Budget Commentary
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How Green is the Budget?

HONG KONG, 6 March 2018 – The Government has produced yet another massive surplus, HK$ 138 billion for 2017-18, taking fiscal reserves to a mega HK$ 1,092 billion. The spread of the announced use of the surplus – on relief measures, community sharing, technology, health care, education, various industries and professions – is wide-ranging and welcoming. However, in regard to greening the environment, there is disproportionately little that has been offered up from the massive surplus.

While this is a disappointment, there are some encouraging good news in the form of the announced new sustainability-related fiscal policies and measures, such as incentives to promote green finance to raise capital for long-term environmental projects, switch to electric vehicles, and encourage eco-friendly building practices.

Most importantly, it is noteworthy of a fundamental change in fiscal policy, which could have ramifications far beyond this fiscal year in how environmental and social works are funded. The Financial Secretary has made a range of decisions – including changes in the way land premium revenues may be used, the introduction of Government green bonds, tax concessions for green buildings, subsidy for green certification and a boost in financial education – to set the stage for long-term development of Hong Kong into a sustainable city and green financial hub.

New Way of Funding "Soft Infrastructure" or "Intangible Capitals"

Until now, the Capital Works Reserve Fund (CWRF), which derives the majority of its HK$ 167 billion from land premiums, was used mostly for "hard infrastructure or "Tangible/Physical Capitals" like roads and bridges, plants and buildings, sewage systems and industrial installations.

The 2018-19 Budget sees a transfer of HK$ 80 billion from the CWRF to the General Revenue Account (GRA) for recurrent spending, meaning that these earnings from land premiums will no longer be limited to only capital works. [1] This responded to Civic Exchange's call in its budget proposals that resources in the CWRF should be released to fund soft infrastructure building such as job creation and the re-skilling of the labour force to meet the challenges of global warming, liveability, technology disruption and an aging population. [2]

Government Green Bonds Could Spur the Green Finance Market

The Financial Secretary also announced a green bond issuance programme with a borrowing ceiling of $100 billion, and with borrowed sums credited to the CWRF. It is notable that this green bond revenue has been earmarked to fund Government "green public work projects."[3] It is hoped that "green public work projects" will address issues like air quality, nature conservation, smarten up urban streets, public open space, road design for walkability and clean public transport systems, better management of our water and waste, and climate change – which were proposals Civic Exchange made in our budget submission in January. [4]

The issuance of Government green bonds could achieve a few wins: Currently, Hong Kong has a very narrow tax base in that 74% of Government revenue is derived from land premium, stamp duty, profits and salary taxes, which are susceptible to economic conditions. By its bond issuance programme, the Government can expand its source of finance, when it has proved difficult to expand its tax base to cater for economic downturns. Instead of using taxpayer money, a whole community of investors can contribute to funding the greening of Hong Kong and earning income yields from this investment.

This sizable Government green bond proposal may also spur the growth of the Hong Kong green finance market, serving as a positive example to the private sector that green financial products can be efficient, reliable and profitable. With success, the Government may expand into a wider spectrum of financing schemes like social impact bonds that could be deployed for financing health, aging, poverty relief etc., which have become an emerging trend in other major markets of the world.

The Budget also introduced a new Green Bond Grant Scheme to subsidise qualified green bond issuers using the Hong Kong Quality Assurance Agency (HKQAA) Green Finance Certification Scheme, announced in January. [5] [6] This promotes the use of the local, third-party green certification service and will enhance development of standards and credibility of the Hong Kong market, necessary for the green finance market to thrive.

The Greening of Financial Education

The Financial Secretary has also asked the Hong Kong Monetary Authority (HKMA) to set up an academy of finance in collaboration with the Financial Services Development Council and other parties. [7] It is hoped that training in green finance, ESG reporting, and sustainable practices will be core to its curriculum. Hong Kong is world-recognized for its financial market expertise, needed to develop into a green finance hub, but human capital development in green project financing at all levels is necessary to take it forward.

Green Buildings

After an allocation of HK$ 200 million last year, the Government will set aside an additional HK$ 800 million to promote the installation of renewable energy (RE) at Government buildings and facilities. [8] The Financial Secretary also announced additional tax concessions for capital expenditure spent on energy-efficient building installations and RE devices. The change announced in the Budget is that tax deductions can be claimed in full in one year, instead of the current timeframe of five years. While these incentives to greener building practices are welcoming, it should be noted that the actual number of applicants for this tax deduction was low and falling (23 applicants in 2012/13; 17 in 2013/14; 12 in 2014/15; and only 9 in 2015/16).[9] It is hoped that the new deduction, if properly promoted, will be taken up for more retrofitting and improvements to buildings.

Transport and Mobility

In terms of transport policy, the Budget reflects the need to balance promoting electric cars over more polluting models, while at the same time containing the total number of all private cars, in a view Civic Exchange shares. It was encouraging to hear the Financial Secretary specifically state the reason for this move, which is "to prevent traffic congestion and aggravation of roadside air pollution."

The Government's announcement of a "one-for-one replacement" scheme, starting immediately, will give a higher concession of up to HK$ 250,000 on First Registration Tax (FRT) for private car owners who buy new electric cars and scrap their current vehicle, subject to several conditions. This is in-line with Civic Exchange's recommendation that car owners should be given incentives to switch from standard cars to electric models.

Over the past few years, the Government has increasingly understood the importance of improving walkability and mobility, in conjunction with restricting private vehicles. The Financial Secretary stated that "to improve roadside air quality and reduce air pollutant emissions in a sustained manner, we will continue to encourage walking and use of public transport." [10] "Improving pedestrian links" is also a part of the HK $8 billion set aside for proposals from the 18 districts to improve their neighbourhoods. [11]

Spending for a Liveable, Green City

The environment is important to the health and well-being of every citizen, and greater budget allocation is required to spearhead urgent projects to address growing problems of air pollution, water wastage, crowded streets and overflowing landfills. Yet, only 4.5% of total public expenditure is budgeted for spending on the "Environment and Food" policy area group in 2018-19; it has been the same low level for many years.

It is imperative that various policy bureaux and departments responsible for the environment must work together to take advantage of the new opportunities that have arisen, from changes in fiscal policy on use of land premiums to establishment of Government green bonds – of which we eagerly await detailed plans. Now is the time to be pro-active in speeding up actions, and putting up concrete, practical environmental improvement programmes – as well as the budgets and financing models needed to bring them forward.

About Civic Exchange

Civic Exchange is a non-partisan think-tank which is committed to evidence-based public policy formulation in addressing urban sustainability and liveability challenges. Our output is independent and analytical rather than opinion-oriented, and always solution-focused. Independence, transparency and collaboration form the foundation of Civic Exchange's core values. Civic Exchange is ranked as one of the top 50 environmental think-tanks in the world, by the University of Pennsylvania's Global Go To Think Tank Index.

Read Civic Exchange's Proposals to 2018-19 Budget here: http://civic-exchange.org/2018/02/01/2018-19-budget/

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[1] Financial Services and Treasury Bureau, HKSAR Government, *Capital Works Reserve Fund (Receipts),* see chart "Movement of the Account," pg 85, https://www.budget.gov.hk/2018/eng/pdf/cwrf-receipts.pdf (accessed 28 February 2018)

[2] Civic Exchange, *Proposals for the 2018-19 Budget*, pg 3, paragraph 12, http://civic-exchange.org/wp-content/uploads/2018/01/CExBudget-2018-20180126final_ForFS_website.pdf

[3] Financial Services and Treasury Bureau, HKSAR Government, *2018-19 Budget*, paragraph 83, https://www.budget.gov.hk/2018/eng/budget14.html (accessed 28 February 2018)

[4] Civic Exchange, *Proposals for the 2018-19 Budget*, http://civic-exchange.org/2018/02/01/2018-19-budget/

[5] Hong Kong Quality Assurance Agency, *Green Finance Certification Scheme Fostering a Green Economy in Hong Kong,* 3 January 2018, http://www.hkqaa.org/cmsimg/1514953363HKQAA_Green%20Finance%20Certification%20Scheme%20Press%20Release_EN.pdf (accessed 28 February 2018)

[6] Financial Services and Treasury Bureau, HKSAR Government, *2018-19 Budget,* paragraph 84, https://www.budget.gov.hk/2018/eng/budget14.html

[7] Ibid, paragraph 77, https://www.budget.gov.hk/2018/eng/budget14.html

[8] Ibid, paragraph 168, https://www.budget.gov.hk/2018/eng/budget29.html

[9] Internal Revenue Department, HKSAR Government, "Press Release: LCQ2: Feed-in tariff scheme for renewable energy power generation installations," 12 July 2017, see Annex 2, https://www.ird.gov.hk/eng/pdf/press_17071201_02.pdf (accessed 2 March 2018)

[10] Financial Services and Treasury Bureau, HKSAR Government, *2018-19 Budget,* paragraph 169 , https://www.budget.gov.hk/2018/eng/budget29.html

[11] Ibid, paragraph 171, https://www.budget.gov.hk/2018/eng/budget30.html