The Big Read: Budget 2016 prediction: No big bang, but a focus on the future

A look at what to expect from this year's Budget before its release later this week

Lee Yen Nee
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SINGAPORE — After grabbing the headlines in the past two years with big-ticket items — namely, the S$9 billion Pioneer Generation Package in 2014 and the multi-billion-dollar SkillsFuture initiative last year — the Budget Statement on Thursday (March 24) is expected to attract less fanfare, experts say.

But make no mistake about it — the 2016 Budget, to be delivered for the first time by new Finance Minister Heng Swee Keat, comes at a critical juncture in Singapore's development and will set the foundations for the country to continue to thrive in the challenging years ahead, as the economy moderates and undergoes transformation.

Experts note that the 2016 Budget — in the same vein as previous Budgets unveiled at the start of a new term of Government — will also adopt a more prudent fiscal approach and re-focus on the economy.

The Singapore Constitution prevents every new term of Government from drawing on the accumulated fiscal surpluses of the previous term, thus limiting the room for large expenditure early on in a fresh term.

A closer examination of the 2002, 2007 and 2012 Budgets — all coming at the start of a new term of government — reveals a common broad thrust: Taking bold steps to position and steer the economy to greater heights, with an eye on generating revenue for future expenditure.

For instance, in 2002 Budget, then-Finance Minister Lee Hsien Loong announced cuts in corporate taxes to increase Singapore's competitiveness in order to attract investments from multinational corporations (MNCs). In the same Budget, Mr Lee also announced the hike in the Goods and Services Tax (GST) from 3 per cent to 5 per cent to reduce Singapore's reliance on direct taxes and to partially compensate for the reduction in revenue from corporate taxes.

In 2007, coming out of a buoyant economic period, a further raise in GST to 7 per cent was announced by Mr Lee, and the message on the importance in strengthening capabilities of both businesses and the workforce featured heavily in that year's Budget speech.

This point was honed further in 2012 when then-Finance Minister Tharman Shanmugaratnam emphasised the need to restructure the economy by shifting to higher-value-added activities and reduce the reliance on lower-skilled foreign manpower.

The 2012 Budget, which featured measures such as cuts in dependency- ratio ceilings and man-year entitlement quotes for foreign workers, came a year after the People's Action Party

(PAP) Government's worst General Election performance since independence, with 60.1 per cent of the vote share. Foreign labour was among the hot button topics during the elections.

Mrs Chung-Sim Siew Moon, head of tax services at Ernst & Young Solutions, said: "The relentless drive to stay globally competitive for sustainable economic growth has underscored the previous first-term Budgets in 2007 and 2012 … The 2012 Budget was a bittersweet one: it showed resolution in staying the course to position Singapore as a productivity leader with a reduced reliance on cheap foreign labour, but had offered little in immediate relief to businesses and individuals to tide over tough times then."

She added: "This year's Budget is likely to be more moderate and perhaps empathetic in approach where the government will likely seek to balance the continued push for a vibrant and competitive economy with more care towards enabling our SMEs (small and medium enterprises), workforce and population to grow and succeed, so as to strengthen the Singapore core and foster an inclusive society."

A few weeks ago, Mr Heng gave a glimpse of the 2016 Budget: It will have a "strong focus" on the economy, with one of the priorities being to assist SMEs as they continue their restructuring journey. He also alluded to the "particularly prudent" nature of first-year Budgets unveiled by previous terms of government, so that the Government will "have resources when we need to act later". Experts noted that this is especially crucial in the current challenging climate, with strong headwinds compounded by fears of a worse-than-expected China slowdown, the end of the commodity super-cycle as well as divergent monetary policies around the world. These factors have dimmed business prospects while Singapore is undergoing an economic transformation.

INCREASING PRODUCTIVITY AMID SLOWER GROWTH

Budget 2016 comes at a time when the Republic is transitioning into a new normal of slower growth as the economy matures.

This makes it all the more important to help Singapore enterprises, as they press on with their restructuring efforts while tackling challenges amid the uncertain global environment, experts whom TODAY spoke to said.

Gross domestic product (GDP) growth came in at 2 per cent last year, the weakest annual expansion since 2009, when the economy was hit by the global financial crisis and shrank 0.6 per cent. Productivity growth — measured by value added per worker — continued to lag, inching down 0.1 per cent last year to mark the second consecutive year of decline.

The Economic Strategies Committee (ESC), chaired by then-Finance Minister Tharman Shanmugaratnam, had set a target in 2010 to achieve 2 to 3 per cent productivity growth annually in the subsequent 10 years — an aim that appears to be a distant reach currently. Nevertheless, the experts believe that Singapore has to stay the course as results are gradually beginning to show.

Dr Faizal Bin Yahya, senior research fellow at the Institute of Policy Studies, said: "At this juncture, there is a confluence of factors, both external and internal, that are hampering efforts to restructure and improve productivity. The Government has been very supportive to businesses in the current restructuring to build a vibrant and dynamic innovative ecosystem that can drive future growth."

He added: "In the near term, the government should not steer too far from the current strategy, since it is well into the halfway mark of restructuring, and the economy is beginning to make significant inroads for lower-productivity industries such as construction and retail."

Unlike first-year Budgets of previous terms of Government that featured major new policy initiatives, this year's Budget is likely to be soft on that front, experts said. This is especially so as the work of the Committee on the Future Economy (CFE), chaired by Mr Heng, is due for completion only in December, when it will present its recommendations on charting Singapore's future economic path.

Instead, the Finance Minister is expected to build on past themes of boosting productivity and encouraging innovation as a way to upgrade the capabilities of firms, as well as laying the foundation to help local enterprises gain the ability to create value — a major agenda in the CFE's work.

With the economy forecast to grow between 1 per cent and 3 per cent this year, experts suggested, among other things, refining existing initiatives to help SMEs, such as the Productivity and Innovation Credit (PIC) scheme. Mr Tay Hong Beng, head of tax at KPMG Singapore said: "This includes customising the PIC to cater for different stages of growth of businesses, giving incentives to grow and keep Singapore brands within Singapore, and broadening the scope of research and development incentives."

Other suggestions included delaying the next round of increases in foreign worker levies, which was deferred from last year to allow SMEs more time to adapt to the tighter labour market. This would temporarily help to alleviate some concerns over costs as businesses navigate the rough patch, the experts said.

But they noted that, over the longer term, companies ought to continue restructuring as the Government is firm on its stance to reduce the economy's reliance on foreign manpower. SMEs must rethink their business models, innovate and internationalise, the experts reiterated.

Dr Walter Theseira, senior lecture at SIM University, said: "The basic problem is that we are a developed economy and most developed economies don't have access to the large supply of foreign workers that we do, for political and other reasons. If we want our domestic businesses to be competitive with other developed economies, we really have to help them become profitable even when their labour costs are not suppressed through foreign labour imports."

Making sure that the workforce possesses the skills necessary to fill job requirements in Singapore's economic transformation is also an area worth looking into at this juncture, Dr Theseira said, noting that the rising number of skilled mid-career professionals, managers, executives and technicians (PMETs) in long-term unemployment is "particularly worrying".

“That could signal structural mismatches between our workforce skills and available jobs. Unemployment today is no longer just a problem of the unskilled — who have plenty of job offers, albeit low-paid, due to foreign manpower restrictions. It’s a problem of people who are qualified on paper not having the right skills,” he said.

FUNDING HIGHER SOCIAL SPENDING: WHERE THE MONEY WILL COME FROM

With social and infrastructure spending set to rise in the coming years, the Government faces the real prospect of running out of money sooner, rather than later — if revenues do not increase in tandem.

Apart from preserving competitiveness and economic success, improving the capabilities of SMEs and the workforce would also allow Singapore to expand its tax revenue base to fund social and infrastructure spending that is set to rise as the population ages.

This is coming at a time when much of Singapore’s past growth formula has been exhausted and the country has to depend on new sources of growth, noted Professor Hoon Hian Teck, Associate Dean of the School of Economics at Singapore Management University.

“The earlier phase of GDP growth came from Singapore being a technology follower and as a result, jobs were created, earnings went up so the tax base went up. We are now at a phase where (this model) has pretty much been exhausted, we now have to focus on new sources of growth, which primarily will have to come from our SMEs becoming more efficient in the way they do things, their ability to expand into overseas markets,” Prof Hoon said.

“And by raising overall productivity of the economy, we’re expanding the pie and therefore indirectly expanding the tax base (because) when businesses do better, they pay their workers better as well, so revenue from corporate and personal income taxes also go up,” he added.

Corporate income tax makes up the largest share, or an estimated 21 per cent, of the country’s total operating revenue in the current financial year ending March 31, while personal income is expected to contribute around 13.9 per cent, making it the third-largest contributor of operating revenue.

The GST forms the second-largest portion of Singapore’s total operating revenue, at an estimated 16.3 per cent in FY2015. GST was introduced at 3 per cent in 1994 to shift the country’s reliance on direct taxes, such as those on corporate and personal income, to indirect taxes. It was subsequently raised twice, as announced in the 2002 and 2007 Budgets, to the current 7 per cent.

With social expenditure due to rise, the questions on everyone’s minds are if and when GST will be raised again.

Rounding up the 2015 Budget Debate, Deputy Prime Minister Tharman Shanmugaratnam said with moves such as incorporating Temasek Holdings into the Net Investment Returns (NIR) framework and the increase in personal income tax rate for top earners, Singapore “will be in a good position for at least the rest of this decade”.

As the end of the decade looms, all experts whom TODAY spoke to agreed that further rises in the consumption tax cannot be the sole solution to raising the revenue Singapore needs, to fund the increases in social spending. Several shared Prof Hoon's sentiment on the upgrading capabilities and productivity of businesses as a long-term answer to expanding Singapore's tax revenue.

Mr Koh Soo How, PricewaterhouseCoopers' Asia Pacific indirect tax leader, noted that an increase in tax rate is a "quick fix". He expects the Government to focus on building a larger tax base through enhancing its competitiveness and productivity, while watching developments in countries such as South Korea and Japan, where measures on taxing the digital economy were introduced.

Mr Richard Mackender, tax partner and indirect tax leader at Deloitte Singapore, agreed that the Government can broaden GST base by taxing online transactions, instead of raising GST, which will increase the cost of living of residents here.

"Measures could include imposing GST on the online purchase of services, as well as removing postal exemption on the importation of low-value goods," he said.

However, CIMB Private Banking economist Song Seng Wun said raising the GST is inevitable given the demographic profile of Singapore's population, which will see the number of workers leaving the workforce outpacing those entering it from as early as 2030.

"(GST) will still go up — it's a question of when. We can push it back by being able to generate growth through productivity improvements that lead to stronger revenue growth — then that definitely will help. So it boils down to the SME side, which is the backbone of the economy, to deliver the incremental improvement on the productivity front," he said.

"But even if we achieve that, all it does is push back (the need to raise GST) because of the underlying demographic of the society. Having said that, we should be able to stretch beyond this decade."