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Estimating the Intergenerational Discount Rate: A Case in Hong Kong

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Abstract:

Current estimates of the term structure of interest rates are only up to a maturity of 30 years. The purpose of this study is to unveil the intergenerational dimension of discount rates using a very "long-lived" and inheritable asset – property. Hong Kong provides a unique data set for empirical study because it has a mix of lands with different lease tenures (e.g. 50, 75, 99, and 999 years), and their transactions have been enormous. This study will: 1) examine the effect of land tenure on property prices, and 2) test whether intergenerational discount rates are different from short-term discount rates. The discount rate uncovered in this study would contribute to a more informed choice of discount rates for intergenerational decision analysis, such as evaluating the cost-effectiveness of environmental legislation and assessing very long-term pollution damages in court. The results would also have important implications for real estate valuation practices in China, as all land in the Mainland and Hong Kong is leasehold.

Keywords:

Discount rate, land tenure, sustainable development

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