Source: *The Business Times,* p17
Date: 28 April 2021

The challenges ahead for Singapore's new Minister for Finance

Grappling with significant challenges, the rewards for getting it right will be a robust and sustainable Singapore economy and society for the next decade and beyond. BY CHRISTOPHER GEE AND KUNAL PAWA

THE recent Cabinet reshuffle saw Lawrence Wong appointed Singapore's ninth Minister for Finance since 1965. His appointment comes at a momentous point in Singapore's fiscal management. While Singapore's fiscal position remains sound and the country retains a top-rated AAA sovereign credit rating from all the major rating agencies, the new Minister for Finance will have to grapple with a number of significant challenges.

Even before the Covid-19 pandemic reared its ugly head, the economy had been facing a number of deep-seated challenges: population ageing, industrial and technological disruptions and climate change to name a few. All these trends and issues had been putting upward pressure on government expenditures which prompted Mr Heng Swee Keat, the outgoing Minister for Finance, to raise the prospect of a two percentage point increase of the Goods and Services Tax (GST) when he presented Budget 2018.

IMPLEMENTING THE 2 PER CENT GST HIKE

Delayed beyond 2021 as the economy recovers from the adverse impact of Covid-19, this GST hike is now scheduled to come into effect sometime between 2022 and 2025. Singaporeans have had much advance warning of this increase, and S$6 billion has already been set aside in 2020's Unity Budget for a GST Assurance Package that will cushion the impact of the GST increase on middle- and lower-income households for 5 to 10 years.

Nevertheless, there is likely to be an active debate about the actual timing of the increase, and the possible alternatives courses of action to raise this additional revenue. Mr Wong, as new Minister of Finance, will have to take the lead in justifying the increase in Parliament and to the public.

BALANCING SPENDING NEEDS

This GST hike, estimated to raise S$3 billion in additional revenue, will come against an anticipated backdrop of very significant increases in government expenditures in the next decade. Every single government ministry has a compelling case for more funding, especially those involved with social development and economic affairs, and on security, both domestic and external.

The Ministry of Health's FY2021 budget allocation of S$18.8 billion is enlarged due to Covid-19 mitigation measures, but it is now four and a half times larger than what was allocated and spent by the ministry only 10 years ago in the FY2011 Budget. The Ministry of Manpower's total FY2021 allocation is more than seven times what it was a decade ago. The renamed Ministry of Sustainability and the Environment's FY2021 Budget allocation is 2.7 times larger than FY2011 (when it was known as the Ministry of the Environment and Water Resources).

Government expenditure as a share of gross domestic product (GDP) is estimated at 21 per cent of GDP for 2021, up from 15 per cent in 2019 and 13 per cent in 2011. Although this is still low by international standards (the OECD country average for this indicator was 41.8 per cent in 2018) it is set to rise further in the future, even as we move beyond the Covid-19 pandemic, given the driving forces such as population ageing and climate change mitigation indicated above. Weighing up all the various funding calls from ministerial colleagues will involve a delicate balancing act by Mr Wong and will necessitate some political dexterity.

BALANCING THE BOOKS

While the trajectory of government expenditure is clearly upwards for the foreseeable future, the outlook for revenues is much more uncertain.

Net Investment Returns Contribution (NIRC), the single largest source of government revenues (larger than corporate income tax receipts) since Budget 2016, is likely to plateau in terms of its share of contribution to the Budget, given low real rates of return globally.

The NIRC is estimated at S$19.6 billion for FY2021, sufficient to cover 19 per cent of budgeted expenditure in the year. But if growth in this revenue source is unable to match the growth in expenditure, then alternative sources of revenue will be required if the government is to abide by the implicit requirement for each government to ensure Budgets are balanced during each five-year Parliamentary term.

The shape of the post-pandemic economic recovery will affect the quantum and the rate of increase in the government's tax receipts beyond the effect of the 2 percentage point GST rate hike. Is there, however, scope to raise other taxes for additional revenues for the government?

The new minister will have a much easier task in selling the Singapore story today than the country's finance ministers in the early formative years. Seen here are incoming Minister for Finance Lawrence Wong (left) and Heng Swee Keat, the outgoing minister. BT FILE PHOTO

Singapore's individual income tax regime is today the second largest source of tax revenues (after corporate income tax and larger than GST) and is already seen as highly progressive. While the top rate of individual income tax is still low by international standards at 22 per cent on assessed income above S$320,000, tax rates at the uppermost thresholds would have to rise very significantly (by 10-14 percentage points) to raise an amount equivalent to the 2 percentage point GST increase, while at the same time maintaining or improving the progressivity of Singapore's individual income tax system.

The concern would be that such a substantial change would result in unintended outcomes, such as causing the highest income earners to move elsewhere, diminishing productivity overall and paradoxically reducing tax revenues.

DEFENDING SINGAPORE'S ECONOMIC HUB AND CORPORATE INCOME TAX POOL

The question of whether higher corporate income tax rates could be another avenue for increasing revenue highlights another pressing challenge that the new Minister for Finance will have to confront immediately.

Around the world, there has been greater urgency to establish a global minimum corporate income tax regime, in large part to reduce tax competition that arises from countries attracting multinational corporations with low tax rates or other fiscal incentives.

While being part of a global initiative to raise corporate income taxes would seem to align with the goal of increasing tax revenue, the fear is that if Singapore's corporate income tax rates were to be increased to better comply with such a global minimum corporate income tax framework, there might be adverse consequences as a result, with many established multinational enterprises shifting their regional or global headquarters away from Singapore.

Although there is a strong case to be made that Singapore's attractions to global business extend far beyond its favourable tax regime, that case will need to be made forcefully by the new Minister for Finance to the international business community.

TAPPING OTHER FORMS OF TAXATION

Most of Singapore's tax revenues are raised based on economic flows (for example on income both corporate and individual, or transactions involving goods and services), and only about 6 per cent of the government's operating revenues are generated from asset taxes (largely property tax). Capital gains are not subject to tax.

Mr Heng indicated in the FY2021 Budget round-up speech that the government will review the possibility of introducing wealth taxes, an issue that has been subject to some debate locally as well as globally.

Mr Wong will have to oversee this review of asset and wealth taxes and handle this ongoing debate, with the side favouring imposing a tax on wealth having moral weight behind it in an age of heightened inequality. Any moves to subject assets and wealth to tax will also need to consider the consequential impact on Singapore's status as an economic and financial hub.

As with the issue of higher corporate and individual income taxes, the introduction of taxes that would disproportionately impact the well-off and the highest earners will require a strong belief in the country's attractions beyond comparatively low tax rates.

But the new Minister will have a much easier task in selling the Singapore story today than the country's ministers for finance in the early formative years such as Goh Keng Swee and Hon Sui Sen.

VALUING THE SINGAPORE STORY

The Singapore brand is today founded on stability, security and reliability, with sound infrastructure and deep global and regional connectivity. All these positive factors can only be sustained if everybody contributes their fair share, especially those who generate and benefit the most in this country.

Apart from these structural challenges, the new Minister for Finance will also oversee other pressing matters such as underwriting Singapore's Green Plan and the issuance of the new SGS (infrastructure) bonds. The challenges may seem daunting. But the rewards for getting it right will be a robust and sustainable Singapore economy and society for the next decade and beyond.

▮ The writers are from the Institute of Policy Studies, National University of Singapore. Christopher Gee is senior research fellow and head of the governance and economy department, and Kunal Pawa is a research associate.

Source: The Business Times © Singapore Press Holdings Ltd. Permission required for reproduction.