

Hong Kong Freedom

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In fifty years (1947-1997) Hong Kong grew from being one of the poorest to one of the richest places in the world.

GDP *per head* grew from less than 20% of Britain's in the early fifties to 120% of Britain's by 1997.

Real GDP averaged 6% annual growth in the final fifteen years of British rule 1982-97 and was even faster in earlier periods.

HONG KONG SEEMED TO HAVE EVERY DISADVANTAGE:

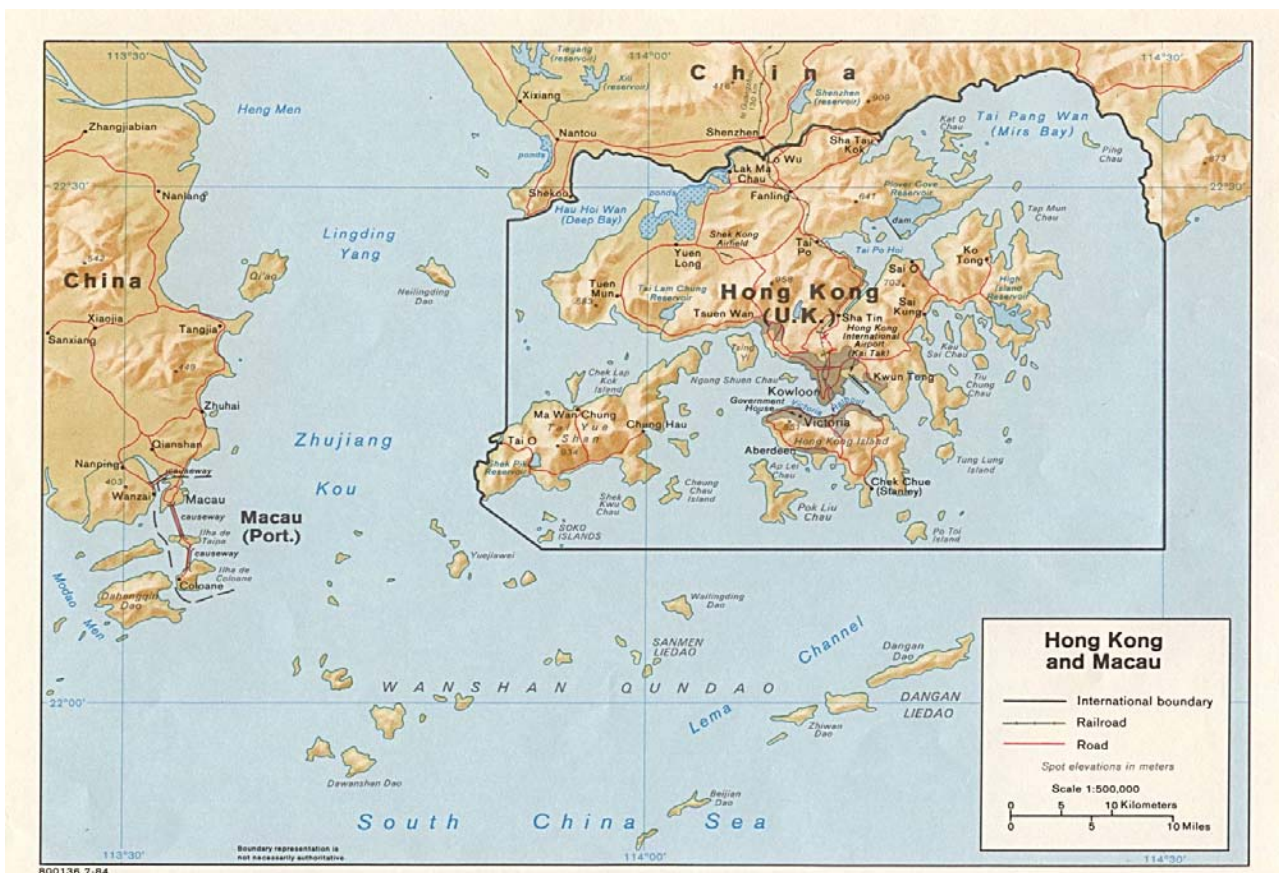
1. No Natural Resources (not even enough water)
2. Over-crowding (over six million people in 440 square miles - smaller than Rhode Island)
3. Geographical isolation, far from its trading partners
4. A hostile neighbor (Communist China)
5. A colonial government (in other words an undemocratic dictatorship)

BUT IT HAD SOME ADVANTAGES, WHICH WERE MUCH MORE IMPORTANT:

1. The impartial rule of law
2. Secure property rights
3. Free trade
4. Low taxation

IN OTHER WORDS, THE PEOPLE OF HONG KONG HAD **FREEDOM**, EVEN THOUGH THEY DIDN'T HAVE DEMOCRACY.

- Hong Kong ranks #1 in economic freedom among all countries measured in the annual *Index of Economic Freedom* sponsored by the Heritage Foundation and the Wall Street Journal.
- Milton Friedman and others have described Hong Kong as one of the freest markets in the world.



WHY WAS HONG KONG SO FREE?

- At two key periods in its history, (the 1840s and 1940s) events helped it be free.
- Entrenched indigenous interests were weak (the majority of people were newly arrived refugees).
- It was a colony, so electoral (pork barrel) political processes were absent.
- The ethics of the top colonial administrators (incorruptible, frugal, modest) and their cultural tradition (British common law) favored freedom.
- Debt free and running government surpluses, the Hong Kong government could afford to shrug off political pressures from Britain.

The most important colonial administrator in this respect was the Financial Secretary (Treasurer) from 1961 to 1971, Sir John Cowperthwaite.

- Son of a Scottish tax collector (like Adam Smith)
- Highly educated, (two degrees from Cambridge and London Universities).
- Brilliant and powerful debater
- Strong believer in the free market and minimal government
- Aggressive defender of freedom against social activists, special interests and well-meaning fools.

Among other things he warded off subsidies, tax breaks, regulations and government construction projects.

As a result, Hong Kong's economy was remarkable in many ways.

LOW TAXATION

1. No tax on foreign earnings. No tax on dividends. No tax on interest income. No tax on capital gains. No sales tax or Value-Added Tax. No excise taxes (taxes on imports or exports) on most goods with the exception of tobacco, alcohol and petrol.
2. Low tax rates on salaries. (The *maximum* rate was 12.5% until 1966, then 15%).
3. Low tax rates on corporate profits, (15%).
4. Very high person exemptions from salary tax. (In 1970, the personal tax exemption in Hong Kong was nearly triple the exemption in the UK and double the exemption in the US, despite having average wages of less than half of the US).
5. As a result, **98% of the workforce paid no tax at all** in the sixties.

LOW GOVERNMENT EXPENDITURE

1. In the sixties total government expenditure averaged about 13% of GDP, about a third the size of total government in the US today. In Sir John Cowperthwaite's last year, 1970, the government was down to 11.5% of GDP.
2. Government employees were less than 5% of the workforce.
3. The government ran budget surpluses in almost every year, and therefore was able to eliminate taxes and simplify the tax code from time to time.
4. The government had no debt. In fact the government *earned* substantial net interest income and rents on its accumulated assets.
5. The Hong Kong dollar, (like the Swiss Franc) was more than 100% backed with foreign currency reserves.

PUBLIC SERVICES WERE RUN AT A PROFIT

The Government provided water (some of it piped in from China) ran the railway and the airport and owned land. All these activities were run profitably. No cross-subsidy of various activities, market pricing was used as far as possible.

SOCIAL WELFARE WAS LIMITED

- All Primary Schools (until 1970) charged (low) fees. All secondary schools charged fees. Primary schooling was not compulsory until 1970.
- Some hospital and clinical services were subsidized.
- A *very* small disability payment was made to those unable to work, or those over seventy years old.

- There was one very big exception. **Large scale provision of public housing.** Nearly half the population lived in subsidized government-built apartment blocks. (This was not a success, and failed in its supposed social purpose.)

MINIMAL REGULATION

- No regulation of foreign exchange transactions, stock brokers or insurance.
- Until the mid sixties, no restraint on the number of banks or banking transactions.
- No minimum wage and no rules governing hiring and firing of employees. No regulation of workplace conditions.
- An exception was land use regulations, including a building code. Unwittingly this caused volatility in the real estate market.

THE RESULTS:

- Very low unemployment... about 2%.
- Very high savings and investment rates
- Real wages rose over 4% per year during Cowperthwaite's tenure even though the population grew by 3% per year.
- It has been estimated that in the late sixties industrial production was growing over 15% per year and GDP was growing over 12% per year.
- During the Cowperthwaite decade, 1961-71 domestic exports compounded at 13.8% per year.
- Total bank deposits grew 19% per year.
- Significant private and voluntary welfare activities. Chinese 'associations' such as the Po Leung Kok. The largest single donor to welfare services was the Royal Hong Kong Jockey Club... recycling its profits from gambling.

By 1997 Hong Kong had life expectancy rates, health statistics and crime statistics as good as and in some cases better than in Britain or the United States.

HONG KONG TODAY

- Beijing appointed chief executive instead of a British colonial governor
- Promise by Beijing to respect Hong Kong's laws and autonomy until 2047 at least
- Collapse in property prices (fell over 65% since 1997)
- Fall in consumer prices (by nearly 20% since 1997)
- Fall in wages... even of government workers
- Fall in government revenues
- Government spending increased as a portion of GDP (doubled since the sixties)
- Education, Health and Welfare now consume over half the budget and continue to grow.
- Government dabbling in real estate projects (for example, an industrial park)
- Large government deficits (up to 6% of GDP) in most years and government debt issued
- Proposal to introduce a sales (VAT) tax
- Over 50% of population now pay taxes.
- Minimum wage introduced
- High Unemployment - 8% at its recent high
- Mass street demonstrations against government policies, such as the anti-secession Act.
- Per capita real GDP growth averaged only 1.5% per year since 1997 versus 3.6% in the prior decade. As a result Britain's per capita GDP has overtaken Hong Kong again.