The Disingenuous 2009-10 Budget

Stephen Ching[1]

August 6, 2009

"…. I will provide a full, clear and honest account of our economic prospects. Through clear appreciation of the troubles we face together, we will endure and overcome them together."
— Fourth Paragraph, the 2009-10 Budget

Introduction

The Financial Secretary claimed that Hong Kong stimulus package was "[e]vidently … stronger than those of many other economies". His claim is based on an overstatement of Hong Kong stimulus package by including two rounds of measures that were "already planned for" and not "crisis-related". Consequently, the cost of the package was overstated to be 5.2% of Hong Kong's GDP. On the other hand, he understated total discretionary measures of the G-20 nations by using dated data and excluding commitments already announced for 2010 by the G-20 nations. As a result, the cost of the G-20 nations' total discretionary measures was understated to be a weighted average of only 2.3% of their GDP. Had there been no such misstatements, the cost of Hong Kong stimulus package would have been only 1.8% of Hong Kong's GDP and that of the G-20 nations a weighted average of 4.0% of their GDP. The truth is completely distorted. The deceptive claim of the Financial Secretary is very disappointing.

Hong Kong "Stimulus Package"

After only 90 days of delivering the 2009-10 Budget[2], his second budget, the Financial Secretary announced additional relief measures of HK$16.8 billion on May 26, 2009.[3] The additional relief measures increased Hong Kong "stimulus package" to a total cost estimated to be about HK$87.6 billion, or 5.2% of Hong Kong's GDP. The "stimulus package" consisted of four rounds of measures spanning over two fiscal years from 2008-2010. In each of the two fiscal years, two rounds of measures were offered.

The first round of measures was launched by the Financial Secretary in his first budget (i.e. the 2008-09 Budget[4]) on February 28, 2008 and the second round by the Chief Executive at the Question and Answer Session in the Legislative Council on July

[1] I am grateful to Kam-Ming Wan and an anonymous referee for detailed comments. School of Economics and Finance, The University of Hong Kong, Pokfulam Road, Hong Kong; Email: steve.ching@hku.hk
[2] The 2009-10 Budget was delivered on February 25, 2009 (available at http://www.budget.gov.hk/2009/eng/speech.html).
[3] The "Additional Relief Measures" is available at http://www.legco.gov.hk/yr08-09/english/panels/fa/papers/fa0529cb1-1740-1-e.pdf.
[4] The 2008-09 Budget is available at http://www.budget.gov.hk/2008/eng/speech.html.

16, 2008.[5] The costs of the first and the second rounds of measures were HK$46.5 billion and HK$11 billion, respectively[6], so their total cost was HK$57.5 billion, or 3.4% (= 5.2% × 57.5 ÷ 87.6) of GDP.

The third round of measures was given in the 2009-10 Budget. A simple calculation shows that its cost was HK$13.3 billion (= HK$87.6 billion – HK$57.5 billion – HK$16.8 billion). Note that the third round of measures was outweighed by the fourth round of measures, i.e. the additional relief measures announced on May 26, 2009. These two rounds of measures together corresponded to 1.8% (= 5.2% – 3.4%) of GDP.

Comparison with G-20's Discretionary Measures

To compare Hong Kong stimulus package to those of other economies, the Financial Secretary made the following reference to an IMF report. "According to the report published by the International Monetary Fund in March, the average expenditure of the G-20 nations in this respect accounts for 2.3% of their GDP"[7]. Recall that Hong Kong stimulus package was estimated to be about 5.2% of Hong Kong's GDP. Hence, he claimed that Hong Kong stimulus package was "[e]vidently … stronger than those of many other economies"[8].

We track down the IMF March report referred by the Financial Secretary to be the Note on "Global Economic Policies and Prospects" prepared by the staff of the IMF for the meeting of the Group of Twenty Ministers and Central Bank Governors on March 13-14, 2009 in London.[9] The relevant figures from the IMF March Note are reproduced in Table 1 below.

Table 1. G-20 Countries: Discretionary Measures, 2008-10
(in percent of GDP) 1/

	IMF March Note 2/			IMF April Update 3/ 4/		
	2008	2009	2010	2008	2009	2010
Argentina	0.0	1.3	…	0.0	**1.5**	…
Australia	0.7	2.1	1.7	0.7	2.1	1.7
Brazil	0.0	0.4	0.2	0.0	**0.6**	**0.8**
Canada	0.0	1.5	1.3	0.0	**1.9**	**1.7**
China	0.4	3.2	2.7	0.4	*3.1*	2.7
France	0.0	0.7	0.7	0.0	0.7	**0.8**
Germany	0.0	1.5	2.0	0.0	**1.6**	2.0
India	0.6	0.6	…	0.6	0.6	0.6
Indonesia	0.0	1.3	0.6	0.0	1.3	0.6

[5] The "Opening Remarks by CE at Question and Answer Session in Legislative Council" is available at http://www.info.gov.hk/gia/general/200807/16/P200807160261.htm.
[6] See the third-last paragraph of the "Opening Remarks by CE at Question and Answer Session in Legislative Council".
[7] See the ninth paragraph of the "Additional Relief Measures".
[8] Ibid.
[9] The IMF March Note is available at http://www.imf.org/external/np/g20/pdf/031909a.pdf.

Italy	0.0	0.2	0.1	0.0	0.2	0.1
Japan	0.4	1.4	0.4	*0.3*	**2.4**	**1.8**
Korea	1.1	2.3	1.3	1.1	**3.9**	*1.2*
Mexico	0.0	1.5	…	0.0	1.5	…
Russia	0.0	2.3	1.6	0.0	**4.1**	**1.3**
Saudi Arabia	2.4	3.3	3.5	2.4	3.3	3.5
South Africa	1.7	1.8	–0.6	1.7	1.8	–0.6
Turkey	0.0	…	…	0.0	0.8	0.3
United Kingdom	0.2	1.4	–0.1	0.2	1.4	–0.1
United States	1.1	2.0	1.8	1.1	2.0	1.8
G-20 PPP-GDP weighted average	0.5	1.8	1.3	0.5	**2.0**	**1.5**

1/ "…" is used for countries for which no information is available on the size of their fiscal packages.
2/ Source: Table 1 in Appendix I on p.37 of "Global Economic Policies and Prospects"
3/ Source: Table 2 on p.5 of "Update on Fiscal Stimulus and Financial Sector Measures"
4/ A decrease in discretionary measures is highlighted in italics and an increase in bold.

Two observations are in order. First, the Financial Secretary only used the first two columns under the heading of IMF March Note, which show that the weighted average of discretionary measures of the G-20 nations was 2.3% (= 0.5% + 1.8%) of GDP in 2008-09. Second, the 2009 March data used by the Financial Secretary is dated. Indeed, an update of it was published by the IMF on April 26, 2009[10], exactly one month before the Financial Secretary did the comparison. The updated data is also reproduced in Table 1, under the heading of IMF April Update. Using dated data for comparison shows that the Financial Secretary is either ignorant or misleading.

A sensible comparison is apples to apples, oranges to oranges. According to both the IMF March Note and the IMF April Update, discretionary measures "reflect the budgetary cost of *crisis-related* discretionary measures in each year compared to 2007 (baseline), ….. They do not include (i) 'below-the-line' operations that involve acquisition of assets (including financial sector support) or (ii) measures that were *already planned for*" (emphases added). The latter condition excluded most measures launched prior to late 2008.[11] Note that discretionary measures in 2008 were significantly weaker than those in either 2009 or 2010.

It is problematic for the Financial Secretary to include the first two rounds of measures in Hong Kong stimulus package when comparing it to discretionary measures in the IMF March Note. Recall that the first round of measures was launched in February 2008 and the second round in July 2008, so they were "already planned for" by late 2008. Including them overstated Hong Kong stimulus package, relative to discretionary measures in either the IMF March Note or the IMF April Update.

[10] The "Update on Fiscal Stimulus and Financial Sector Measures" is available at http://www.imf.org/external/np/fad/2009/042609.pdf.
[11] Lehman Brothers filed for bankruptcy under Chapter 11 on September 15, 2008.

There is another reason the first two rounds of measures in Hong Kong's package were not comparable to discretionary measures of the G-20 nations. The first two rounds of measures were not "crisis-related". The Financial Secretary gave the following assessment to the first round of measures in the 2008-09 Budget. "[T]his will give some impetus to the overall economy although the effect will not be significant in 2008. … The impact of these measures will be felt in the medium to long term and will not have any short term economic impact. … these measures will not generate a lot of domestic demand in a short period of time. The stimulating effect on inflation should be limited."[12]

Clearly, the first round of measures was intended to minimize their short-term stimulating effect. This is against the nature of "crisis-related" measures, which are designed to generate immediate, effective impact. It is illuminating to compare how the Financial Secretary characterized "crisis-related" measures when the additional relief measures were announced on May 26, 2009. "[W]hen considering the new relief measures and their intensity, we want them to be forward-looking, simple and direct, … so that they can benefit the people as early as possible. The new measures should also be targeted, timely and effective …."[13]

Neither was the second round of measures crisis-related. This is how the Chief Executive rationalized the second round of measures when they were introduced on July 16, 2008. "Today … I think that it's time for immediate action because global oil and food prices have increased rapidly in the first half of the year. The drastic price increases … have upset the lives of Hong Kong people and our social harmony. Therefore, I have decided to announce some short-term relief measures today to alleviate the pressure on the grassroots and middle-class community as a result of high inflation."[14] The second round of measures was purely inflation-driven. Spinning them as "crisis-related" is to have your cake and eat it too. Indeed, the concern of inflation had been largely put aside by the G-20 nations when discretionary measures were being formulated.

Our analysis shows that Hong Kong stimulus package was overstated by the inclusion of the first two rounds of measures. To rectify the misstatements, these two rounds of measures need to be removed. Consequently, the cost of Hong Kong stimulus package only accounted for 1.8% of Hong Kong's GDP, or slightly above one-third (0.35 = 1.8% ÷ 5.2%) of the amount claimed by the Financial Secretary.

The Financial Secretary not only overstated Hong Kong's package, but also understated the G20 nations' discretionary measures. First, he used the dated data in the IMF March Note. Second, he excluded discretionary measures already committed by the G-20 nations for 2010. (Note that those committed by the Hong Kong Government for 2010 were already reflected in the 2009-10 Budget and the additional relief measures announced on May 26, 2009.) After correcting these two understatements, the cost of the

[12] See paragraphs 189-191 of the 2008-09 Budget.
[13] See the fourth paragraph of the "Additional Relief Measures".
[14] See the first paragraph of the "Opening Remarks by CE at Question and Answer Session in Legislative Council".

G-20 nations' total discretionary measures for 2008-10 increased to a weighted average of 4.0% (= 0.5% + 2.0% +1.5%) of their GDP, or almost one and three-quarter times (1.74 = 4% ÷ 2.3%) of the figure used by the Financial Secretary.

Either the overstatement or the understatement alone is a gross misstatement. Two wrongs don't make a right. They are even deceptive in this case. The overstated Hong Kong's package was 2.26 (= 5.2% ÷ 2.3%) times of the understated G-20 nations' discretionary measures (by percent of GDP). This is an outright contradiction to the fact that the G-20 nations' total discretionary measures were 2.22 (= 4.0% ÷ 1.8%) times of Hong Kong's package (also by percent of GDP).

Concluding Remarks

The Financial Secretary argued that he had offered a patently strong stimulus package to help Hong Kong overcome the once-in-a-century financial tsunami. Alas, the claim is not real. It is based on an overstated Hong Kong stimulus package and understated G-20 nations' discretionary measures. Hong Kong stimulus package was overstated by including non-crisis-related measures. The costs of the crisis-related measures and the non-crisis related measures accounted for 1.8% and 3.4% of Hong Kong's GDP, respectively. It is absurd that the crisis-related measures in 2009 were even weaker than the non-crisis-related measures prior to late 2008. Ironically, we had counted on the government for strong doses of medicine during late 2008 and the first half of 2009.[15]

Food for Thought

We end this article with a counterfactual analysis. How much would it have costed the government to offer a genuine package that were "evidently stronger than" the G-20 nations' total discretionary measures?

A back-of-the-envelope calculation shows that such a package is around 2.25[16] times of the G-20 nations' total discretionary measures (by percent of GDP), so it will be 9% (= 4% × 2.25) of Hong Kong's GDP or HK$150.5 billion, corresponding to one-third of Hong Kong's fiscal reserve!

Putting money where the Financial Secretary's mouth is would have costed the government not only a fortune, but also a violation of the budgetary guideline of limiting public expenditure to less than 20% of GDP and even the principles of prudent management of public finances stipulated in Article 107 of the Basic Law. Nonetheless, making a deceptive claim is inexcusable. Engineering a financial shenanigan by the Financial Secretary is an accounting scandal of the government.

[15] "Below-the-line" operations that involve acquisition of assets (including financial sector support) were not considered as discretionary measures by the IMF.

[16] We pick a number between 2.22 and 2.26 for ease of calculation. The latter two numbers are obtained at the end of the previous section.