

# HONG KONG: MYSTERY OF THE OPEN SECRET

HONG KONG, the island that reverts to Chinese control next year, continues to bemuse observers. For they have not yet fathomed out the secret of the prosperity of the colony, despite public access to the evidence.

Governor Chris Patten, who recently advocated that Britain ought to learn the lesson of the island's prosperity, referred to the low-tax status of the colony. This attracts investment and provides the incentives that has turned the barren rock into a haven of good fortune.

The tax profile ought to have provoked Governor Patten's Conservative colleagues in Westminster into a searching analysis. For Tory Prime Minister John Major now heads a government that claims to advocate a tax-cutting philosophy, while presiding over tax increases that have taken the burden to record levels.

WHY has Hong Kong been able to operate a regime of low taxation? The politicians do not focus on the reason: the public sector in the colony is financed largely out of the rent of land.

But economists are none the wiser, even when they note the land factor. One of them is *Guardian* writer Will Hutton, author of the best-seller *The State We're In*. Mr. Hutton argues that the colony's success stems from its deep-sea harbour: it is the gateway to the Chinese market. And yet, he adds:

"The increased infrastructure of airport facilities, railway networks, docks, expressways, water and sewage treatment to keep pace with this growth has been astonishing. Education and public housing have expanded sharply, too — all apparently in a low-tax

environment.

"This is also something of a myth. The Hong Kong government has an enormous asset: it owns all the land and, with prices rocketing at its regular auctions, that is a huge source of income."<sup>1</sup>

Despite the socialisation of a large slice of the rental value of land, the government of Hong Kong does not take it all. That is why, as Mr Hutton notes: "...the impact of high rents offsets low taxes - and those rents reflect the land shortage that the government creates to its fiscal advantage".

This is a flawed presentation of the facts. For despite those high rents, the low-tax regime attracts entrepreneurs. Why? Their exported goods enjoy a sharp edge in the world markets, for their prices reflect the low-tax burden! Thus, with the inflow of profits to Hong Kong, the rental value of land rises...and entrepreneurs find that it pays to compete for a toe-hold in the colony, just to benefit from the fiscal regime.

This relationship — high rents are a measure of economic success, not a planned shortage of land — eludes Mr Hutton. Nonetheless, he does say: "If the UK government owned every acre in Britain and sold off parcels to raise revenue, income tax could be eliminated; but even the Conservative Right, celebrating low-tax Hong Kong, does not propose land nationalisation to achieve this end."<sup>2</sup>

It is not necessary to nationalise and sell the land: in fact, that would be short-sighted, for selling land produces a one-off result. *All that is necessary is to treat the annual rent of land as public*

*revenue, offset by commensurate reductions in taxes on labour and capital.*

Even so, given his recognition of the role of land in Hong Kong, readers might have expected Mr Hutton to advocate the rent-revenue for a reformed British economy: that is what his book was supposed to be all about. In fact, he fails to advocate this policy. Instead, he bemoans the institutional flaws without acknowledging that these cannot be rectified until the structure of the fiscal system is radically altered in favour of treating the rent of land as public revenue. Thus, he has popularised a concept — the "stakeholder" society — without proposing a working mechanism for achieving his worthy ends.

New Labour leader Tony Blair has swallowed the stakeholder notion, which appears to be the cornerstone of his manifesto for the 1997 general election. But he, too, has so far failed to realise that a future Labour government could not neutralise the booms and slumps of the business cycle until land speculation is removed from the economic landscape.

Land speculation is at the heart of boom/busts. Hong Kong has not removed these from its economy, either, for the colonial government does not take all of the rent of land for public use. If it did so, it would be possible to change from a low-tax to a no-tax economy!

<sup>1</sup> Will Hutton, *The State We're In*, London: Vintage, 1996.

<sup>2</sup> Will Hutton, "Myths that lay claim to a colonial miracle", *The Guardian*, London, March 4, 1996.