Squaring the welfare circle of the Hong Kong Special Administrative Region – Lessons for governance in social policy

Chack Kie Wong

6,577

Abstract
This article sees how the Hong Kong Special Administration Region Government squares the welfare circle. Due to institutional pathway of the established welfare system, it is not successful in either reducing public expenditures or raising taxes. The article argues that it is important to look into the role of institutional design in the management of public expectations.

Key words: squaring welfare circle, governance, welfare state, managing public expectations, welfare institutions.

Introduction
This article looks at governance in social policy in the post-1997 era in the Hong Kong Special Administrative Region of China (hereafter Hong Kong SAR or before 1997, Hong Kong). It assesses the abilities of the Hong Kong Special Administration Region Government (hereafter the SAR Government) in striking a proper balance between rising demand for social services and benefits on one hand, and the simultaneous demand for limiting public expenditures on the other, whilst maintaining popular legitimacy. A number of authors use the term ‘squaring the welfare circle’ to describe the challenges that governments in the West’s affluent societies are now facing. In George and Miller’s view, the term is used to convey the message of the continual and intensifying struggle of governments in all advanced industrial

societies to harmonize the need for meeting the constantly rising need and demand for social service provisions and benefits and meeting simultaneous demands for limiting public expenditure.2

The background of the squaring the welfare circle dilemma is the drastic social and economic changes that the welfare states are facing: population ageing, labour market change, economic globalization and weakened families. All these social and economic changes have put pressures on the welfare states into a state of ‘permanent austerity’3 due to falling rates of growth, reduced scope for tax increase and the belief that tax rises undermine work, savings and investment incentives.4 The ability to square the welfare circle is basically not only about resources, but also the management of the public expectations of those who have already become vested interests of the current system. This is to suggest, there is likely an institutional pathway or path dependency once a welfare system or welfare state is established,5 albeit in our case, a non-western neo-liberal welfare state with comparatively small public social expenditure. In other words, it is important to pay attention to the squaring of the welfare circle challenge as public demands for social services and benefits are unlimited and citizens

---

2 See George, V. and Miller, S. p.1.


would become strong defenders of the status quo. Hence, governance plays an important role in terms of managing public expectation and designing welfare institutions in the ways which can harmonise right with responsibility.

Social policy is referred to the social actions taken by policy-makers for improving human well-being or welfare. The major program tools of social policy, that is state’s social actions, are the ‘big five’ of social services – education, health care, housing, personal social services and social security. In the Hong Kong SAR, personal social services, that is, social welfare services and social security are classified under the category of social welfare. Social actions require financial support. In the case of governments, they have to extract resources from society, particular from the economy; here comes the issue of the squaring of the welfare circle. According to George and Taylor-Gooby, there are two major perspectives of how governments in the western affluent societies respond to this challenge.

The first perspective suggests that the welfare circle challenge is a zero-sum game; therefore, governments can either increase taxation or cut provision; or a combination of both. They find governments in the UK and the USA follow this perspective in responding to the welfare circle challenge. The second perspective has a positive assumption about the relationship between social policy and the economy – some forms of welfare expenditure are conducive to stronger economic growth, they have an investment function, and are able to increase the resources available for redistribution. According to this complementary view of social policy to the economy, education and labour market policy, and even family policy can be designed to enhance economic competitiveness. They find governments in Europe, the Nordic countries in particular, with this optimistic view about the welfare circle challenge.

These two perspectives towards the welfare circle challenge reflect country divergence, not convergence, despite structural social and economic forces are similar and constant. In

---

this light, it is worthwhile to know how non-western welfare states square the welfare circle. In this study, we look into the case of Hong Kong SAR, an affluent Chinese society in the Asian Pacific rim, to see which response pattern it adopts in the squaring of the welfare circle, despite the fact that it does not have a mature welfare state. Its experiences are valuable, not only of the reason mentioned above, but also culturally it is part of a larger Confucian tradition. Accordingly, the Chinese people of Hong Kong are assumed to have a self-reliance ethos which is supposed to constrain demands for social services and benefits. In other words, it is easier for the SAR Government to square the welfare circle as compared with advanced countries in the West. How far is this true?

We shall have the following organization for the paper. Firstly, it looks at the main features of Hong Kong’s welfare system. This will provide an understanding of the heritage of the present welfare system and how its institutional features affect the later development. Secondly, it examines the efforts of the SAR Government for squaring of the welfare circle in the Post-1997 era. Lastly, it discusses the dilemmas and difficulties on the part of the SAR Government to square the welfare circle.

**Main features of the Hong Kong’s neo-liberal welfare state**

Walker and Wong conceptualized Hong Kong as a neo-liberal welfare state on the basis of their analysis of social policy before the 1997 sovereignty handover. Here, this paper refers Hong Kong’s welfare system as a welfare state. A state is a political entity; a welfare state is that political entity with welfare features. We refer to Briggs' classic definition of welfare state here:

---


a welfare state is a state in which organized power is deliberately used in an effort to modify the play of the market forces in at least three directions – first, by guaranteeing individuals and families a minimum income irrespective of market value of their work or their property; second, by narrowing the extent of insecurity by enabling individuals and families to meet certain ‘social contingencies’… which lead otherwise to individual and family crises; and third, by ensuring that all citizens without distinction of status or class are offered the best standards available in relation to a certain agreed range of social services.9

What we unveil in below about Hong Kong’s welfare system shows these features of a welfare state. A neo-liberal welfare state is one which typically provides minimal state welfare. When public services and benefits are provided, they tend to be strictly means-tested and confined to those who are the less fortunate. In other words, the average persons living in a neo-liberal welfare state have to rely upon their own arrangements, for example, through consumption in the private sector or mutual support of family members, for meeting their welfare needs.

However, a neo-liberal welfare state can provide beyond minimum state welfare if social policy is in favor of economic growth. In the case of Hong Kong, social policy with such a characteristic receives higher priority. For example, is it not interesting to see that Hong Kong’s pre-1997 welfare system had free and universal basic education. This was primarily because education was regarded as essential for economic growth; it had an investment function. Even in post-compulsory levels, i.e., upper secondary education and above, the government also provided substantial subsidies to students. For example, university tuition fees were set at 18 percent of the full cost; students from low-income households could also apply for loans and grants. This provided an institutional environment where no one in Hong Kong was denied educational opportunities simply because of a lack in means. The Hong Kong SAR also inherits this social policy legacy.

Pre-1997 Hong Kong also had a British-style National Health Service in place, which

---

provided basic health care to its people at low cost. The basic structure of universal health care was set in the mid-1960s when the Colonial Government knew from a survey report that half of the respondents could not afford the fees and charges at public clinics, and another eighty percent of them could not do so at public hospitals.\textsuperscript{10} The policy of providing public health care at low cost was then established; such a policy was considered essential for enhancing labour productivity and promoting economic growth. The implication is clear: fees at public health care were extremely low and could be basically regarded as a free provision, especially in the case of hospitalization. For example, a government report in 1993 found that patients at an in-patient general ward received 90 percent to 98 percent in subsidies.\textsuperscript{11} Apparently, this health care institutional legacy inherited from the Colonial era has become a source of dilemma for the SAR Government – rising expectations fuel the rise in health care costs, as yet there is inadequate built-in financing mechanism, which, except for long-waiting times, thwarts misuses and abuses.

Public housing was another social policy that had a strong economic flavor in colonial Hong Kong. The Housing Authority, a statutory body established in 1973, is responsible for planning, building, and managing all public housing programs for the government. One important structural force for building massive public housing, especially in the case of rental flats in the colonial age, was for the supply of stable and cheap labor for industrial production.\textsuperscript{12} In this regard, rents could be regarded as an indirect production cost – its low

\textsuperscript{10} Hong Kong Government, Development of Medical Services in Hong Kong (Hong Kong: Government Printer, 1964).

\textsuperscript{11} Hong Kong Government, Towards Better Health, A Consultation Document (Hong Kong: Government Printer, 1993).

levels helped provide a favorable economic environment where labour did not need to ask for higher wages, if other factors were constant. The medium rent-to-income ratios of households between private housing and public housing were illustrative: around 26 percent for the former and 9 percent for the latter in 1997, respectively. The difference represents a social wage for the public housing tenants and a social cost that society must pay. In other words, public rental housing is redistributive, but this social equality function is latent – it does not work through the tax system, traceable in public finance, but is disguised as a means-tested state provision. Hence, the progressive, egalitarian nature of public housing, rentals in particular, did not attract opposition from neo-liberal economists and property developers in society. It was only in the Hong Kong SAR era when the then Chief Executive of the SAR Government, Mr. Tung Chee-Hwa, initiated the policy of building 85,000 housing flats annually that invited strong criticism from property developers. The public housing and home ownership schemes, in particular, were successfully that the public sector always intruded the interests of the market. This led to the eventual withdrawal of the policy and the end of building home ownership schemes in 2002.

Apart from social policy as a function of economic growth, the other defining feature of a neo-liberal welfare state is its anti-redistribution stance. Social security captures this important feature of Hong Kong in its pre-1997 era. The main program in social security is Comprehensive Social Security Assistance (CSSA); which is means-tested income maintenance program, provides a safety net for those who cannot support themselves financially. The Scheme is designed to bring the income of such individuals and families up to a prescribed level to meet their basic needs. CSSA is basically a social assistance or poverty relief program; but in mature welfare systems like those of the West, the defining social

---

13 Hong Kong Housing Authority, *Housing in Figures, 2000 edition* (Hong Kong: Information and Community Relations Section, Hong Kong Housing Authority, 2000).
security program is usually its retirement benefits scheme, and which is basically a pay-as-you-go system, meaning that there is an intergenerational redistributive element in retirement protection.

The choice of retirement protection in 1995 for Hong Kong by the Colonial Government is a case which reflects the neo-liberal values underlying Hong Kong’s welfare system. The Mandatory Provident Fund (MPF) is an employment-based forced savings scheme; it helps employees save money, with matching contributions from employers for retirement protection. The alternative option is a state pension that is supposed to benefit all people, not only employees. In principle, a state pension, primarily a pay-as-you-go system, has the following redistributive functions – intergenerational, between retirees and the working population; inter-class, between high income and low income groups; and across employment status, between employees and non-working persons. Apparently, these redistributive functions were not in line with the orthodox underlying the neo-liberal welfare state of colonial Hong Kong. Its rejection should not be surprising simply on this rationale. But MPF also has an important economic objective – it is a means to develop Hong Kong’s financial market and to socialize the whole working population to investment activities. Therefore, MPF fitted perfectly well with Hong Kong’s neo-liberal welfare state in its pre-1997 era.

The social policy programs briefly outlined above sound substantial and comprehensive. Social services and benefits ranging from health care to housing, education to income maintenance should apparently be able to meet the basic needs for daily living. More than that, due to rising economic standards, people, East and West, expect more from the welfare state. It is particularly obvious in the cases of two major universal social services – health care and education – people in the Hong Kong SAR expect the best possible standards offered to all.

---

But a comparative perspective highlights the inadequacy of the Hong Kong SAR’s neo-liberal welfare state due to its comparatively limited budget. Take, for example, social expenditure of the Hong Kong SAR as a percentage of GDP in the second year of the new millennium, i.e., 11.7 percent in 2001, was a little bit lower than the OECD average of 13.1 percent in 1960, but is comparable with those of Norway, Ireland (both 11.7%), and USA and Australia (both 10.9%) in that year (Table 1). In other words, the welfare state Hong Kong SAR has is not a mature one, as compared with those of the western advanced economies, at least in public social expenditure terms – it is forty years behind in this respect.

【Insert Table 1 here】

Even at this level of provisions and benefits, the neo-liberal welfare state does not have a reliable and sustainable fiscal base for supporting it. It has relied heavily upon growth dividends for its funding, especially from the huge revenue of land sales and property taxes. For example, land sales were 13 percent (or HK$27.1 billion, HK$7.8=US1.0) of government revenue in 1996-97. But it shrunk to 2.6 percent (or HK$2.5 billion) of the SAR government’s operating revenue in 2003-04 15 – the year when the Hong Kong SAR had the SARS outbreak and its economy fell substantially. As such, revenue from land sale is unstable, subject to economic fluctuations; the worst is that, it is needed when it is in least supply. Clearly, land sale is also a good proxy for economic growth. Moreover, the Hong Kong SAR has also relied upon property taxes more than many other countries for revenue.16 For

16 KPMG, Tax Base Study for the Hong Kong Government Advisory Committee on New Broad-based Taxes, Hong Kong, (Finance Bureau, Government of the Hong Kong SAR, 2001), pp.38.
instance, a government-commissioned tax-base study found that tax on property was 5 percent and 10 percent of tax revenue in 1997-98 in OECD and Asia Pacific countries, respectively, whilst the corresponding figure for the SAR was 24 percent.17

Now we turn to the supply side of the welfare circle. Does the Hong Kong SAR have a sound fiscal base for supporting its welfare state? The neo-liberal welfare state sketched earlier depicts a picture of nearly all non-contributory social services (e.g., health care and education) and benefits (e.g., social assistance), with the exception of the recently introduced MPF and public housing (still subsidized). From a financial sustainability perspective, this is definitely unhealthy. The Hong Kong SAR’s welfare state does not have a secure and sustainable fiscal base. Apparently, the following features attribute to this phenomenon:

Firstly, Hong Kong SAR has a low-tax regime: 17.5 percent for a corporate tax rate and 16 percent for income tax.18 A 2006 government consultation document on tax reform reveals how narrow is Hong Kong SAR’s tax base - only 1.2 million out of 3.4 million employees paying salary taxes; the top hundred thousand taxpayers contribute 60% of the salary taxes.19 In other words, the majority of the population does not pay salary taxes; they do not see a personal financial responsibility, but do feel they have a right to the expansion of the welfare state.

Secondly, fees and charges for social services, health care in particular, are set at low levels that do not allow for substantial cost-recovery. This financial structure fuels abuses and

17 Task Force on Review of Public Finance, Final Report to the Financial Secretary, Hong Kong, (Finance Bureau, Government of the Hong Kong SAR, 2002).
19 Financial Services and the Treasury Bureau, Broadening the Tax Base Ensuring our Future Prosperity, Consultation Document. (Hong Kong: The Government of the Hong Kong Special Administration Region, 2006). P.4
poses an inherent obstacle for quality service. It will attract more demand to a level beyond their coping capacity.

Thirdly, the way the social security system is financed in the Hong Kong SAR has added pressure on government revenue. Its retirement plan, the MPF, is basically a personal savings scheme that does not have any inter-class or inter-generational redistribution functions. In other words, the poor and the low-waged will have to rely upon social assistance for old age income protection. The high percentage of CSSA beneficiaries being old age persons is a cause for concern. Here we see a dilemma in terms of the institutional design for old age protection. The choice of personal savings by MPF, instead of a pension scheme, seems to be the right thing to do from the neo-liberal perspective, however, it takes a long time to bring the neo-liberal system out of this dilemma – as now large number of citizens entering old age without private means and have to rely upon social assistance. Further, the lack of unemployment insurance has forced unemployed people to rely upon CSSA for income support. This adds further pressure on the means-tested non-contributory social assistance scheme.

All of these features underscore important beliefs about the Hong Kong SAR’s neo-liberal welfare state. First, means-tested social services and benefits such as CSSA and public housing are for the poor, whilst universal services such as education and health care are perceived as social services for all. The former attracts less public support than the latter. Second, universal social services have stronger public support not only because of their wider

---


coverage scope, but also because they are associated with economic development. This is a primary feature of a neo-liberal welfare state. In other words, the structure of public support for social policy in the Hong Kong SAR is partly explained by its function for economic development. Third, most of the population is not tax-payers or insurance subscribers for the services and benefits they enjoy; if they do pay, the fees and charges are low. Hence, the fiscal side of the welfare circle is seldom a concern to the users and the general public – they delegate the responsibility to the government. Finally, the provision of social services and benefits are regarded as a business for the government, not that of the public. These popular beliefs are divisive, instrumental, and do not foster a society where social obligations and empathy for the poor and the vulnerable are part of its culture.

Apparently, these popular beliefs also engender a classical moral hazard mentality – strong in right but weak in responsibility - on the part of the users and the general public. Nevertheless, a local empirical study of social citizenship found that Hong Kong Chinese are generally “right-deficit” at the practice level because they also expect themselves to have similar or more responsibilities in many social rights such as the rights to a job, a basic living, a basic education, and child care. However, the subjective indicators depicted in that study may reflect the inadequate social rights people enjoy in a neo-liberal welfare state; it does not specifically address the issue of its narrow and weak fiscal base.

The efforts of the SAR Government to square the welfare circle

In terms of squaring the welfare circle, the SAR Government has performed in a mixed manner. It had increased social expenditure in the post-1997 era, both in absolute amounts and as a percentage of total public expenditure, except in the case of housing if we use 1997-98

---

and 2004-05 as the comparators (Table 2). Social welfare received the largest percentage gain in the same period, from HK$21,710 million to HK$34,119 million; seconded by education, from HK$47,027 million to HK$55,732 million, representing respectively 57.2 percent and 18.5 percent rises over a period of seven financial years. The large rise in social welfare was largely due to social assistance benefits payments, an open-ended entitlement primarily for the old age poor, the unemployed, and the single-parent family. The only decrease was in housing, that is 20.8 percent between 1997-98 and 2004-05, was primarily a result of the abandonment of massive housing building projects from 1999-2000 by the SAR Government due to a serious property market slump in the period; housing expenditures peaked in that year and began to decrease. However, it was able to reduce the civil service establishment from some 198,000 in 2000 to about 160,000 by March 2007.

Moreover, the SAR Government’s substantial increases in social expenditure should be placed against the background of continued budget deficit in the same period of time. In the
first eight years of the SAR period, 1997-98 to 2004-05, the SAR Government had incurred budget deficits for five years, with the largest rate of minus 5 percent of the GDP in 2001-02 (Table 3). In other words, in spite of the overall economic downturn and fiscal deficit, the SAR Government still committed itself on more spending for social policy. Nevertheless, when the economic picks up again, for example in 2004-05, the SAR Government was able to restore fiscal balance.23

【Insert Table 3 here】

But, people expect more from the SAR Government. The followings are two cases illustrating the dilemmas facing the SAR Government. In 2004, a few public housing tenants filed in the courts for rent cuts because the overall median rent to income ratio had exceeded 10 percent, a standard set in 1997 by the legislature in an inflationary economic environment.24 In a deflationary environment, public housing tenants should change their expectations. Evidently, this was not the case - they brought their lawsuits against the Housing Authority, not only about the expectation generated from the 1997 legislation, but also from a reflection of their personal hardship due to the overall economic downturn. For example, 5.7% of the full-time employees earned less than HK$5,000 a month in the third quarter of 2005.25 That is in general regarded as a working-poor wage. From their perspective, whether or not public housing finance could be sustainable after a rent cut was not a concern. Apparently, they did not see a responsibility in them for sustainable public housing finance. If expectations of this kind with the SAR Government continue, the welfare circle can hardly be


24 Wen Wei Po, (Hong Kong, China), November 23, 2004: Hong Kong Standard, (Hong Kong, China), November 23, 2004.

squared. The Court of Appeal’s ruling was in the favor of the authority – it decided that the Housing Ordinance does not impose a duty on the authority to carry out a rent review every three years, or to keep rents below 10 percent of median household income. In other words, the Housing Authority was allowed to carry out a flexible rent system for sustainable development.

The second case is about listing of public property. When the Housing Authority decided in July 2004 to list its shopping malls and car parks by means of a real estate investment trust in the local stock exchange, it was once again faced with legal challenges. Two elderly public housing tenants, both were welfare recipients, had sought an injunction to block the listing. They alleged that the authority’s disposal of shopping malls and parking space was a breach of the Housing Ordinance. Underlying their litigation was the worry that the sale of public assets might affect their interests – they had to pay a higher price for goods and services as the new management had the incentive to raise rents of shopping malls. Due to their injunction, at the end, the authority had to delay the listing of HK$21.9 billion of its assets until the end of 2005.

These two cases indicate the dilemma facing the SAR Government – it was not very successful in terms of managing the expectation of the people, especially those who are welfare beneficiaries, in a way which is compatible with the new economic and fiscal realities. In other words, governance in social policy, in the case of the SAR Government, is not simply a matter of adequate social resources. It is a matter of how well a social welfare system can be restructured to deal with the problems and the challenges of the time, and how well people’s expectations with the government can be moderated. The litigations on rent cut and listing of government property assets are a case in point. Evidently, the SAR Government does not have strong political legitimacy, despite its strong financial commitments for social policy in an economic downturn environment. But the larger spending in social policy cannot be
maintained in the long run. Insofar, it has been supported by the reserves cumulative over the pre-1997 era, primarily from land sale revenues. The economic growth in 2004 through 2006 did give more breathing space for the SAR Government; for example, it had a surplus of HK$12 billion in 2004-05; however, if discounting the proceeds from the issuance of government bonds, there would be a deficit of HK$13.4 billion. In the long run, the SAR Government needs to take up squaring of the welfare circle challenge. In this regard, the SAR Government raised the idea of introducing a Goods and Services Tax (GST) in mid-2006 with the intention to broaden the tax base. But it failed to convince the public that this was the right option for broadening the tax base – due to strong opposition, the SAR Government declared retreating from advocating GST in early December 2006, at a time nearly four months before the end of the consultation period.

In our view, the dilemma facing the SAR Government is three-fold.

First, it has to meet the basic needs of its people arising from worsening poverty, a widening income gap, population ageing, unemployment, broken families due to rapid social and economic changes, and many other serious social problems. Many of these problems are structural and have tremendous implications for social policy. For instance, according to the 2001 census, the lowest 40 percent household owned only 11 percent of the total household income, whilst the top 20 percent owned 56.5 percent of the respective share. Apparently, many low-income households have to rely upon social services and benefits for basic living; hence, any fee and charge rise in public and social services are likely to be fiercely resisted.

---


The fee charging of patients admitted to public hospitals’ casualty wards is a case in question. A nominal fee of HK$100, out of a cost of HK$570, was introduced in late 2002 which attempted to halt the misuse or abuse of this public health service. However, it was still once strongly opposed by patient advocacy groups. They argued that the introduced fee charging would deter the poor and long-term illness patients from seeking medical consultations.

The coming of Hong Kong SAR as an ageing society is another structural social change that has significant implications for social policy. The number of persons of 65 years and above reached 11.7 percent in 2003, and it is forecasted to rise to 27 percent by 2033.29 Clearly, an ageing population will add pressure on social policy for health care and income protection, while at the same time the labour force will decline and will result in reduced revenue. Take the case of income protection for example. Nowadays, more than half of CSSA cases come from old age persons. This is a phenomenon which is unique in advanced countries where the main recipients of poverty relief are usually single-parents and low-income families. The underlying reason is clear that the Hong Kong SAR does not have a state pension. The newly introduced Mandatory Provident Fund is a personal forced savings scheme which needs time for participants to accumulate adequate income for protection. This retirement protection model does not offer income support for the present-day old aged persons. Henceforth, they have to rely upon government poverty relief. This explains the high percentage of old aged persons on CSSA, as we mentioned above. In the long run, due to the scheme’s personal savings nature, it is quite clear that low-income workers and non-contributors such as housewives have to look for social assistance when they get older.

There is more to the list. But the point is clear that rapid social and economic changes, such as a widening income gap, rising unemployment and the working poor, are structural and hostile to a government with a limited budget and especially against a shrinking economy.

Second, the SAR Government has to restructure social service provisions and benefits for reducing costs and for enhancing competitiveness for the economy. Social services and benefits cannot be isolated from the need of the economy. Restructuring social policy is part of a larger economic restructuring. \(^{30}\) For instance, the review of the CSSA is a case in question. It was implemented in June 1999, with the aim to provide assistance to the needy without reducing their incentive to work. \(^{31}\) Its Support for Self-reliance component is in fact a *workfare* program, or disciplinary welfare, as one authority describes it, \(^{32}\) which requires the employable recipients to seek jobs and to perform community services in exchange for benefits. The standard benefit rates were cut to ensure that they were not better off than citizens who were employed. \(^{33}\) The implication is clear – the employable recipients are “encouraged” to seek jobs, hence, wages at the lower end of the labor market were driven down.

Despite the SAR Government’s efforts to restructure social policy, expenditures for social assistance benefits keep rising. For example, despite the fact that old age persons on CSSA declined from 57.3 percent of the total cases in 1997-98 to that of 50.7 percent in 2004-05, their absolute caseloads rose from 112,067 to 150,399, respectively (Table 4). In fact, the declining share of old age persons on CSSA was taken up by the respective increases in the categories of single-parent families and the unemployed, which rose from 8.8 percent and

\(^{30}\) See Chau & Wong, (2002).


9.8 percent in 1997-98 to 13.4 percent and 14.9 percent, in 2004-05, respectively (Table 4).

It is clear that the structure of expressed needs has changed especially in the case of the unemployed and single-parent families; these categories of people have to rely upon public welfare primarily due to economic restructuring. In this regard, despite the cuts in standard rates of CSSA and the workfare initiatives, as mentioned earlier, CSSA expenditure has increased from HK$9,441.3 million in 1997-98 to HK$17,631 million in 2004-05 (Table 4). This represents an 86.7 percentage hike in a period of seven years. In a similar vein, the SAR Government’s reform initiatives in education were fueled by increases in respective spending. The successful case - slower growth in social expenditure, not of revenue reduction – was in public housing. It was, ironically, not a factor of deliberate government effort, but was largely a result of lower production costs in a deflationary environment and the abandonment of massive housing projects due to economic downturn.

【Insert Table 4 here】

Third, the SAR Government has to manage the rising public expectations of a citizenry that has greater aspirations for quality social policies, but is also not well prepared to fund them. This is most vividly illustrated in the case of health care financing. A Harvard team report on Hong Kong SAR’s health care system projects that in order to maintain the 1998 level of quality and access to public health services (against the background of an ageing population, continued innovations in medicine technologies and rises in public expectations for quality health services), public health care expenditure might have to increase from 14 percent in 1998 to 20-23 percent of the total government budget by 2016.34 Clearly, this is impossible, as expectations for other social services would also rise. Hence, it was logical for

the Harvard health experts to recommend the insertion of an individual responsibility element into the health care system by increasing user fees, and other viable financial options such as health care savings plans. Unfortunately, the public wanted to stick to the prevalent system, which does not have financial and organizational sustainability. The failure of the Harvard health experts’ recommendations for change is not an isolated incident; earlier in 1993, health care financing initiatives of the Colonial Government were met with fierce resistance and little advanced.

Difficulties in the squaring of the welfare circle

As briefly mentioned, the neo-liberal welfare state of Hong Kong SAR has become an entrenched part of its capitalist economic system. It has provided substantial and comprehensive benefits for the majority of its population. This is especially the case in education, health care, and a less extent in public housing. With these bases the demand for state welfare is genuine; it reflects that many people in Hong Kong SAR have to depend upon state welfare for tackling social risks beyond their personal control. Imagine the lowest 40 percent of households getting only 11 percent of the total household income in 2001. The lower income groups, quite a substantial minority, would have to depend upon state welfare to make up their insufficient market wage. High expectations for state welfare are also a function of the lack of or inadequate built-in mechanism in the transaction of social services and benefits. There had been reasonable grounds for providing non-contributory universal and means-tested social services and benefits over the colonial era. The initial development of low fees and charges for public health services in the mid-1960s is a case in question. But the


low-tax regime and narrow tax-base served as the context where many people do not perceive the need for their own responsibility for the welfare state. Clearly, these institutional arrangements for service provisions are socially created.

This is not to suggest that those lower-income households were able to pay, but the institutional arrangements deprive their chance to recognize the fiscal side, on their parts, of the welfare circle. In other words, a growth-dividend fuelled welfare state desensitizes people of the need and responsibility for squaring of the welfare circle. In hindsight, the colonial era was too good to be true – a ‘growing cake’, due to a long period of economic development. This development allowed redistribution without ‘pain’ to the majority. But the harsh reality of a continued budget deficit in the beginning years of Hong Kong SAR is a wake-up call to alert people and the government of the need to manage expectations for squaring the welfare circle. For example, when the economy has begun to pick up, with economic growth in a row for two years, the SAR Government, as we mentioned in above, proposed the idea of a GST with the intention to broaden the tax base.

The strength of a neo-liberal state is its emphasis of self-reliance, underscored by the value of individualism, which fits well with market operations in a free economy like the Hong Kong SAR. But one important presumption of self-reliance is full employment, which has become currently difficult. In addition, policy failures of the Colonial Government to initiate contributory insurance schemes and substantial cost-recovery measures in retirement, unemployment, and health care at the time when it was more affordable, sowed the seeds for the present scenario of the inability for squaring the welfare circle, even at a level where the Hong Kong SAR’s social expenditure as a share of GDP is forty years behind the OECD countries.

In other words, the present problem in the case of squaring the welfare circle is partly structural – the vulnerability of people to social risks beyond their control; partly state
failure – the Colonial Government’s inability to plan when the economy was able to make dividends for ‘painless’ redistribution for the rainy days ahead; and partly institutional – the lack of establishing built-in mechanisms by the taxation system and fees and charges in social service transactions for managing people’s expectations.

Conclusion

To conclude, it seems that the Hong Kong SAR has inherited a neo-liberal welfare state from its colonial past. According to Briggs’ definition of a welfare state, the Hong Kong SAR provides income guarantees, tackles social contingencies of different kinds and ensures best standards of public education and health care services are offered to all its citizens disregard of class differences. As such, Hong Kong SAR has a well-established welfare system or welfare state in place, albeit it is not matured as those in the West at least in expenditure terms. However, the welfare state is somewhat rigid and it seemed to be on a path of growth amid an economic crisis, as illustrated in the two cases and the increase of social expenditures in the post-1997 era (Table 1). The SAR Government attempted to reduce social expenditures, but it was not successful. Nevertheless, it was able to reduce the size of the civil service establishment that was helpful in achieving fiscal balance. Moreover, it was evident that the SAR Government also increased expenditures which had an explicit investment function. In other words, the response pattern of the SAR Government to the squaring of the welfare circle is a mixture of the above-mentioned two perspectives – first, it attempted to reduce budget and concomitantly increase taxes; second, it increased spending on social policy which had an investment function.

On the reduction of budget, it is demonstrated that welfare institutions have enormous powers and life of their own and are able to change people’s values and behaviour,

---

37 See Bonoli, George & Taylor-Gooby, (2000), pp.11-12; North, D., Institutions, Institutional Change, and
that the Hong Kong SAR has a legacy of the Confucian self-reliance ethos. Welfare institutions also created powerful interest groups favoring further intervention as illustrated in the two litigation case examples. In this vein, it is extremely important to design welfare institutions with mechanisms which can harmonise rights with responsibilities to avoid moral hazard.

In the case of the Hong Kong SAR, structural factors nevertheless have a role to play in welfare development. They are the basis for social protection and policy expansion – the poor in a vastly unequal society, at least in income term, have to depend upon social policy. Nevertheless, the arrangements of welfare institutions are the contexts where the structural changes are embedded and moderated – for example a universal health service at low cost to patients blurs the distinction between need and want and is vulnerable to abuses; and most importantly, it does not have a sustainable financial basis with inbuilt mechanism to constrain demands for services. In this regard, it seems that there is much to be done as welfare institutions are socially created; hence, they can also be recreated to fit new social and economic context. Here, we come back to the issue of governance in social policy – the role of governments to manage expectations is important as public demands for social services and benefits are unlimited as the case of Hong Kong vividly illustrates. The failure of this government role means that despite increases in social expenditures, political legitimacy still suffers. In this regard, institutional design of social services and welfare benefits are part and partial of good governance.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Australia</td>
<td>10.9</td>
<td>17.8</td>
<td>18.0</td>
<td>17.7</td>
<td>17.8</td>
<td>17.5</td>
<td>18.6</td>
<td>18.0</td>
</tr>
<tr>
<td>Ireland</td>
<td>11.7</td>
<td>19.4</td>
<td>18.2</td>
<td>16.8</td>
<td>15.6</td>
<td>14.2</td>
<td>13.6</td>
<td>13.8</td>
</tr>
<tr>
<td>Japan</td>
<td>/</td>
<td>13.5</td>
<td>13.7</td>
<td>13.8</td>
<td>14.5</td>
<td>15.1</td>
<td>16.1</td>
<td>16.9</td>
</tr>
<tr>
<td>Norway</td>
<td>11.7</td>
<td>26.0</td>
<td>24.9</td>
<td>24.1</td>
<td>25.7</td>
<td>25.8</td>
<td>23.0</td>
<td>23.9</td>
</tr>
<tr>
<td>United States</td>
<td>10.9</td>
<td>15.5</td>
<td>15.3</td>
<td>14.9</td>
<td>14.5</td>
<td>14.2</td>
<td>14.2</td>
<td>14.8</td>
</tr>
<tr>
<td>OECD+</td>
<td>13.1</td>
<td>22.5</td>
<td>22.7</td>
<td>22.3</td>
<td>21.9</td>
<td>21.9</td>
<td>21.6</td>
<td>21.9</td>
</tr>
<tr>
<td>Hong Kong*</td>
<td>8.3</td>
<td>8.7</td>
<td>9.0</td>
<td>11.3</td>
<td>12.5</td>
<td>12.0</td>
<td>11.7</td>
<td></td>
</tr>
</tbody>
</table>


+OECD includes countries of Australia, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Netherlands, New Zealand, Portugal, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States.

* Calculated on financial year, e.g., 1995=April 1995- March 96

Note: Figure exclude transfers between the General Revenue Account and funds
### Table 2 Social Expenditure in Hong Kong 1997/98-2003/04

<table>
<thead>
<tr>
<th></th>
<th>97/98</th>
<th>98/99</th>
<th>99/00</th>
<th>00/01</th>
<th>01/02</th>
<th>02/03</th>
<th>03/04</th>
<th>04/05</th>
<th>05/06*</th>
<th>06/07*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Expenditure</td>
<td>234,780</td>
<td>266,448</td>
<td>269,484</td>
<td>267,507</td>
<td>269,359</td>
<td>263,520</td>
<td>271,098</td>
<td>265,259</td>
<td>250,255</td>
<td>264,889</td>
</tr>
<tr>
<td>Social Expenditure</td>
<td>121,370</td>
<td>145,106</td>
<td>155,689</td>
<td>154,932</td>
<td>148,559</td>
<td>144,297</td>
<td>149,790</td>
<td>141,729</td>
<td>136,915</td>
<td>140,824</td>
</tr>
<tr>
<td>Education</td>
<td>47,027</td>
<td>48,479</td>
<td>50,307</td>
<td>51,408</td>
<td>52,232</td>
<td>54,785</td>
<td>56,496</td>
<td>55,732</td>
<td>55,576</td>
<td>56,450</td>
</tr>
<tr>
<td>Health</td>
<td>27,982</td>
<td>31,400</td>
<td>31,894</td>
<td>32,753</td>
<td>34,213</td>
<td>33,199</td>
<td>34,231</td>
<td>32,355</td>
<td>31,639</td>
<td>32,340</td>
</tr>
<tr>
<td>Housing</td>
<td>24,651</td>
<td>38,850</td>
<td>45,872</td>
<td>42,606</td>
<td>32,055</td>
<td>24,031</td>
<td>25,277</td>
<td>19,523</td>
<td>15,874</td>
<td>15,821</td>
</tr>
<tr>
<td>Social Welfare</td>
<td>21,710</td>
<td>26,377</td>
<td>27,616</td>
<td>28,165</td>
<td>30,059</td>
<td>32,282</td>
<td>33,786</td>
<td>34,119</td>
<td>33,826</td>
<td>36,231</td>
</tr>
<tr>
<td>(Social Security)</td>
<td>(14,015)</td>
<td>(17,949)</td>
<td>(18,653)</td>
<td>(18,830)</td>
<td>(19,798)</td>
<td>(21,574)</td>
<td>(22,680)</td>
<td>(23,043)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social Expenditure as % of Public Expenditure</td>
<td>51.7</td>
<td>54.5</td>
<td>57.8</td>
<td>57.9</td>
<td>55.2</td>
<td>54.8</td>
<td>55.3</td>
<td>53.4</td>
<td>54.7</td>
<td>53.2</td>
</tr>
</tbody>
</table>

* Revised estimates/Estimates


Note: Public expenditure, also known as Consolidated Public Sector expenditure, includes government expenditure, total expenditure of the trading funds, the Housing Authority and the previous Provisional urban and Regional Councils (up to 31 Dec. 1999), and payments from the Lotteries Fund. Where appropriate, historical figures have been adjusted to comply with the current classification expenditure.
Table 3 Hong Kong Government’s Budget Balances, 1991/92 to 2005/06 (HK$ million)

<table>
<thead>
<tr>
<th></th>
<th>91/92</th>
<th>92/93</th>
<th>93/94</th>
<th>94/95</th>
<th>95/96</th>
<th>96/97</th>
<th>97/98</th>
<th>98/99</th>
<th>99/00</th>
<th>00/01</th>
<th>01/02</th>
<th>02/03</th>
<th>03/04</th>
<th>04/05</th>
<th>05/06*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Budget surplus/(Deficit)</td>
<td>22,509</td>
<td>21,979</td>
<td>19,164</td>
<td>10,843</td>
<td>(3,113)</td>
<td>25,678</td>
<td>86,866</td>
<td>(23,241)</td>
<td>9,952</td>
<td>(7,833)</td>
<td>(63,331)</td>
<td>(61,688)</td>
<td>(40,128)</td>
<td>21,356</td>
<td>4,057</td>
</tr>
<tr>
<td>% of GDP</td>
<td>3.3</td>
<td>2.8</td>
<td>2.1</td>
<td>1.1</td>
<td>-0.3</td>
<td>2.1</td>
<td>6.5</td>
<td>-1.8</td>
<td>0.8</td>
<td>-0.6</td>
<td>-5.0</td>
<td>-4.9</td>
<td>-3.2</td>
<td>1.7</td>
<td>0.3</td>
</tr>
</tbody>
</table>

*Revised estimate

<table>
<thead>
<tr>
<th></th>
<th>97/98</th>
<th>98/99</th>
<th>99/00</th>
<th>00/01</th>
<th>01/02</th>
<th>02/03</th>
<th>03/04</th>
<th>04/05</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number</td>
<td>% of total cases</td>
<td>Number</td>
<td>% of total cases</td>
<td>Number</td>
<td>% of total cases</td>
<td>Number</td>
<td>% of total cases</td>
</tr>
<tr>
<td>Old age</td>
<td>112,067</td>
<td>57.3</td>
<td>124,304</td>
<td>53.4</td>
<td>130,070</td>
<td>58.4</td>
<td>139,288</td>
<td>59.3</td>
</tr>
<tr>
<td>Disable and ill health</td>
<td>34,519</td>
<td>17.6</td>
<td>39,782</td>
<td>17.1</td>
<td>31,693</td>
<td>13.9</td>
<td>33,810</td>
<td>13.8</td>
</tr>
<tr>
<td>Single parent family</td>
<td>17,161</td>
<td>8.8</td>
<td>25,613</td>
<td>11.0</td>
<td>25,146</td>
<td>11.0</td>
<td>29,534</td>
<td>11.9</td>
</tr>
<tr>
<td>Unemployment</td>
<td>19,108</td>
<td>9.8</td>
<td>31,942</td>
<td>13.7</td>
<td>26,185</td>
<td>11.5</td>
<td>31,602</td>
<td>12.8</td>
</tr>
<tr>
<td>Low earnings</td>
<td>4,714</td>
<td>2.4</td>
<td>7,562</td>
<td>3.2</td>
<td>8,002</td>
<td>3.5</td>
<td>9,140</td>
<td>3.6</td>
</tr>
<tr>
<td>Others</td>
<td>8,076</td>
<td>4.1</td>
<td>3,616</td>
<td>1.6</td>
<td>3,919</td>
<td>1.7</td>
<td>3,818</td>
<td>1.6</td>
</tr>
<tr>
<td>Total number of cases</td>
<td>195,645</td>
<td>100.0</td>
<td>232,819</td>
<td>100.0</td>
<td>228,015</td>
<td>100.0</td>
<td>247,192</td>
<td>100.0</td>
</tr>
<tr>
<td>Amount (HK$ million)</td>
<td>9,441.3</td>
<td>13,028.7</td>
<td>13,623.4</td>
<td>13,559.8</td>
<td>14,404.6</td>
<td>16,130.8</td>
<td>17,306.2</td>
<td>17,631.0</td>
</tr>
</tbody>
</table>

Note: Figures are as at end of the financial year.