

**THE HONG KONG HOUSING AUTHORITY**

**Memorandum for the Housing Authority**

**Housing Authority's Revised Budgets 1999/2000  
Proposed Budgets 2000/2001  
and  
Financial Forecasts 2001/2002 to 2003/2004**

**PURPOSE**

To seek Members' approval of the 1999/2000 Revised Budgets and 2000/2001 Proposed Budgets of the Authority prior to their submission to the Chief Executive for formal approval and for Members to note the Financial Forecasts for 2001/2002 to 2003/2004.

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## BACKGROUND

3. The Authority provides subsidised housing and related support facilities comprising -

- approximately 648,000 rental units
- 298,000 Home Ownership Scheme (HOS) flats
- 1.0M sq.m. commercial space
- 77,000 + parking spaces
- 400,000 + sq.m. factory space
- 2.0M sq.m. Welfare and Non-domestic space

4. While the Authority's expenditure is not part of the Government's expenditure and general revenue, it represents an important element of public sector spending and averages about **16.5% of public sector expenditure**. Based on the Authority's revised 1999/2000 budgets and the Government's approved 1999/2000 budgets, the following figures give a reasonable indication of the Authority's finances compared to the Government's -

	HA		HKG	% HA to HKG
	\$Bn		\$Bn	
(a) Operating Income	41.1	)		
(b) Net Investment Income	2.1	)	145.3	29.7
(c) Operating Expenditure	31.3		188.9	16.5
(d) Average Funds Managed	26.8		N/A	-
(e) Capital Budget	29.9		33.1	90.3

## BUDGET PROCESS

5. The budgets and forecasts are prepared as an integral part of the business planning process. Under this business planning process, each Business Director has produced a business plan which includes the key budget and forecast proposals. The business plans have been discussed and endorsed by the respective Business Committees. To interface with the business planning process, a strategic plan has been developed for the Authority. The strategic plan and the individual business plans are then consolidated together with extracts from the proposed budgets to form the Authority's Corporate Plan which was endorsed in the Strategic Planning Committee (SPC) at its meeting on 12 January 2000.

6. The Budgets and Forecasts Proposal for 1999/2000 to 2003/2004 attached has been prepared in line with the business planning process. The annual business plans including the Operating Accounts, Capital and Cash Budgets and the Financial Forecasts of the Authority have been examined and endorsed by the Finance Committee (FC) before their submission to the Authority for approval.

## **BUDGETARY BASES, ASSUMPTIONS AND PRINCIPLES**

7. In keeping with previous exercises, the budgets and forecasts are based on the June 1999 PHDP and only approved policies as at 31 July 1999 have been factored into the budgets and forecasts.

8. For the purpose of preparing the business budgets and forecasts, the bases and assumptions which affect all businesses and other general or cross business parameters were approved by the Finance Committee. Those business specific bases and assumptions were approved by the respective Business Committees. Details are summarised at Section III of the Budgets and Forecasts Proposal.

9. In addition, the following principles were adopted -

(a) **Revenue policy**

The philosophy as stated in the Long Term Housing Strategy, i.e. to ensure that adequate housing at affordable price or rent is available to all households, continues to be followed. With regard to the public rental housing, Members' attention is drawn to the following clauses of the Housing Ordinance -

- Section 4 (4) "revenue accruing from its estates shall be sufficient to meet its recurrent expenditure on its estates."  
and
- Section 16 (1A) (b) "the median rent to income ratio in respect of all classes of land in all estates let for residential purposes, as determined by the Authority, shall not exceed 10%."

(b) **Cash flow**

The Authority aims to maintain adequate funds to sustain its capital programmes and recurrent operations. The Authority is financially autonomous and the Government has agreed that available funds currently in excess of the short-term requirements should be placed in the Development Fund as part of HA's finances to accelerate the provision of public housing.

(c) **Expenditure growth**

The Authority will continue to adopt prudent financial policies to make the best use of its funds and to strive to get better value for money in respect of the services which the Authority provides or which are contracted out.

Members are also requested to note the financial objectives of the core businesses as set out in paragraph 21, 25 and 30.

10. As demonstrated at paragraph 4 above, the scale of the Authority's operations and finances are very large and complex compared to any Government department or public sector organisation. The increased uncertainty arising from fluctuations in economic, market, government and political risks will impact significantly on the Authority's budgets and forecasts which are subject to a wide range of variables and external factors. In particular, the recent volatile economic environment together with the peaking of production over these few years has caused the Authority's cash to drop from \$37Bn in November 1998 to the current level of \$16Bn, i.e. a reduction of \$21Bn over 14 months. Sensitivity analyses to gauge the financial impact on the Authority with changes in the key budget parameters and assumptions are at paragraphs 41 and 42.

## **ENHANCED PRODUCTIVITY PROGRAMME**

11. The Department is fully committed to the Enhanced Productivity Programme (EPP) and has various BPR, outsourcing and similar initiatives to enhance efficiency and productivity which have already been incorporated into the business plans and budgets. The estimated EPP savings for 1999/2000 and 2000/2001 are 1.41% and 1.32% respectively. It is expected that the target of cumulative saving of 5% by 2002/2003 will be well exceeded.

## REVISED BUDGETS 1999/2000 AND PROPOSED BUDGETS 2000/2001

### A. Consolidated Budgets for the Authority

#### Consolidated Operating Account

12. The consolidated operating results for 1999/2000 and 2000/2001 are set out at Table 1 below -

	Public Rental Housing	Commercial Properties	Home Ownership	Consolidated Operating Surplus
1998/1999 (Actual)	(1,979)	2,242	15,873	16,136
1999/2000 (Approved Budget)	(1,592)	1,755	10,161	10,324
1999/2000 (Revised Budget)	(1,915)	1,384	10,272	9,741
2000/2001 (Proposed Budget)	(1,640)	1,448	15,150	14,958

#### Cash Budget

13. The budgeted cash flows and closing cash balances are summarised below -

	Net Cash Inflow/ (Outflow) in the year	Closing Cash Balance	Analysis of Cash Balance		
			HCWF <sup>(1)</sup>	DF <sup>(2)</sup>	WC <sup>(3)</sup>
1998/1999 (Actual)	(1,042)	30,987	15,698	3,116	12,173
1999/2000 (Approved Budget)	(4,552)	21,831	15,518	-	6,313
1999/2000 (Revised Budget)	(8,362)	22,624	15,092	-	7,532
2000/2001 (Proposed Budget)	9,637	32,261	13,138	7,854	11,269

Notes :  
 (1) Housing Capital Works Fund  
 (2) Development Fund  
 (3) Working Capital

14. The Authority's cash position is forecast to remain reasonably strong throughout the budgets and forecasts period notwithstanding the fall in 1999/2000 by \$8.4Bn mainly due to increase in construction payments during the peak production period. With increased no. of HOS/PSPS flats completed for sale from 2000/2001 onwards, the cash position is expected to improve from the current level of \$16Bn to \$32.3Bn at 31 March 2001.

### Capital Expenditure (HCWF)

15. The capital budgets are summarised at **Table 3** below -

<b>Table 3 - Summary of Capital Expenditure (\$M)</b>				
	<b>Actual 1998/1999</b>	<b>Approved Budget 1999/2000</b>	<b>Revised Budget 1999/2000</b>	<b>Proposed Budget 2000/2001</b>
(A) Construction Expenditure	20,548	24,975	26,116	23,554
(B) Improvement Works	925	842	945	1,102
(C) Purchase of Computer Assets & Equipment	176	144	221	169
(D) Direct Costs and Overheads charged to Construction, Improvement Works and Computer Projects	1,854	2,512	2,681	2,867
<b>Total</b>	<b>23,503</b>	<b>28,473</b>	<b>29,963</b>	<b>27,692</b>

16. The Authority's proposed capital budget for 2000/2001 represents a decrease by \$2,271M ( about 8%) compared to the 1999/2000 Revised Budget. This is mainly due to a reduction in the average number of rental and HOS flats under construction, as explained in paragraphs 33 to 37.

### Development Fund

17. This is a separate account used to finance the development of housing and housing-related projects, infrastructure and community facilities. In accordance with the 1994 Supplemental Agreement to the 1988 Financial Arrangements with the Government, the amount held in this account is the excess, if any, of the Authority's total cash balance above the amounts required for the Housing Capital Works Fund plus normal working capital requirements.

18. The budgets for the Development Fund are summarized at **Table 4** below -

<b>Table 4 - Estimated Balance of the Development Fund (\$M)</b>		
	<b>Transfers to/(from) the Fund</b>	<b>Closing Balance</b>
1998/1999 (Actual)	(5,455)	3,116
1999/2000 (Approved Budget)	(3,079)	-
1999/2000 (Revised Budget)	(3,062)	-
2000/2001 (Proposed Budget)	7,875	7,854

19. The closing balance of the Development Fund is expected to be \$7,854M as at 31 March 2001 due to the net cash surplus of \$9,637M in 2000/2001. The detailed Budgets/Forecasts for the Development Fund are set out at Section 2.6 of the Budgets and Forecasts Proposal.

## **B. Budgets For Core Businesses**

### **Public Rental Housing**

20. The business is responsible for the allocation, management and maintenance of the domestic rental properties of the Authority.

21. **The financial objective of the business is to develop and manage each domestic rental estate i.e. excluding all commercial operations, at a return to generate sufficient funds to meet the operating expenses, including depreciation, over its economic life.**



22. The financial performance of the business for the budget periods is summarised below -

<b>Table 5 - Rental Housing Operating Account (\$M)</b>				
	<b>Actual 1998/1999</b>	<b>Approved Budget 1999/2000</b>	<b>Revised Budget 1999/2000</b>	<b>Proposed Budget 2000/2001</b>
Income	9,227	10,632	9,475	10,425
Expenditure	11,206	12,224	11,390	12,065
Operating Deficit	(1,979)	(1,592)	(1,915)	(1,640)

23. With the extension of various rent relief measures including rent freeze and waiver, the operating deficit for the 1999/2000 Revised Budget only shows a slight improvement of \$64M as compared to 1998/1999. The 2000/2001 estimated deficit is forecast to reduce to \$1,640M as a result of increases in rental income and various measures to contain costs.

### **Commercial Properties**

24. The business is responsible for the management and operation of the commercial properties of the Authority. The portfolio of properties can be broadly categorized into retail premises, car parking spaces, flatted factory premises and welfare/community premises.

25. **The financial objective of the business is to develop and manage each commercial property, on full commercial principles, with a view to achieving a specific return.**

26. The financial performance of the business for the budget periods is summarised below -

<b>Table 6 - Commercial Operating Account (\$M)</b>				
	<b>Actual 1998/1999</b>	<b>Approved Budget 1999/2000</b>	<b>Revised Budget 1999/2000</b>	<b>Proposed Budget 2000/2001</b>
Income	5,023	5,121	4,854	5,189
Expenditure	2,556	3,078	2,977	3,275
	<u>2,467</u>	<u>2,043</u>	<u>1,877</u>	<u>1,914</u>
Government Non- Reimbursable (GNR)	<u>225</u>	<u>288</u>	<u>493</u>	<u>466</u>
Operating Surplus	2,242	1,755	1,384	1,448

27. The operating surplus before GNR for the 1999/2000 Revised Budget is lower by \$166M compared to the Approved Budget as a result of the reduced income of \$267M due to the extension of rent freeze and rent re-assessment, offset by reduction in expenditure of \$101M. The rental income is estimated to increase by \$335M in 2000/2001 with new stock, to be offset by an increase of \$118M and \$115M in other recurrent expenditure and depreciation for new buildings and improvement works respectively.

28. GNR for 1999/2000 Revised Budget and 2000/2001 Proposed Budget is estimated to increase by 71% and 62% to \$493M and \$466M respectively compared to the Approved Budget mainly due to development cost for Tiu Keng Leng.

### **Home Ownership**

29. The business is responsible for the development, monitoring and review of measures to assist the lower-middle income families to become home owners through the Home Ownership Scheme/Private Sector Participation Scheme (HOS/PSPS), Home Purchase Loan Scheme (HPLS), Secondary Market Scheme (SMS), Mortgage Subsidy Scheme (MSS), Tenants Purchase Scheme (TPS) and the Buy or Rent Option (BRO).

30. The **financial objectives** of home ownership operations are summarised as follows -

- **To develop HOS estate as cost effectively as possible and to maximize the return to sustain the construction development programmes, HPLS and other initiatives.**
- **To make use of private sector resources to develop PSPS estates as cost effectively as possible and to maximize the return to sustain the construction development programmes, HPLS and other initiatives.**
- **To maximize the use of HPLS in increasing the home ownership rate commensurate with levels affordable to the Authority.**

31. The financial performance of the business for the budget periods is summarised below -

<b>Table 7 - Home Ownership Operating Account (\$M)</b>				
	<b>Actual 1998/1999</b>	<b>Approved Budget 1999/2000</b>	<b>Revised Budget 1999/2000</b>	<b>Proposed Budget 2000/2001</b>
Income	22,513	27,781	26,776	40,767
Expenditure	6,640	17,620	16,504	25,617
Operating Surplus	15,873	10,161	10,272	15,150

32. Income for the 1999/2000 Revised Budget of \$26,776M is less than the Approved Budget by \$1,005M. This is mainly due to the rescheduling of the sale programme and delay in Tin Chung Court's completion, which is partly offset by the sales proceeds of the BRO flats. The operating surplus for the 2000/2001 Proposed Budget represents an increase of \$4,878M compared to the 1999/2000 Revised Budget as a result of a higher number of HOS units to be completed and sold (26,638 for 2000/2001 as compared to 16,539 for 1999/2000).

## Building

33. The business is responsible for planning, design and building public housing and associated facilities as well as facilitating the PSPS projects.

34. The types of construction expenditure for the budget periods is summarised below -

	<b>Actual 1998/1999</b>	<b>Approved Budget 1999/2000</b>	<b>Revised Budget 1999/2000</b>	<b>Proposed Budget 2000/2001</b>
Housing Authority Projects	20,115	24,588	25,392	22,864
Government Non-Reimbursable Government Funded Projects	189	267	474	440
Direct Costs	244	120	250	250
Overheads	1,586	2,088	2,265	2,437
	49	187	71	71
<b>Total</b>	<b>22,183</b>	<b>27,250</b>	<b>28,452</b>	<b>26,062</b>

35. The construction expenditure remains at a high level during the peak production period for 1999/2000 and 2000/2001, with an average number of 184,000 rental/HOS units under construction. The Proposed Budget for 2000/2001 represents an 8.4% reduction as compared to the 1999/2000 Revised Budget and is mainly attributable to the lower level of flat production projected in the coming two years. The major decrease is in expenditure on rental housing and HOS projects of \$1,829M and \$858M respectively.

36. The amount incurred by the Authority for Government Non-Reimbursable shows a significant increase to \$474M and \$440M in 1999/2000 Revised Budget and 2000/2001 Proposed Budget mainly due to estimated payments for the Tiu Keng Leng development.

37. The construction budget also includes payments for consultancy fees of \$506M and \$339M in 1999/2000 Revised Budget and 2000/2001 Proposed Budget in respect of consultancy services for architecture, building, engineering and surveying.

## C. Budgets For Other Services

## **Agency and Management Services**

38. The scope of the services includes the following -

(a) **Agency Functions**

In accordance with the 1988 Financial Arrangements, the Authority is responsible for the Government, on an agency basis and with funds provided by the Government, squatter control, improvements to squatter areas and the clearance of squatters from land required for development.

(b) **Agency Management Services**

The Authority manages property on behalf of other parties and charges a management fee for the services rendered. This covers the management of TPS estates, supervision of the management agency for completed Home Ownership Courts without Owners' Corporations.

(c) **Supervision of Government Reimbursable Projects**

The Authority provides supervision of certain Government projects. This includes the building of schools or community buildings in new estates, additions, alterations, improvements and external maintenance of Government buildings in rental estates. As a standard practice, the Authority pays the contractors first and obtains reimbursement from the Government including full cost of the supervision services, although recently Secretary for the Treasury has issued instructions to Departments to revert to 2% rather than full cost recovery. This matter is now under negotiation between the Department and Secretary for the Treasury.

The total level of agency expenditure for 1999/2000 Revised Budget is \$625M and should be fully recoverable.

39. The financial forecasts for 2001/2002 to 2003/2004 are summarised at Section II of the Budgets and Forecasts Proposal for members' information only.

40. The five year summary of the operating results and cash position is set out at Table 9 below -

<b>Table 9 - Summary of Operating Results and Cash Position (\$M)</b>					
	Public Rental Housing	Commercial Properties	Home Ownership	Consolidated Operating Surplus	Cash Balance
1999/2000 (Revised Budget)	(1,915)	1,384	10,272	9,741	22,624
2000/2001 (Proposed Budget)	(1,640)	1,448	15,150	14,958	32,261
2001/2002 (Forecast)	(880)	1,777	11,912	12,809	40,338
2002/2003 (Forecast)	(831)	2,048	13,630	14,847	49,154
2003/2004 (Forecast)	(474)	2,284	18,106	19,916	60,371

## **SENSITIVITY ANALYSES AND OTHER FACTORS**

41. The results of our sensitivity analyses are summarised at Section IV of the Budgets and Forecasts Proposal. These analyses illustrate the impact on the Authority's overall operating surplus and cash flow with variations in major budget bases and assumptions. As the impact of such changes would be cumulative, the Authority should be able to detect an early warning of a potentially serious deterioration of funds.

42. The analyses cover the following changes -

- Increase in construction cost
- Property prices remain at current level
- No rent increase for public rental housing
- Increase in HOS discount rate
- Increase in HPLS quota

## CONSULTATION

43. The Authority's 1999/2000 Revised Budget, 2000/2001 Proposed Budget and the Financial Forecast for 2001/2002 to 2003/2004 were endorsed at the Finance Committee meeting on 13 January 2000, after detailed examination and discussion. The Budgets and Forecasts of the businesses have also been discussed and endorsed (as part of the Business/Service Plans) at the following business committee meetings -

<b>Committee</b>	<b>Paper No.</b>	<b>Date</b>
Building	BC 170/99	21 October 1999
Rental Housing	RHC 84/99	4 November 1999
Commercial Properties	CPC 63/99	4 November 1999
Finance	FC 60/99	18 November 1999
Human Resources	HRC 44/99	22 November 1999
Home Ownership	HOC 101/99	26 November 1999

## PUBLICITY

44. The Department briefed the media on the salient points of the budgets on 13 January 2000 while the FC meeting was in progress and a press conference was held after the FC meeting.

## ADVICE SOUGHT

45. This paper is issued for discussion at the next meeting of the Housing Authority to be held on 27 January 2000. Members are invited to **approve** the Authority's Revised Budgets for 1999/2000 and Proposed Budgets for 2000/2001 at Section I and to **note** the Financial Forecasts for 2001/2002 to 2003/2004 at Section II of the Budgets and Forecasts Proposal.

46. Following the Authority's approval, the 1999/2000 Revised Budgets and 2000/2001 Proposed Budgets will be submitted to the Chief Executive for formal approval in accordance with Section 4(3) of the Housing Ordinance.

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