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Hong Kong's 2011/12 Budget:

Aiming to Provide Inflation Relief and Reduce Inflation Expectations

- ❖ The Financial Secretary, Mr. John Tsang delivered his fourth budget speech today.
- ❖ The government hands out a HKD19.5 billion package for inflation relief as widely expected and showed its determination to increase housing supply to anchor inflationary expectations.

The Third Highest Surplus on Record

- ❖ Instead of the government's earlier estimate of a deficit of HKD25 billion, the estimated 2010/11 consolidated budget ended with a surplus of HKD71.3 billion, the third highest on record, amounting to 4.1% of GDP. The surplus mainly reflected higher-than-expected revenues from profits and salaries tax, stock and property stamp duty and land sales, as well as smaller government spending.

Exhibit 1

	HKD bn	Change from initial estimate HKD bn
Total Revenue	374.8	+82.8
<i>Profit and salaries tax</i>	140.5	+22.2
<i>Stock and property stamp duty</i>	51.0	+21.0
<i>Land sales</i>	62.0	+27.9
Total expenditure	303.5	-13.7
Consolidated budget surplus	71.3	

Source: 2011/12 Budget

Exhibit 2

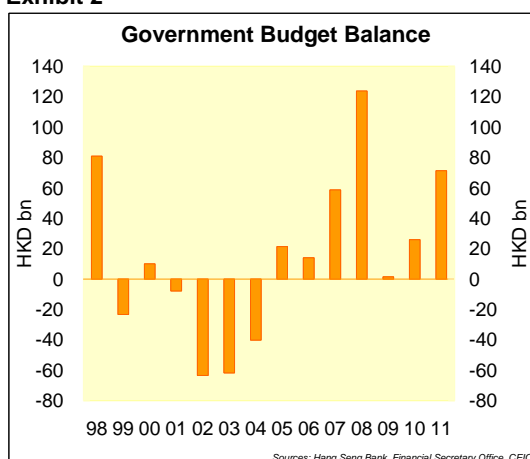
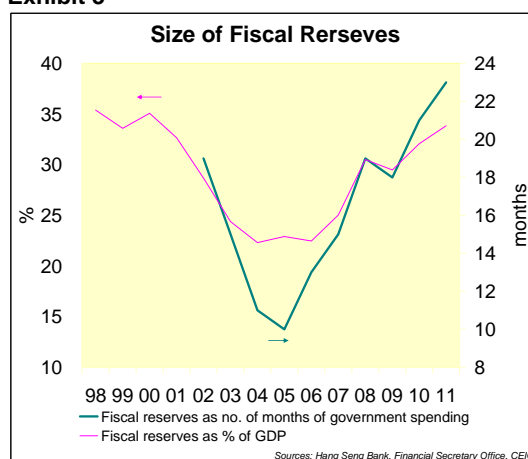


Exhibit 3



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- ❖ According to the government's latest estimates, Hong Kong's fiscal reserves will reach a record high of HKD591.6 billion by March 2011, equivalent to 23 months of government expenditure, or 34% of GDP.
- ❖ For 2011/12, the government expected a relatively small surplus of HKD3.9 billion in the budget, equivalent to about 0.2% of GDP. This implies that the potential impact of the budget on the economy will be relatively neutral in the year ahead.

Inflation Relief Measures

- ❖ Despite the sizable fiscal reserves, the government did not aggressively expand public spending, probably for fear of further fanning price pressures. Instead, this year's Budget offered a HKD19.5 billion package to help relieve the rising costs of living, as Hong Kong's inflation rose to a 29-month high of 3.6% in January.
- ❖ The major measures include:
 - The issuance of HKD5-10 billion of Inflation indexed retail bonds to help reduce the impact of inflation on small investors
 - One-off concessions worth HKD18.3 billion, such as
 - exemption of property rates for the four quarters of 2011/12, capped at HKD1,500 per quarter for each rateable unit
 - waiver of public rental for two months
 - electricity subsidies of HKD1,800 per household
- ❖ In addition, tax allowance for children and dependent parents, and for business would be raised, at a cost of HKD1.2 billion.

Increasing Land Supply

- ❖ While rising property prices and rentals, in addition to food prices, are among the main culprits driving up inflation, the government launched no new measures to curb short-term activities in the housing market. Instead, it focuses on measures to address the structural issue of increasing supply to anchor price expectations.
 - For FY11/12, the government aims to provide a potential supply of 30,000 to 40,000 housing units, more than the average annual supply of 20,000 units, by proactively offering land to the market;
 - Speed up new MTRC and urban renewal tenders
- ❖ While the impacts of these changes may need more time to be seen, the latest moves do imply a fundamental change in its overall housing or land policy. We would not be surprised to see more new measures if property prices continue to accelerate.

Strong Economic Performance and Rising Risk of Inflation

- ❖ Underpinned by strong domestic demand, Hong Kong's 4Q GDP registered four straight quarters of above-trend growth, expanding 6.2% year-on-year. For 2010 as a whole, the Hong Kong economy registered a robust growth of 6.8%, the fastest in four years.



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- ❖ Going forward, external demand is likely to slow as the global economic recovery remains fragile, but consumer demand should continue to underpin growth, particularly in view of the improvement in the labour market. The ongoing government infrastructure would also boost investment spending.
- ❖ The outlook for inflation is more uncertain, particularly in light of surging oil prices amidst the recent political turmoil in oil exporting countries in the Middle East and North Africa.
- ❖ Against such backdrop, we expect Hong Kong's GDP to grow by 5.0% this year and inflation to trend higher to 4.7% from last year's 2.4%.
- ❖ The government sees the economy expand 4% to 5% 2011 and inflation to climb to 4.5%.

Exhibit 4

	2010 (yoy %)	2011 Forecast (yoy %)	
		Hang Seng Bank	Government
Private Consumption	5.8	5.1	---
Government Consumption	2.7	3.0	---
Gross Fixed Capital Formation	8.1	7.5	---
Export of goods	17.3	8.9	---
Import of goods	18.1	8.9	---
Export of Services	15.0	8.1	---
Import of Services	10.9	6.0	---
Real GDP	6.8	5.0	4% to 5%
Composite CPI	2.4	4.7	4.5%
Underlying CPI inflation	1.7	4.7	4.5%
Nominal GDP	7.8	8.2	6.5% to 7.5%

Source: Census and Statistics, Financial Secretary's Office, Hang Seng Bank.



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