

# Sustaining economic dynamism not just a numbers game

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This is an edited excerpt of a speech by Monetary Authority of Singapore managing director Ravi Menon at the Singapore Perspectives 2018 conference on Monday. He spoke about sustaining economic dynamism in the face of demographic challenges. Singapore has a falling total fertility rate and an ageing population. The result: a dwindling labour force, which curtails economic growth. The country thus has to consider net immigration, adding to the number of citizens and permanent residents who can live and work in Singapore. It also needs to allow good-quality foreign workers to beef up the workforce, he stressed. But in the end, economic dynamism is not just a numbers game. Raising productivity and having an open-minded, adaptable, well-educated workforce can help Singapore sustain its dynamism.

Gross domestic product (GDP) growth can be seen as the sum of productivity growth and labour force growth.

This means, holding productivity growth constant, a decline in labour force growth will have a direct impact on economic growth. If labour force growth falls to near zero, then the only source of GDP growth is productivity growth.

If productivity growth stays at about 1.5 per cent, which is what we have likely averaged over the last seven years (based on mid-year employment), then GDP growth will approach that level.

So, what are the trade-offs?

If we want labour force to grow and have zero net immigration, then we have to allow the share of foreign workers in the workforce to rise.

If we want the overall labour force to grow and the share of foreign workers to be stable, then we have to allow net immigration.

If we want zero net immigration and the foreign worker share to be stable, then we have to accept zero labour force growth. This is the demographic trilemma. Are there ways to escape the trilemma? Or at least soften its hard constraints? There are two solutions often mentioned.

First, an increase in fertility. Second, an increase in resident labour force participation rate.

## **Increasing fertility**

A recovery in Singapore's TFR (total fertility rate) is the best and most lasting solution that we can have, but its positive effects on labour force will only occur in the very long run.

A recovery in the TFR will not have any perceptible impact on labour force and GDP growth until nearly 2040.

It will take time for the extra babies born in the next 15 years to start entering the labour force. So while it's the most lasting solution to our challenges, TFR effects will only impact the economy in the long run.

### **Increase resident labour force participation rate**

The second way to soften the trilemma is to increase our resident Labour Force Participation Rate (LFPR). This will have more immediate payoffs. But even at plausible stretch targets, its effects on resident labour force growth will be quite limited.

Singapore's LFPR - defined as the share of the resident population aged 15-64 who are in the labour force - is currently 75.4.

It is not bad by OECD standards but there is scope to improve it. Japan is at 76.8; Germany is at 77.9; the Netherlands is at 79.9; Sweden is at 82.1. Our LFPR for older workers is not bad; it is female LFPR where we are lagging behind.

There is currently still a fairly large gender LFPR gap between males and females in their 40s and 50s. This gap in Singapore is higher than that in leading OECD countries. In many advanced economies, women tend to return to the workforce after their prime child-bearing years.

In Singapore, this is much less prevalent. If we can make it easier for our women to return to the workforce after they have had their children, we can narrow the gender gap vis-a-vis the advanced economies.

Assume we narrow our gender gap from the current 15 per cent points to 11 per cent points by 2035 - approximately the level seen in Germany and Netherlands.

This will only translate into a cumulative labour force increase of about 2 per cent in 2035.

The demographic trilemma presents the constraints and choices facing us. We can soften it by raising the TFR and LFPR.

Of course, having babies or returning to work are deeply personal choices. The Government tries to facilitate fertility and labour force participation because that is what many people desire for their own fulfilment.

Many women would like to return to work, but they face a number of constraints. We must make it easier for them to do so.

The Government has made significant efforts in recent years to invest in childcare and facilitate more flexible working arrangements. We must continue to push on this front and, collectively as a society, enable more who want to work enter the workforce. We must make balanced choices in addressing the trilemma. We must accept a slower rate of labour force growth.

The underlying demographic slowdown is so severe that it is neither feasible nor desirable to try to completely offset it through immigration or foreign workers.

But we must also allow a certain rate of net immigration to augment our resident population.

This is not just about numbers but about rejuvenation and expanding our talent base. While we cannot keep increasing our share of foreign workforce indefinitely, we must be flexible in allowing fluctuations in the ratio according to economic cycles, changing circumstances and opportunities.

Finally, we must reframe our question on foreign workers.

It is not about how many foreign workers industry wants or society can afford to have, but what number and kind of foreign workers we need to maximise the job and wage opportunities for Singaporeans.

Foreign workers must be a complement to the local workforce.

### **Demographics is not destiny**

Let me move on to the second broad theme: that demographics is not destiny. We can sustain our economic dynamism in the face of demographic change.

First, we should not grow despondent over our slowing rate of economic growth. Countries with low level of GDP per capita tend to have higher rates of GDP growth. This is called "catch-up" in the literature.

Meanwhile, countries with higher levels of GDP per capita tend to grow at slower rates as they are more mature. Singapore is a mature economy: It has one of the highest levels of per capita income in the world. We will not be able to sustain 6-7 per cent rates of growth that were seen a decade ago.

But while we must accept a lower rate of growth than before, as a global city, we cannot afford to grow too slowly either.

Many leading global cities grow at rates of 2.5-3.5 per cent, faster than the national average of the countries they are part of.

London has averaged 3.3 per cent annual growth since the financial crisis, while Sydney has averaged around 2.9 per cent. San Jose (which encompasses Silicon Valley) has averaged 2.7 per cent p.a. It is hard to imagine a dynamic city growing at less than 2 per cent or worse still, 1.5 per cent.

It will be unattractive to investors and talent, including the city's own investors and talented people. A reasonably good rate of growth helps to create opportunities and preserve a sense of progress and hope, particularly among the young. It will also facilitate upward social mobility.

### **Not headcount but productivity**

The experience of other leading cities suggests that demographics is not destiny.

Yes, vibrant cities do attract people - and their additions to the labour force add to growth. But the main source of their growth and dynamism is not headcount but productivity. About two-thirds of overall GDP growth in the cities mentioned above is due to productivity improvements.

In comparison, productivity has accounted for about half of Singapore's GDP growth. There is clearly scope for us to do better and thereby sustain our dynamism.

How can we do this?

## **Sustaining dynamism**

### **Education dividend**

First, Singapore has scope to reap the human capital dividends that are arising from the continual investments we have made in education and training in past decades.

As recently as 2000, 45 per cent of resident workforce had below secondary school education, and only 12 per cent had university education. In just 11/2 decades, those ratios have converged, reflecting the cumulation of efforts made over preceding decades: The proportion with less than secondary education has dipped below 30 per cent, while the proportion of the university-educated has more than doubled to nearly 30 per cent.

The effects of this transformation in human capital will continue to be felt in the productive capacity of the workforce. With higher levels of education, the ability of the workforce to take on more complex tasks and to leverage technology is substantially stronger.

There is still plenty of scope to increase the share of those with secondary, post-secondary and diploma and professional qualifications.

They will be better placed to transform the nature of many jobs, raising standards and quality, thus enabling productivity and wages in these occupations to rise.

### **Improve foreign workforce quality**

Second, there is scope to improve the quality of the foreign workforce.

We should increasingly be concerned about the skills of the foreign workers that we take in, rather than just the numbers.

In fact, more skilled foreign workers will mean that we will need fewer of them. The trend of improving quality in our foreign workforce has already begun. The proportion of work-permit holders has declined by about 10 percentage points over the last 10 years, while the proportion of S Pass and employment pass holders has increased by around 10 percentage points.

This trend must continue as we restructure our economy towards higher value-added activities, seek deeper skills and undertake more pervasive digitalisation.

### **Raise productivity in domestic services**

Third, there is scope to increase productivity and efficiency in many domestic services jobs.

Consider wages in four occupations (plasterer, childcare worker, baker and security guard) across four countries (Singapore, Australia, the US and the UK).

In Singapore, the typical pay in these occupations range from 30-60 per cent of the local median wage. In Australia, these occupations have wages much closer to the median wage. Wages in these occupations are also higher in the US and the UK.

There is scope to further professionalise these jobs in Singapore. In particular, to increase the skills content, leverage technology and improve business processes, and raise the quality of output. This will enhance productivity and help to support higher wages in these occupations.

In fact, the professionalising of more such so-called "rank-and-file" jobs in Singapore will help to strengthen and broaden the middle class, and make for a more equitable society.

Singapore can do this.

We have good examples of jobs that have historically been perceived to be less skilled that have been successfully upgraded.

These jobs now command much relatively good wages, close to those seen in Australia, the US and the UK, controlling for median incomes.

Our bank tellers, vehicle mechanics, hairdressers and bus drivers earn a good (median) wage that is quite close to the median.

In fact, our bus drivers appear to be paid just below the median in Singapore (96 per cent of national median wage), comparable with their counterparts in Australia, the US, the UK (107, 94 and 101 per cent respectively).

And hairdressers in Singapore are doing amazingly well. They earn much closer to the median wage (82 per cent) compared with their counterparts in Australia, the US and the UK (32, 68 and 44 per cent).

The story of our bus drivers is interesting. Since the introduction of the Bus Contracting Model by the Ministry of Transport and the entrance of foreign bus operators, there has been greater competition in the bus industry, raising the game.

Bus driving became more professional. The focus is on driving well, increasing fuel efficiency and meeting the targets set by the Ministry of Transport on frequency and timeliness.

More women have also been drawn to the industry with the introduction of flexible working arrangements and maternity leave. The result is that the dependency on foreign workers has been reduced and productivity and wages have increased.

Now our bus drivers are making close to the median wage in Singapore.

Demographics is not destiny and economic dynamism is not about numbers. Dynamism is about quality - the quality of our workforce, the quality of our enterprises and the quality of our institutions. It is about high levels of efficiency and productivity.

It is about growing the Singaporean talent base as well as being a magnet for the world's talents. It is about a vibrant entrepreneurial and innovation base, characterised by a lot of start-ups, a lot of experimentation, and a lot of research and development (R&D).

Finally, dynamism must be about our people. We must remain an open society. Not just in being open to foreign trade, investment, and talent, but being deeply connected to the rest of the world. Not just attracting foreign talent to Singapore but Singaporeans venturing abroad as our companies and industries internationalise.

Most of all, being open in spirit and mindset, staying open to diversity, being comfortable working in multicultural settings, thriving in a globalised world, having an enterprising spirit - always seeking new and better ways to do things.