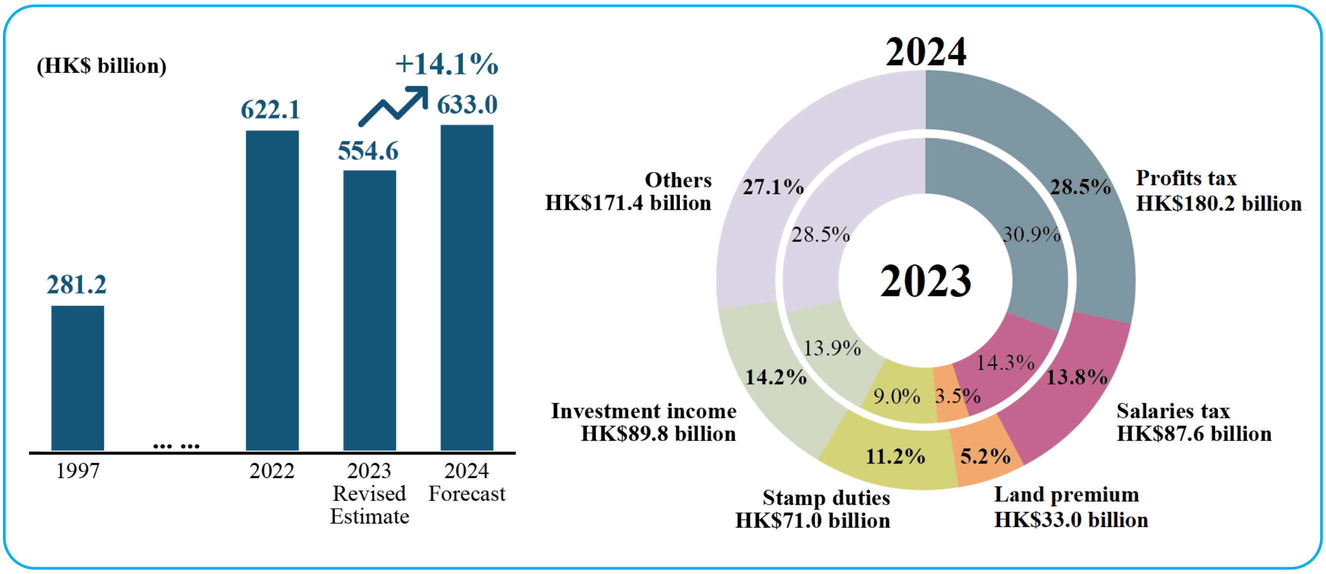
2 The Government forecasts the Hong Kong economy to grow further by 2.5% to 3.5% in 2024, after having resumed growth of 3.2% in 2023. The projection, which aligns with the average forecast of 2.7% by private sector analysts, should bode well for the potential increase in tax revenue.

3 Until 2021-2022, land premium consistently ranked among the four largest revenue sources of the Government. It was even the top contributor in 2017-2018, accounting for 26.6% of total government revenue for that year.

Figure 3 – Total government revenue and its major sources, 1997-1998 to 2024-2025(1)



Note: (1) Figures might not add up to the total due to rounding.
Sources: Budget speech (various years) and Financial Services and the Treasury Bureau.

2.3 In the 2024-2025 Budget, the Financial Secretary announced targeted new tax measures intended to strengthen government revenue without increasing tax burdens on the general public. More specifically: (a) high-income earners will, for the first time, be subject to a two-tiered standard rates regime for salaries tax and tax under personal assessment;[4] (b) legislative amendments will be introduced in the first half of 2024 to implement a progressive rating system for domestic properties with a higher rateable value;[5] and (c) hotel accommodation tax ("HAT"), which had been waived since 1 July 2008, will be reinstated at a rate of 3% on accommodation charges.[6] These three measures will together bring about more than HK$2.8 billion of additional revenue per year, according to the Government's estimate.[7]

4 For taxpayers whose net income exceeds HK$5 million a year, the first HK$5 million of their net income will be taxed at 15% and the excess at 16% under the new proposal. The new tax measure is expected to bring in some HK$910 million extra revenue for the Government each year.

5 The new rating system will affect those domestic properties with a rateable value over HK$550,000. While rates will remain to be charged at 5% of the rateable value on the first HK$550,000, the rates percentage charge will be raised to 8% on the next HK$250,000, and further to 12% on the portion of exceeding HK$800,000. The new system will contribute HK$840 million annually to the government coffers.

6 Arising from HAT, it is forecast that government revenue will increase by about HK$1.1 billion per year. HAT will take effect from 1 January 2025, in order to allow the hotel and tourism industries more time for preparation.

7 Other revenue-raising measures include increasing the business registration fees by HK$200 and the duty rate on tobacco products.

2.4 In a further effort to boost government revenue, the Financial Secretary has proposed in the 2024-2025 Budget to seek the approval from the Legislative Council to bring back the accumulated investment return of the Future Fund into the Operating Account.[8] The Budget also reveals the issuance of HK$120.0 billion worth of silver, green and infrastructure bonds in 2024-2025, of which HK$24.2 billion will be earmarked for repayment of bonds previously issued. The net bond proceeds will significantly reduce the consolidated fiscal deficit to HK$48.1 billion. Without the bond issuance, the consolidated fiscal deficit before issuance and repayment of bonds for 2024-2025 would have amounted to HK$143.8 billion[9] or some HK$95.8 billion higher than would otherwise be possible.

2.5 The 2024-2025 Budget also outlines the Government's plan to tap into bond issuance as a new funding source in the years ahead, which should help reduce the consolidated fiscal deficit sooner. The bond programmes are expected to yield HK$135.0 billion in proceeds for 2025-2026, thereby setting the stage for Hong Kong's earlier return to a consolidated budget surplus by that year (of HK$6.3 billion).[10] As the bond programmes continue, the consolidated budget surplus is set to increase to HK$32.8 billion in 2026-2027 and further to HK$42.7 billion in 2027-2028 and HK$65.2 billion by 2028-2029.

<u>Expenditure initiatives</u>

2.6 In 2024-2025, total government expenditure is forecast to increase by 6.7% to HK$776.9 billion,[11] with a slight rebound in its ratio to GDP to 24.6%.[12] Of the total, recurrent expenditure is set to grow by 7.0% to HK$580.2 billion,[13] with continued substantial resources allocated to livelihood-related policy areas like health, social welfare and education. These three policy areas will together account for a combined share of 59.2%.

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[8] The Future Fund, set up in 2016, comprises an initial endowment from the Land Fund and periodic top-up from budget surpluses. The Future Fund, together with investment return not received and compounded on an annual basis, is retained within the Exchange Fund until 31 December 2030 or upon decision of the Financial Secretary for withdrawal, whichever is the earlier.

[9] For 2023-2024, the revised estimate for consolidated fiscal deficit before issuance and repayment of bonds was HK$173.3 billion.

[10] Absent the bond programmes, the consolidated fiscal deficit before issuance and repayment of bonds will continue until 2026-2027. However, a turnaround is expected in 2027-2028, with a forecast consolidated budget surplus of HK$14.1 billion.

[11] Government expenditure is the aggregate of operating expenditure and capital expenditure. Both recurrent and non-recurrent expenditure items are charged to the operating account.

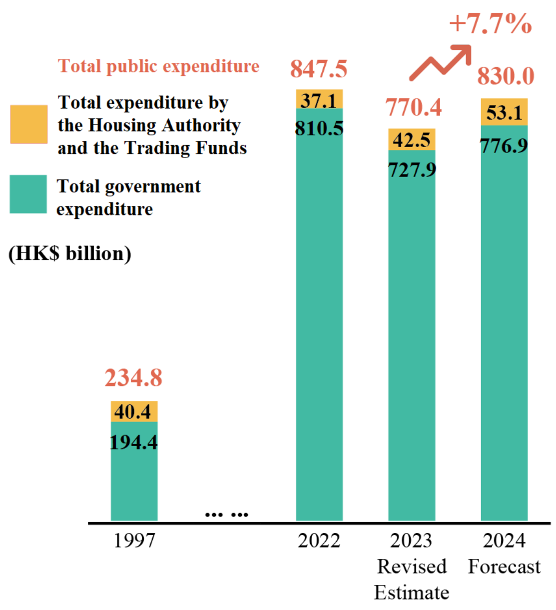
[12] The ratio stood at 24.3% in 2023-2024, followed a high of 28.9% in the preceding year when the Government incurred hefty expenditure in the implementation of massive counter-cyclical measures and anti-epidemic work.

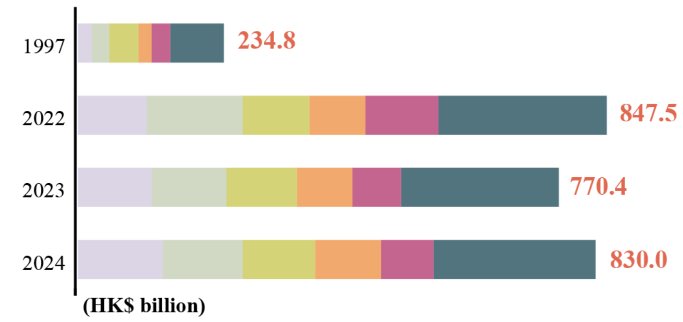
[13] Growth of recurrent expenditure will slow to between 3.0% and 4.3% per year in the following four financial years, according to the Government's projection.

2.7 On the other hand, non-recurrent expenditure is projected to decrease markedly by 47.7% to HK$33.6 billion in 2024-2025 due to reduced needs for pandemic-related spending.[14] Notably, the amount budgeted for one-off relief measures will amount to HK$11.5 billion, representing an 80.6% plunge from the previous year's budgeted HK$59.4 billion. This cutback can be attributable to: (a) the cessation of electricity subsidies; (b) the discontinuation of consumption voucher scheme; and (c) the scale-back of property rate concessions (covering one quarter instead of the two quarters provided last year). Furthermore, taxpayers will receive a 100% salaries tax/profits tax deduction that is capped at HK$3,000 per case, which is only half of last year's ceiling of HK$6,000.

2.8 Public expenditure includes government expenditure and expenditure by the Housing Authority and the Trading Funds. In 2024-2025, public expenditure will increase by 7.7% to HK$830.0 billion (**Figure 4**). Expenditure initiatives of the top four expenditure items by policy area, namely social welfare, health, education and infrastructure, are detailed in the paragraphs below.

Figure 4 – Total public expenditure and its major components, 1997-1998 to 2024-2025[(1)]





	1997	2022	2023	2024
Social welfare	9.1%	13.0%	15.3%	16.4%
Health	11.9%	18.1%	15.6%	15.4%
Education	20.3%	12.6%	14.7%	13.9%
Infrastructure	10.1%	10.6%	11.5%	12.8%
Support	11.8%	13.8%	10.1%	10.1%
Others[(2)]	36.8%	31.9%	32.8%	31.4%
Total amount (HK$ billion)	**234.8**	**847.5**	**770.4**	**830.0**

Notes: (1) Figures might not add up to the total due to rounding.
(2) Others include the following policy areas: (a) Security; (b) Environment and Food; (c) Economic; (d) Housing; and (e) Community and External Affairs.

Sources: Budget speech (various years) and Financial Services and the Treasury Bureau.

[14] As mentioned in footnote 11 above, government expenditure includes operating expenditure (i.e. recurrent and non-recurrent expenditure) and capital expenditure. Capital expenditure is projected to reach HK$163.1 billion in 2024-2025; revised estimate on capital expenditure in 2023-2024, meanwhile, was HK$121.6 billion.

Social welfare

2.9 Expenditure on social welfare is expected to represent the largest share of total public expenditure in 2024-2025, receiving HK$136.2 billion or 16.4% of the budget. This represents an increase from HK$117.8 billion in 2023-2024, or a 15.7% expansion (**Figure 5**). As an important programme of the Social Welfare Department ("SWD"), social security will account for a substantial portion of SWD's financial provisions, at 68.2% or HK$82.0 billion. Within this total, the Social Security Allowance Scheme is poised to see significant growth in expenditure between 2019-2020 and 2024-2025, with a 56.2% increase to HK$57.2 billion. The surge reflects the large number of cases to be served during the period, which is expected to increase by 35.5% to reach a high of 1.5 million cases by 2024-2025.

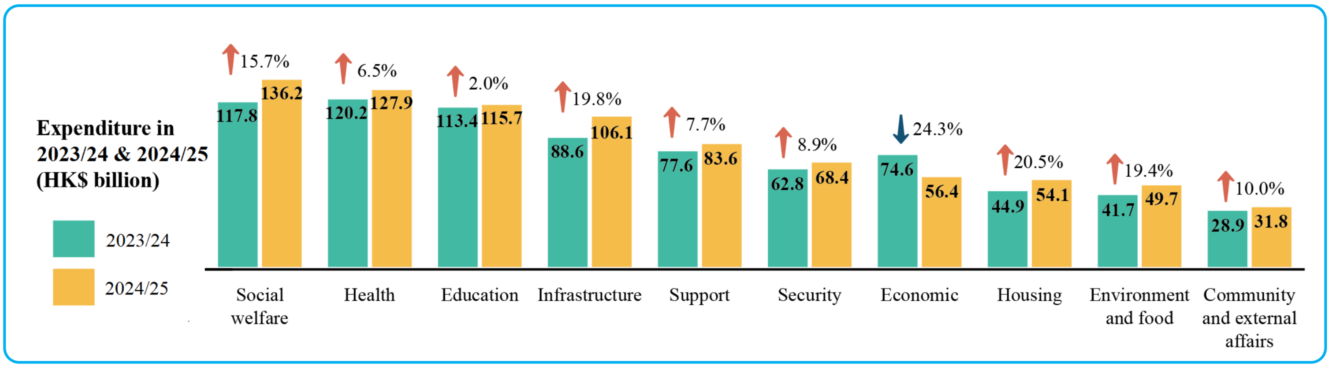
Health

2.10 Health expenditure for 2024-2025 is expected to reach HK$127.9 billion, with its share in total public expenditure edging down slightly to 15.4% despite a 6.5% increase in funding from the preceding year. This continues the easing trend from the previous year when the corresponding share decreased to 15.6% from 18.1% in 2022-2023. Meanwhile, recurrent health expenditure for 2024-2025 is forecast to increase by 4.6% from the previous year, reaching HK$109.5 billion to account for 18.1% of the total. A substantial portion of health expenditure is related to the delivery of public health services by the Hospital Authority ("HA"). The annual subvention for HA is forecast to increase by a modest 2.2% to HK$95.4 billion in 2024-2025.

Education

2.11 Education expenditure for 2024-2025 is estimated at HK$115.7 billion. This represents a modest increase of 2.0% over 2023-2024, which is one of the lowest growth rates among all policy areas. As a result, the share of education expenditure in total public expenditure will ease to 13.9% from 14.7% in the previous year.

Figure 5 – Year-on-year growth rate of total public expenditure by policy area, 2024-2025



Source: The 2024-2025 Budget.

Infrastructure

2.12 Infrastructure spending is set to increase by 19.8% to HK$106.1 billion in 2024-2025, outpacing growth rates of other policy areas except Housing. This places infrastructure spending as the fourth largest expenditure item after social welfare, health and education. It is worth noting that in recent years, there has been a discernible reduction in contributions from land premium towards the Capital Works Reserve Fund ("CWRF"), a major funding source for capital works in Hong Kong. The share of land premium in total income of CWRF declined visibly from a high of 78.3% in 2021-2022 to 19.6% in 2023-2024. The shortfall had been made up by increased bond issuance, which contributed to a much larger share of CWRF's total income from 15.9% to 73.4% over the same period.

3. Fiscal consolidation programme

3.1 The economic fallout from the outbreak of the COVID-19 pandemic in 2020 had necessitated unprecedent policy responses from governments around the world, significantly impacting their overall fiscal health. Sizable stimulus package and relief measures deployed during the pandemic had resulted in a noticeable deterioration in the fiscal positions of many developed places, with significant increases in their fiscal deficits and government debts compared with the pre-pandemic levels. Consequently, a key challenge in the post-pandemic landscape is unwinding pandemic-related support measures (i.e. fiscal normalization) and recalibrating fiscal policy to restore fiscal balance through a combination of revenue-raising and expenditure-reducing measures (i.e. fiscal consolidation).

3.2 In the light of the above challenge, the International Monetary Fund ("IMF") and the Organisation for Economic Co-operation and Development have provided guidelines to their member states on implementing the fiscal consolidation strategies.[15] Regarding expenditure control, prudent expenditure is essential to enhancing fiscal sustainability in the long-run. Nevertheless, it is crucial to avoid excessive spending cuts that could undermine support for vulnerable sectors, weaken economic recovery and derail long-term development priorities. The guidelines also stress the importance of prioritizing expenditure and achieving efficiency gains to reduce the cost of public services without compromising their quality. On revenue enhancement, places with relatively low tax-to-GDP ratios should focus more on revenue mobilization in their fiscal consolidation efforts, especially targeting top-end taxpayers and purchases of luxury goods and services. Furthermore, structural reforms that aim at protecting and expanding the tax base, as well as ensuring a fair tax system and making good use of any fiscal room to fortify growth, are proposed to secure sustainability of government revenue streams.

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[15] See International Monetary Fund (2023b & 2024b), Organisation for Economic Co-operation and Development (2021) and Robinson (2022).

3.3 Amidst the global trend towards fiscal consolidation, the Financial Secretary has, in the 2024-2025 Budget, announced the implementation of a fiscal consolidation strategy aimed at gradually reducing the fiscal deficit and working towards restoring fiscal balance in a few years' time. This marks a shift from the "moderately liberal" fiscal stance of the 2023-2024 Budget and contrasts with the adoption of "expansionary fiscal policy" of the 2022-2023 Budget. The new fiscal consolidation strategy encompasses measures to increase revenue (as detailed in paragraphs 2.3-2.5 above), control the growth of operating expenditure, and review and re-prioritize capital works.

3.4 Control over operating expenditure will be enforced by (a) maintaining zero growth in the civil service establishment; (b) implementing the Productivity Enhancement Programme to reduce recurrent government expenditure by 1% for two consecutive years; and (c) reviewing operation mode of the "$2 Scheme"[16] and Public Transport Fare Subsidy Scheme. Regarding capital works expenditure, relevant bureaux and departments are tasked with reviewing the cost-effectiveness of works projects and giving due regard to priority and urgency to adjust the implementation schedule.[17]

3.5 While Hong Kong has recently embarked on the path of fiscal consolidation, some other developed places began similar efforts as early as in 2021 to restore fiscal balance. For example, the United Kingdom ("the UK") and Canada have pursued fiscal consolidation in a gradual pace, steering clear of substantial tax increases or swingeing cuts in government services and benefits. In Singapore, although the government has raised tax rates on luxury cars, high-income earners and higher-value properties, the primary focus of its fiscal consolidation effort is to boost tax revenues through promoting economic growth. The following paragraphs will review the fiscal consolidation strategies implemented in the afore-mentioned places. Highlights of individual fiscal measures so adopted will also be presented in **Figure 6** thereafter, and listed by categories such as (a) prudent expenditure (including efficiency savings in the public sector, and re-prioritizing and more focused expenditure); (b) revenue enhancement (especially targeting top-end taxpayers); and (c) fiscal structural reform.

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[16] The "$2 Scheme" is formally known as Government Public Transport Fare Concession Scheme for the Elderly and Eligible Persons with Disabilities.

[17] Works projects that are currently at the preliminary planning or conceptual stage will be adjusted according to importance. Consequently, a huge reclamation plan to build the Kau Yi Chau Artificial Islands is expected to be delayed by two to three years.

The United Kingdom

3.6 In 2023, the UK government set out a new set of fiscal rules in the Charter for Budget Responsibility ("the Charter")[18] to restore discipline in the fiscal framework. This was in response to earlier relaxation of fiscal rule to accommodate the introduction of various relief measures during the pandemic. The Charter sets specific targets for the levels of government debt and borrowing to be achieved in the years ahead and imposes a spending cap on welfare for fiscal prudence.

3.7 In an effort to control government expenditure, the UK government has prioritized efficiency improvements in the public sector over significant expenditure cut. The Public Sector Productivity Programme, launched across all government departments in June 2023, reflects this commitment to optimizing efficiency.[19] On revenue enhancement, the UK government has sought to diversify the economic base and thereby promote growth to boost tax revenues. The Spring Budget 2024 features greater tax relief and additional financial support to sectors crucial to the UK's sustainable growth, including creative industries, artificial intelligence ("AI"), digital technologies, advanced manufacturing, green industries and life sciences. In addition, reductions in the rates of National Insurance Contributions paid by employees and self-employed persons are proposed, with a view to benefiting working individuals, stimulating growth, and promoting a fairer tax system. The impact on revenue, meanwhile, will be balanced by some targeted new tax measures.

Canada

3.8 The Canadian government has emphasized fiscal prudence to repair the damage to public finances caused by substantial government spending during the pandemic, and the consequential inflated fiscal deficit and debt ratio. Budget 2021 was thus formulated as a prudent fiscal plan designed to reduce the ratio of federal debt to GDP over the medium-term and unwind the pandemic-related deficits.[20] Budget 2022 continued the fiscal prudence to restate the declining debt-to-GDP ratio as the fiscal anchor, aiming to return the ratio to its pre-pandemic level by the end of the budget's forecast horizon.

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[18] In the UK, HM Treasury must prepare a document – the Charter for Budget Responsibility – to set out the government's fiscal and debt management policy and how this will operate. The Charter was first introduced in April 2011 and has been revised on several occasions since then.

[19] According to the Spring Budget 2024, raising public sector productivity by 5% would be equivalent of around £20 billion (HK$198 billion) additional funding. See Keep et al. (2024).

[20] In Budget 2021, the government expected the federal deficit to shrink significantly from 16.1% of GDP in 2020-2021 to 6.4% in 2021-2022 and gradually to 1.1% of GDP (i.e. close to its pre-pandemic level) in 2025-2026.

3.9 For Budget 2023, Canada's Finance Minister has framed it as a commitment of fiscal restraint, outlining measures to reduce civil service travel costs and professional service fees by 15% and, more broadly, cut spending across departments and agencies by roughly 3% by 2026-2027. Despite these cost-cutting efforts, the budget has introduced several new spending initiatives, including the launch of a national dental programme, support for green technology development, and provision of targeted assistance for lower-income families. To boost revenue, Budget 2023 revises the Alternative Minimum Tax ("AMT")[21] regime which increase the tax payable by more affluent taxpayers. This move aligns with the earlier introduction of a new luxury tax on yachts, private jets and luxury vehicles in 2022. The targeted tax measures reflect the government's commitment to "affordable users pay" principle and its adherence to a more progressive tax structure.

<u>Singapore</u>

3.10 The Singaporean government has embraced a fiscal consolidation strategy prioritizing raising more revenue over expenditure tightening. This approach has been reflected in the 2024 Budget which forecasts a 4.6% increase in total government expenditure in 2024-2025, up from 1.9% in 2023-2024. The budgetary increase includes enhanced Assurance Package and Enterprise Support Package which offer near-term relief to Singaporean households and firms respectively. The "young seniors" who are currently in their 50s and early 60s will receive further support through increased financial provisions dedicated for their retirement and healthcare needs. The fiscal space for these initiatives has been enabled by higher-than-expected tax revenue in 2023-2024, consequential to the robust economic recovery in the preceding two years.

3.11 On revenue enhancements, the 2022 and 2023 Budgets have sought to raise the Goods and Services Tax ("GST") and the property tax of higher-value properties, as well as introducing a more progressive tax structure targeting top income-earners. In addition, the 2022 Budget introduced another Additional Registration Fee tier for luxury cars. For long-term fiscal sustainability, the Singaporean government has focused on revenue growth through bolstering economic growth. The 2024 Budget details the government's initiatives to support businesses and stimulate growth, including (a) strengthening Singapore's competitive advantages to attract foreign investment; (b) investing in emerging technologies to foster a culture of innovation; (c) supporting local enterprises to manage rising business costs; and (d) equipping workers with the skills and resources for success.

[21] In Canada, AMT is an alternative tax that is calculated based on fewer deductions, exemptions and tax credits than under the normal income tax calculation rules. A taxpayer must pay the higher of AMT and income tax calculated under the ordinary rules.

Figure 6 – Highlights of fiscal consolidation measures implemented in the United Kingdom, Canada and Singapore

Prudent expenditure | Revenue enhancement | Fiscal structural reform

	Efficiency savings in the public sector	Review and re-prioritization of expenditure	More focused expenditure
UK	• Implement the Public Sector Productivity Programme to streamline the UK's public sector workforce, focusing on enhancing the efficiency of the public service delivery and optimizing the public sector operations	• Allocate additional funding in the Spring Budget 2024 to enable various government departments to leverage cutting-edge technologies, such as AI and digital technologies, for enhancing efficiency and improving daily operations	• Direct government expenditure to: catalyze the growth sectors of the future[4]; and create an environment conducive to boosting growth, productivity and investment [5]
Canada	• Implement a 15% reduction in civil service spending on professional services and travel • Budget for a 3% cut in spending by departments and agencies by 2026-2027	• Assess the pace and scale of previously announced spending, reducing the funding that remains unallocated or is no longer required	• Pledge "transformative investments" in green economy as Canada strives to maintain its competitiveness in the global clean technology competition • Build a healthy future for Canadians by allocating funds to a national dental programme that assists uninsured individuals
Singapore	• Implement a 1% reduction in budget caps across all Ministries and state agencies for ongoing functions under the block budget starting from the 2023 financial year[1], [2]	• Prioritize government expenditure to support Singaporeans coping with high cost of living through Assurance Package and to help local businesses in managing rising business costs with Enterprise Support Package [3] • Launch the S$8.2 billion (HK$47.7 billion) Majulah Package to support the retirement and healthcare needs of 1.6 million Singaporeans born in 1973 or earlier	• Invest in emerging technologies and allocate additional funds for R&D • Put in place financing schemes and grants to support enterprises in green transition • Prioritize human capital development through investing in formal schooling and enabling workforce reskilling and upskilling

Notes: (1) Even with the budget reduction, the total budget of Ministries and state agencies can grow partly due to the budget for specific projects funded on top of the block budget.
(2) This, coupled with the earlier 2% cut in 2017, means a cumulative 3% reduction in budget caps.
(3) The S$1.9 billion (HK$11.1 billion) Assurance Package, especially for low- and middle-income households, offers a range of benefits including consumption vouchers, cash payouts and utilities rebates. The S$1.3 billion (HK$7.6 billion) Enterprise Support Package offers a corporate income tax rebate, enhancements to the Enterprise Financing Scheme, and an extension of the SkillsFuture Enterprise Credit for business and work transformation.
(4) For example, the Spring Budget 2024 allocates over £1 billion (HK$9.88 billion) of new tax reliefs for the UK's creative industries.
(5) This includes earmarking £280 million (HK$2.8 billion) annually to improve research and development ("R&D") tax reliefs which, in turn, helps drive innovation in the UK.

Figure 6 – Highlights of fiscal consolidation measures implemented in the United Kingdom, Canada and Singapore (cont'd)

Prudent expenditure | **Revenue enhancement** | **Fiscal structural reform**

	Higher income/profits tax rates for top-end taxpayers	Other tax-raising measures
UK	• Raise the corporation tax rate from 19% to 25% for companies with profits exceeding £250,000 (HK$2.5 million)	• Increase airline passenger duty • Introduce a new duty on vaping industries • Implement a one-off tobacco duty increase
Canada	• Propose to raise the AMT rate from 15% to 20.5% to ensure the wealthiest Canadians pay their fair share of tax(6)	• Introduce a new luxury goods tax on yachts, private jets and luxury vehicles • Enhance tax collection by: (a) amending the Income Tax Act's General Anti-Avoidance Rule; and (b) increasing funding for the Canada Revenue Agency to combat abusive tax avoidance
Singapore	• Raise the personal income tax rate for the highest income tax bracket from 22% to 24%	• Raise (a) the property tax rates for higher-value residential properties; and (b) the Buyer's Stamp Duty for higher-value residential and non-residential properties • Introduce a new tier for the Additional Registration Fee applicable to luxury cars, initially set at 220% in 2022 and adjusted to 320% in 2023 • Implement a 15% increase in tobacco excise duty across all tobacco products • Raise GST rate in two steps from 7% to 8% in 2023 and from 8% to 9% in 2024

Prudent expenditure | **Increasing Revenue** | **Fiscal structural reform**

UK	• Set new fiscal rules that: (a) mandate government debt (i.e. the stock of government's past borrowings) to follow a declining trajectory relative to GDP by 2028-2029; and restrict government borrowings to not more than 3% of GDP within the same timeframe; and (b) establish a welfare spending cap to ensure that expenditure on certain welfare items remains within a pre-determined limit and margin set by HM Treasury
Canada	• Restate the fiscal anchors of keeping the debt-to-GDP ratio on a declining path and reducing the fiscal deficit to below 1% of GDP in 2026-2027 and thereafter
Singapore	• Launch a new tax credit scheme – the Refundable Investment Credit scheme – with a refundable cash feature for eligible projects. The scheme aims to incentivize a broad range of high-value economic activities (7), thereby attracting investment from global companies into Singapore

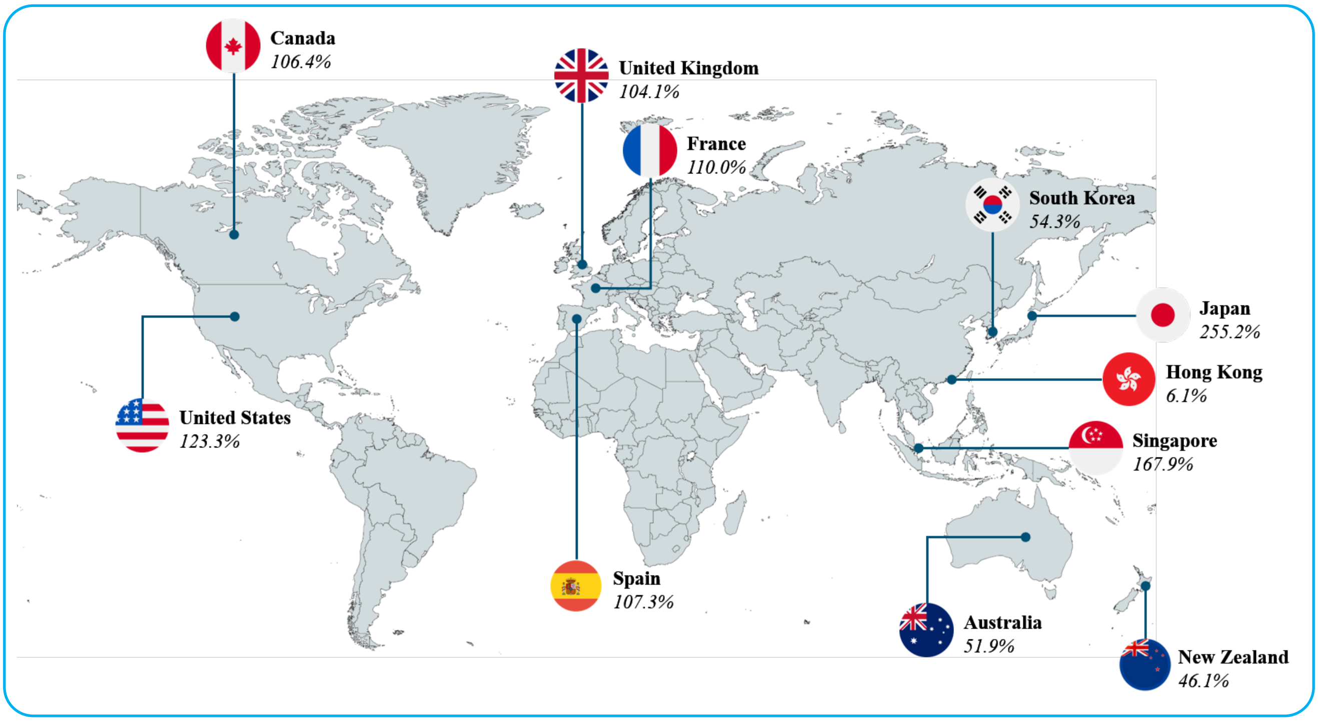
Notes: (6) The legislative proposal to enact the tax change, which was released in August 2023, has not yet passed into legislation.
(7) These activities include the setting up or expansion of manufacturing activities, new innovation and R&D activities, as well as activities in support of the green transition.

Sources: Budget statements from the UK, Canadian and Singaporean governments (various years) and various government websites.

4. Bond issuance

4.1 In the 2024-2025 Budget, the Government continues its commitment to infrastructure investment, forecasting an average annual capital works expenditure of about HK$90 billion between 2024-2025 and 2028-2029. A total of HK$620 billion in bonds will be issued over the period to drive green/sustainable and infrastructure projects[22], which allows for a fair and efficient way of distributing the fiscal responsibility as the debt burden is borne by generations who will directly benefit from improved infrastructure. Despite the recent reduction in fiscal reserves, Hong Kong still has considerable room for borrowing in view of its relatively low government debt-to-GDP ratio. According to IMF, Hong Kong's debt ratio stood at 6.1% in 2023, the fifth lowest among the 190 places it assessed (**Figure 7**). Furthermore, notwithstanding the Government's proactive bond issuance programme, this year's Budget also foreshadows a tapering or even slight retreat in amount of bond outstanding towards the end of the "medium range", as indicated by the forecast for 2028-2029 when bond repayment (HK$107.9 billion) is anticipated to exceed that for proceeds from issuance (HK$95.0 billion).

Figure 7 – Government debt-to-GDP ratio in selected places, 2023



Source: International Monetary Fund (2024a).

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[22] Some HK$338.2 billion of the bond proceeds will be used for repayment of bonds issued previously.

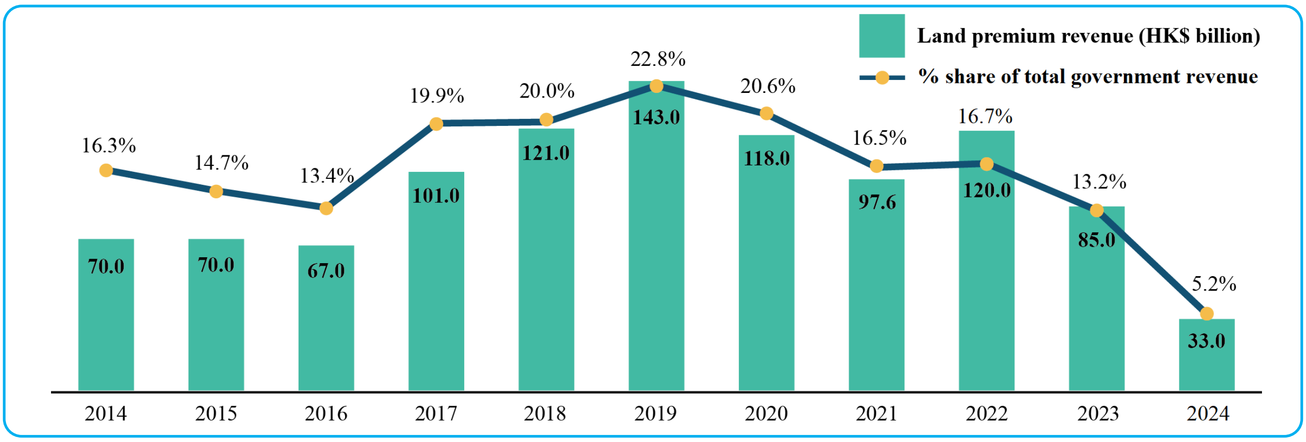
5. Removal of all demand-side management measures for residential properties

5.1 Another key highlight of this year's Budget is the removal of all demand-side management measures for residential properties that had been introduced since 2010. The Buyer's Stamp Duty, New Residential Stamp Duty and Special Stamp Duty have been cancelled with immediate effect.[23] Following the Budget announcement, the Hong Kong Monetary Authority has further relaxed the maximum loan-to-value ratios for certain mortgage loans and suspended the stress test requirements for mortgage borrowers.

5.2 Following the elimination of the demand-side management measures, there have been reports of improved sentiments in the local property market with some pick-up in transactions in both primary and secondary markets. Nevertheless, concerns over the prospects for the property market remain, particularly in view of the inventory of 20 300 unsold units of completed projects as at end-2023. Furthermore, the potential ample supply of new residential units coming on stream might further impact the market, in view of 71 000 units under construction but not yet sold or not yet offered for sale during the same period.[24]

5.3 Amid prevailing market uncertainties, the Government seems to be cautious with its 2024-2025 Land Sale Programme. It plans to sell 11 sites, of which eight are residential plots projected to supply 5 690 flats. This represents a pullback from the previous year's 18 sites, of which 12 were residential plots capable of producing 9 120 flats. Reflecting this, the estimated land premium for 2024-2025, at HK$33.0 billion[25], is forecast to account for a mere 5.2% of total government revenue, versus an average of 17.4% during the previous decade (**Figure 8**).

Figure 8 – Forecast for land premium in Budgets, 2014-2015 to 2024-2025



Source: Budget speech (various years).

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23 Previously, Buyer's Stamp Duty applied to non-permanent Hong Kong residents and New Residential Stamp Duty targeted second-time home purchasers. As for Special Stamp Duty, those homeowners who sold their flats within two years of purchase would have to pay the tax.

24 See Housing Bureau (2024).

25 In addition to land sales, land premium also includes revenue received from (a) private treaty grants; (b) modification of existing leases, exchanges and extensions; and (c) fees received in respect of short-term waivers.

5.4 Indeed, IMF has previously highlighted Hong Kong's reliance on volatile property-related sources (land premium and stamp duties) and a small number of taxpayers to cover most of its government expenditure before the pandemic.[26] Salaries and profits taxes have continued as a major source of revenue after the pandemic, with their combined shares in total government revenue rising from 35.0% in 2021-2022 to 40.8% in 2022-2023 and further to 45.2% in 2023-2024. In contrast, the corresponding combined shares of land premium and stamp duties have been on the decline, at 35.0%, 22.4% and 12.5% respectively over the period.[27] Notwithstanding the fluctuations in property-related sources, the majority of government expenditure goes to areas related to people's livelihood and is therefore relatively rigid. Meanwhile, estimate of land premium in the medium range forecast is based on historical average of the past figures. The forecast for 2025-2026 onwards is assumed to be 3.4% of GDP, being the 20-year historical average with possible adjustment with reference to the land sale programme. However, there have been significant variances between forecast and actual land premium revenue over the past decade, with differences ranging from HK$1.2 billion to HK$65.6 billion between 2014-2015 and 2023-2024.

5.5 Against the volatility of revenue from land premium, there have been renewed discussions about whether the Government should undertake a comprehensive review to assess (a) any major structural issues in government finances that need to be addressed; and (b) the feasibility of introducing new broad-based taxes while ensuring that the new tax system remains attractive to investors at the same time.[28] On the latter, a variety of options have been suggested by the community and studied by the Government to broaden the tax base over the years. Yet, there is no consensus on the preferred options given the merits and concerns over each individual option. Some options such as increasing tax rates for salaries tax and profits tax might raise government revenue, but they do not resolve the core issues of a narrow tax base and vulnerability to cyclical volatilities (**Figure 9**). Reducing allowances and deductions under salaries tax could help broaden the tax base by bringing low-income earners into the tax net. However, it could lead to higher effective tax rates for high-income earners, potentially having some disincentivizing effect on the inflows of international talent. On the other hand, implementing GST could provide a stable revenue stream as the tax is broad-based and less affected by economic downturns. Nevertheless, it is inherently regressive and might incur high administrative and compliance costs. Additionally, imposing taxes on luxury goods, capital gains, dividends and land and sea departures might deter the inflows of capital or tourists into Hong Kong.

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[26] See International Monetary Fund (2023c).

[27] Revenue from land premium to total government revenue for 2021-2022 stood at 20.6%, before easing markedly to 11.2% in 2022-2023 and 3.5% in 2023-2024. The corresponding shares for stamp duties were 14.4%, 11.2% and 9.0%.

[28] See Hong Kong General Chamber of Commerce (2024), Hong Kong Institute of Certified Public Accountants (2024) and China Daily (2024a).

Figure 9 – Comparison of tax options proposed to broaden the tax base

Considerations	Adjustments to existing salaries and profits taxes			Introduction of new taxes				
	Increase the tax rates	Reduce personal allowances and deductions	Enhance the progressivity of the taxes	Goods and Services Tax	Luxury Goods Tax	Capital Gains Tax ("CGT")	Dividends Tax	Land & Sea Departure Tax
Broadening of tax base	✗	✓	✗	✓	✓	✓	✓	✓
Revenue stability (immunity from economic cycles)	✗	✗	✗	✓	✗	✗	✗	✓
Fairness (in line with the "capacity to pay" principle)	✓	✗(1)	✓	✗	✓	✓	✓	n.a.(2)
Maintain international competitiveness of Hong Kong	Against the international trend of reducing direct taxes to attract talent/capital			✓ / ✗(3)	✗(4)	✗(5)	✗(6)	✗(7)
Easy to implement with low administrative/compliance cost	✓	✓	✓	✗(8)	✗(9)	✗(10)	✗(11)	✓

Notes: (1) The lower tax threshold will mean less room for low-income individuals/households with dependents to escape the tax burden.
(2) Under this tax, all persons departing by land or sea would be charged at the same rate. It has nothing to do with the "capacity to pay" principle.
(3) A GST with a tax rate that is lower than regional or international norm will have no material impact on competitiveness of Hong Kong, as the territory is among the few developed places without such tax.
(4) Price of taxable luxury goods may rise and this may have adverse impact on retail industry and tourism.
(5) Some investors may choose to invest offshore for tax avoidance purposes, while some others might seek to retain their current investments to avoid CGT even if profitable opportunities arise.
(6) Under Hong Kong's existing territorial source principle of taxation, the new tax would only apply to dividends paid by Hong Kong companies. This may prompt investors to invest overseas in order to avoid paying the tax.
(7) Commentators are concerned that the tax may affect inbound tourism and Hong Kong's further integration with the Mainland.
(8) Businesses may need to invest in new accounting systems, staff training and additional record-keeping.
(9) Given the lack of a universally accepted or socially agreed-upon definition, identifying what constitutes "luxury goods" for taxation purposes can be challenging.
(10) Overseas experience shows that legislation for a CGT is complex and the introduction of such tax would affect the simple tax system of Hong Kong.
(11) The introduction of Dividends Tax may be prejudicial to Hong Kong's simple tax system as complicated legislation is required to prevent double taxation of businesses' income.

Sources: Financial Services and the Treasury Bureau (2006 & 2014) and Legislative Council Secretariat (2021).

5.6 In the light of each tax option's own set of trade-offs, there are views that a thorough assessment is imperative when considering any such introduction. New taxes and major adjustments to existing ones, if chosen, should be capable of generating a stable and adequate revenue stream for the Government, as well as adhering to the principle of fairness by equitably distributing the tax burden. Additionally, such tax option should also maintain the simplicity and competitive edge of Hong Kong's tax system relative to those of other developed places.

6. Observations

6.1 The following observations are made based on the findings above:

(a) the Government reported a larger-than-expected fiscal deficit for 2023-2024, attributable to a noticeable shortfall in revenue from land premium and stamp duties amid the lacklustre performance of the property and stock markets. This has resulted in a further depletion of the fiscal reserves to HK$733.2 billion, the lowest level since 2012-2013;

(b) in the face of pressure on public finances, the Financial Secretary has budgeted for a restrained increase in total government expenditure with significantly fewer "sweeteners" in this year's Budget. Coupled with the introduction of several targeted new tax measures and an increase in bond issuance, the consolidated fiscal deficit will narrow by more than half in 2024-2025 vis-à-vis 2023-2024;

(c) despite the above fiscal improvement, the 2024-2025 Budget introduces a fiscal consolidation strategy aimed at progressively narrowing the fiscal deficit to restore fiscal balance. The strategy will focus on expenditure cuts and include some revenue increases pragmatically. While Hong Kong is at the nascent stage of fiscal consolidation journey, other developed places such as the UK, Canada and Singapore have commenced their efforts earlier to restore fiscal health. They have pursued a gradual pace of fiscal consolidation, avoiding significant tax hikes or drastic reductions in government expenditure;

(d) in controlling expenditure, the UK, Canada and Singapore have adopted a three-pronged approach consisting of: (i) achieving efficiency savings in the public sector, as exemplified by the UK's Public Sector Productivity Programme which has been implemented across all government departments, or by setting targets for expenditure reduction as seen in Canada and Singapore; (ii) reviewing and re-prioritizing government spending to direct funds towards more essential areas; and (iii) earmarking new spending specifically for sectors that could enhance the countries' competitiveness and/or to provide targeted support to the most vulnerable groups. Additionally, the UK and Canada have also established new fiscal rules that set limits on the government's debt and borrowings and/or on certain welfare spending;

(e) concerning revenue enhancement, the UK, Canada and Singapore have focused their fiscal consolidation efforts on stimulating higher economic growth to boost tax revenues. Nevertheless, Canada and Singapore have complemented this initiative by raising the tax rates paid by high-income earners. Canada has further introduced some forms of wealth tax that target luxury goods, whereas Singapore has opted to increase wealth taxes by applying higher tax rates to luxury cars and higher-value properties;

(f) the 2024-2025 Budget also includes an expansion in bond issuance programmes to drive green/sustainable and infrastructure projects. With a relatively low government debt-to-GDP ratio, the Government has ample fiscal room for further bond issuance to meet the long-term funding needs; and

(g) another highlight of this year's Budget is the removal of all property-related demand-side management measures and relaxation of mortgage lending rules. Nevertheless, the inventory of unsold units, coupled with potential ample supply of new flats, might challenge the continued reliance on land sales as a substantial revenue source for the Government as has been the trend in the past years. This has in turn renewed discussions about whether the Government should conduct a review to explore the various options to broaden the tax bases, each accompanied by its own set of trade-offs.

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Note: ^ Internet resources listed in this section were accessed in April 2024.