Economics & Strategy

DBS Focus

Singapore Budget 2022: Walking the fiscal tightrope

Economics/growth/fiscal

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- *Budget 2022 focuses on long-term priorities*
- *Measures were introduced to sustain the recovery and to help tackle rising costs*
- *Significant emphasis was placed to drive economic transformation*
- *New initiatives were announced to buttress Singapore's Green Plan 2030*
- *There is a leftward slant with greater focus on income equality*
- *Significant adjustments in tax policies were put forth to ensure fiscal sustainability*
- *A budget deficit of about SGD 3bn (0.5% of GDP) was allocated for FY22*

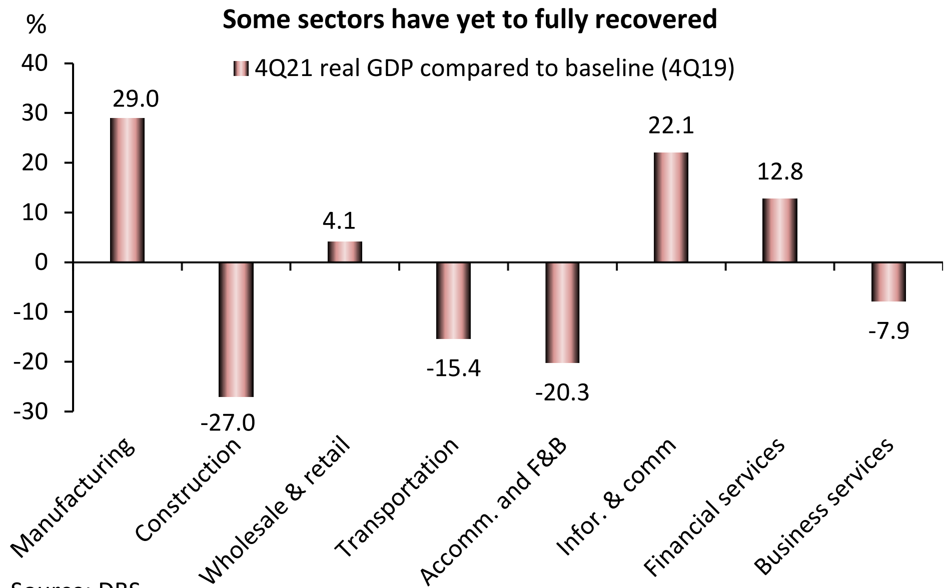
Budget 2022

Budget 2022 marks a key turning point in the fiscal policy focus. Coming off the worst recession since Independence and two years of pandemic, policy thrusts have shifted from crisis management to addressing longer term priorities. Emphasis have been placed on sustaining Singapore's longer term economic relevance in a post-COVID world and supporting Singaporeans and local companies in the way forward.

In a bid to raise revenue to fund ever rising social and economic needs, a comprehensive adjustment in tax policies have been announced, affecting companies and across all income groups in the coming years. This calls for some delicate balancing of the potential impact particularly amid rising inflationary pressure at present. As such, policymakers have backloaded most of the tax hikes in the coming years. However, doing so may be cutting it too close as it entails certain risk (more details in later section).

Sustaining the recovery and tackling rising costs

At present, the Singapore economy is firmly on the recovery path, although an uneven one. Despite strong headline growth of 7.6% in



Source: DBS

Calibrated measures to tackle an uneven recovery

2021 and double-digit growth in some sectors, the reality is that some of these worst hit sectors have yet to recover to pre-COVID levels in terms of their real GDP (sa). The challenge is further compounded by rising inflation. The effect cascades down to the workers in these sectors, who may not have enjoyed wage growth comparable to those in sectors that are less impacted. Moreover, the SMEs have also bore the brunt of the domestic COVID measures. Compounded with the impact of rising costs, workers and companies in these sectors have yet to fully benefit from the recovery.

In this regard, policy measures have been introduced under the Jobs and Business Support Package (SGD 500mn), the Household Support package (SGD 560mn) and the enhanced GSTV scheme to provide the transient support to companies and workers [1]. These will go a long way in terms of alleviating the concerns of having to cope with a slow recovery in earnings and rising costs. Yet, one must recognize that **such subsidy driven initiatives are not sustainable and would have to taper off eventually for reason of fiscal prudence, and more so when economic activities normalize.**

Persevering with economic transformation

Indeed, global economy has become increasingly more volatile and COVID has exacerbated the changes in the external environment. For Singapore to remain relevant in the rapidly changing world, Singapore must be agile and ready to pivot to new emerging trends, transform and leverage on new opportunities when they emerge. Efforts must also be

made to continuously enhance our domestic productivity and economic dynamism despite an aging demographic. This calls for a decisive and concerted effort to invest in our capacity for growth.

Investing in human capital

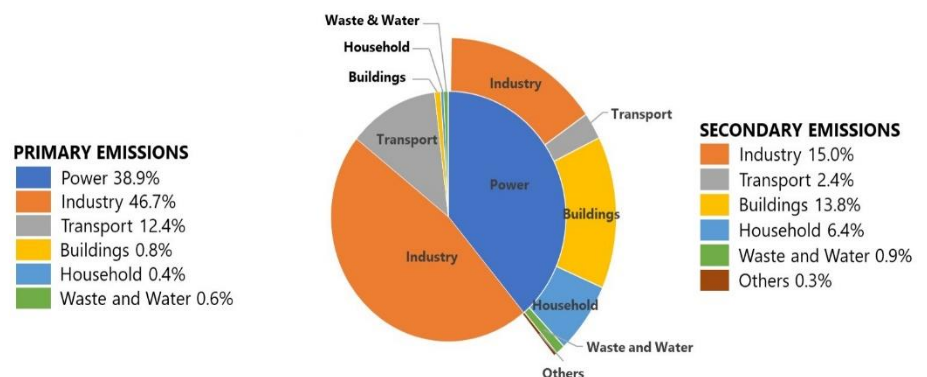
The enhanced support for SMEs, productivity and digitalization initiatives (e.g., PSG), R&D, as well as providing bespoke help to companies in growth stages (Singapore Global Enterprise initiative) will help to buttress the policy thrust. Additionally, the Job Growth Initiative has been extended to spur hiring of locals. Support for lifelong learning and training via the Skillsfuture scheme and SGUnited Mid-Career Pathway programme will help to strengthen the local human capital and to alleviate the skill mismatch problem in the labour market.

That said, further tightening of foreign labour policies (i.e., higher min. qualifying salary for EP and S-pass, and lower DRCs for WP) implies higher costs for companies that are dependent on foreign manpower and worsening of manpower crunch in some industries [2]. **Beside hiring locals, companies would have to intensify their investment in technologies to reduce their reliance on foreign workers**.

Elevating the green agenda

Singapore's green agenda has been taken to a new level with the announcement of the impending carbon tax hikes in the coming years. At present, Singapore carbon tax rate of S$5/tonne of carbon emission pales in comparison to many other economies at similar stage of economic development (e.g., Sweden (US$119/ton); Switzerland (US$99/ton); France (US$45/ton); Korea (US$33/ton). In a bid to achieve the net zero emission ambition by the second half of the

Singapore's industrial emission profile



Source: National Climate Change Secretariat

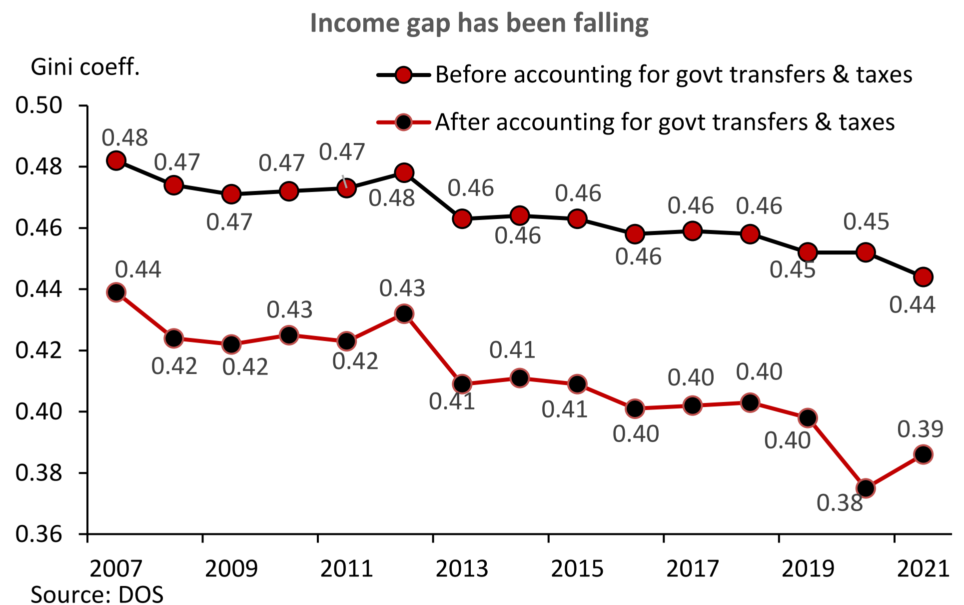
century, carbon tax rate will be raised steadily to between S$50-80 by 2030. While this will place Singapore closer to many developed economies, the impact on the economy will be significant. **Industries with high carbon emission such as power generation, manufacturing, aviation and land transport sectors will be most impacted, which in turn will likely be passed on to consumers as higher prices.**

That said, advancing Singapore Green Plan 2030 could provide impetus to emerging green sectors like green finance and carbon services. The government's intention to issue SGD 35bn of green bonds by 2030 to fund public sector green infrastructure projects would be an important catalyst. Efforts in this aspect will benefit sectors such as the financial, infrastructure and green solution providers.

Strengthening equality

Income gap will continue to narrow

There has been a distinct leftward slant in the budget focus. Significant emphasis has been placed to alleviate the income of the lower wage workers. The Progressive Wage Model (PWM) will be extended to cover more professions across all industries. Furthermore, the introduction of the Progressive Wage Credit Scheme (PWCS) and the enhancement to the Workfare Income Supplement schemes (S$2bn in total) will add more impetus to achieving the policy objective.



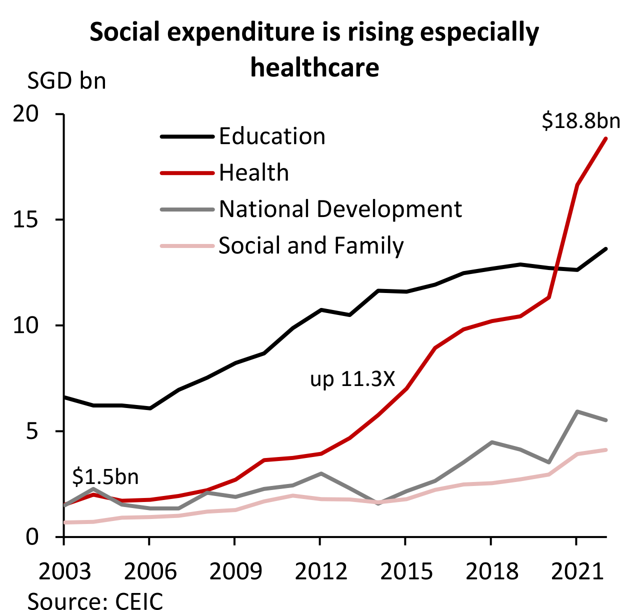
Source: DOS

As it is, Singapore's Gini Coefficient has been falling along with the efforts made in past years to strengthen the social safety net. In this regard, the measures announced in this Budget will likely guarantee a

continued decline in the Gini coefficient (i.e., income gap) and a more equitable society in the coming years.

Ensuring fiscal sustainability

While rebuilding public finance is a pressing concern, the bigger focus of Budget 2022 is ensuring the long-term robustness of Singapore's fiscal system to cope with challenges such as aging, future-proofing our human capital and climate change. These longer-term issues would incur significant costs on the nation and would need to be supported by a sustainable source of revenue.



Source: CEIC

Govt Operating Revenue, 2019	SGD mn	% share
Total operating revenue	74,274	100.0
Tax	67,645	91.1
Tax: Income: Corporate	16,732	22.5
Tax: Income: Personal	12,368	16.7
Tax: Income: Withholding	1,638	2.2
Tax: Contributions By Statutory Boards	1,798	2.4
Tax: Assets Taxes	4,762	6.4
Tax: Customs & Excise Duties	3,264	4.4
Tax: Goods and Services	11,164	15.0
Tax: Motor Vehicles	2,419	3.3
Tax: Betting Taxes	2,620	3.5
Tax: Stamp Duty	4,199	5.7
Tax: Others	6,683	9.0
Fees & Charges	6,275	8.4
Fees & Charges: Vehicle Quota Premiums	2,865	3.9
Fees & Charges: Others	3,409	4.6
Other Receipts	354	0.5

Source: MOF

Take for example, Singapore's population has been aging rapidly. Median age will rise to 50 years old over the next two decades, up from 43 years old at present. Policymakers have been pre-empting the eventual aging of Singaporeans by raising public healthcare expenditure. As such, expenditure on healthcare has risen by 11.3x, from SGD 1.5bn in FY02 to a budgeted 18.8bn in FY21. Moreover, there is also the need to strengthen the social safety net and investment in human capital. This means overall social expenditure will only continue to rise in the coming decades. Maintaining Singapore's fiscal prudence would thus require such recurring expenditure to be funded by recurring revenue. Unfortunately, there aren't many options available when it comes to reliable sources of tax revenue. Though corporate and personal income taxes remained the two largest sources of tax revenue for the fiscal coffer, the room for maneuvering is limited without diluting Singapore's overall competitiveness.

Indeed, Singapore is already facing immediate threat to its corporate income tax revenue. The forthcoming revision to the tax incentives for MNCs to raise effective tax rate to comply to the OECD Inclusive Framework on BEPS will be keenly watched. A right balance would have to be achieved and careful calibration of the Minimum Effective Tax Rate (METR) to meet the Global Minimum Tax Rate of 15% would be crucial. The tax "top-up" may derive additional revenue, but the risk is that it may not be enough to offset the potential loss in tax revenue resulting from Pillar 1 of BEPS [3]. There is concern on whether the island state will be able to retain its allure to global companies when its effective tax rate is adjusted up to align to BEPS standard. In this regard, **Singapore must continue to strengthen its overall value propositions to global companies beyond just tax incentives**.

Downside risk on corporate tax revenue

Raising wealth taxes and the personal income tax rates for top tier income earners were also announced to buttress Singapore's fiscal position and to ensure its tax system remains progressive. With effect from YA2024, the Personal Income Tax (PIT) rate for income above SGD 500,000 will be raised to 23% while income more than SGD 1mn will be taxed at 24% [4]. Luxury car buyers would now have to pay higher ARF rate (220%) and significant changes were also made to property tax policy to enhance its progressivity – higher rate for property of higher value. Simply put, high income earners will be confronted with a multiple whammy of tax increases in the coming years (e.g., personal income tax, property tax, ARF for luxury car and GST). As such, **some negative wealth effect on consumption of luxury goods and property investment is to be expected.**

Changes in property tax

Annual Value	Property tax rate for owner-occupied residential properties		Annual Value	Property tax rate for non owner-occupied residential properties	
	Effective 1 Jan23	Effective 1 Jan24		Effective 1 Jan23	Effective 1 Jan24
First $8,000	0%	0%	First $30,000	11%	12%
Next $22,000	4%	4%	Next $15,000	16%	20%
Next $10,000	5%	6%	Next $15,000	21%	28%
Next $15,000	7%	10%	> $60,000	27%	36%
Next $15,000	10%	14%			
Next $15,000	14%	20%			
Next $15,000	18%	26%			
> $100,000	23%	32%			

Source: MOF

The much-anticipated GST hike was also announced. Though the timeline did come as a surprise, the silver lining is perhaps on the fact that the 2%-pts increase to 9%, from 7% currently, will be delayed till

2023 and staggered over a period of 2 years (2023-2024) amid concerns of rising inflation. The Assurance Package was also enhanced to $6.6bn to render more support for the lower income group. We expect the GST changes to yield an additional S$3.2bn for the fiscal coffer after the hikes have fully taken effect, which together with all the other tax adjustments should help to bolster the fiscal position.

Another fiscal deficit

The fiscal deficit for FY2021 (SGD 5.0bn, 0.9% of GDP) was smaller than originally budgeted (SGD 11bn) but in line with our forecast [5]. The economic recovery turned out stronger than anticipated, which buttressed revenue collections. Spending was also lower than budgeted, especially in developmental expenditure as some infrastructure projects were delayed due to the COVID situation.

Singapore's overall fiscal position

	Actual FY2020	Revised FY2021	Budgeted FY2022	Change over Revised FY2021	
	SGD bn	SGD bn		SGD bn	% change
Operating revenue	**67.4**	**80.4**	**81.8**	**1.4**	**1.7**
Less:					
Total expenditure	**86.4**	**98.4**	**102.4**	**4.0**	**4.1**
Operating expenditure	72.9	81.5	85.1	3.5	4.3
Developmental expenditure	13.4	16.9	17.3	0.5	2.8
Primary surplus/deficit	**-19.0**	**-18.0**	**-20.7**		
Less:					
Special transfers	**50.8**	**7.9**	**6.2**	**-1.7**	**-21.0**
Special transfers excluding top-ups to endownment and trust funds	33.5	7.9	2.2		
Basic surplus/deficit	**-52.5**	**-25.9**	**-22.8**		
Top-ups to endownment & trust funds	17.3		4.1		
Add:					
Net investment returns contribution	**18.2**	**20.3**	**21.6**	**1.2**	6.0
Overall budget surplus/deficit	**-51.6**	**-5.6**	**-5.4**		
Add:					
Capitalisation of nationally significant infrastructure		0.7	2.4		
Overall fiscal position	**-51.6**	**-5.0**	**-3.0**		
Overall balance as % of GDP	**-10.8**	**-0.9**	**-0.5**		

An overall fiscal deficit of about SGD 3bn (0.5% of nominal GDP) is allocated for Budget 2022. This came as a surprise as expectation was that the government may be eager to accumulate fiscal surplus amid the recovery, which can then be deployed to cushion the negative effects of tax increases in subsequent years. In fact, even if a modest surplus is not feasible, a 2%-pts GST hike in 2H22 would help to generate at least about SGD 1.6bn in FY2022, essentially offsetting about half of the projected fiscal deficit.

Tight fiscal balancing ahead

The average annual balance over the ten-year period (FY10-19) prior to the COVID pandemic was about SGD 3bn. Assuming growth remains stable in the coming years, policymakers would very likely be able to offset the existing deficit, and still achieve its mandate of a balanced budget in the current term of government. However, there is downside risk on corporate tax revenue inflow due to BEPS 2.0, which could dampen the fiscal position. The impending series of tax hikes (GST, PIT, carbon tax, property tax etc) will also take a toll on growth performance and may require additional fiscal offsets to mitigate the economic impact. Yet, the biggest concern is that given economic cycles are becoming more volatile and unpredictable in recent times, **Singapore could be sandwiched between rising taxes and falling growth should another recession occur in the next 2-3 years**.

Notes:

[1] More details on the **Jobs and Business Support Package** (https://www.mof.gov.sg/docs/librariesprovider3/budget2022/download/pdf/annexa1.pdf); the **Household Support Package** (https://www.mof.gov.sg/docs/librariesprovider3/budget2022/download/pdf/annexa2.pdf) and the **enhanced GSTV scheme** (https://www.mof.gov.sg/docs/librariesprovider3/budget2022/download/pdf/annexf4.pdf)

[2] More details on the tightening of foreign manpower policies (https://www.mof.gov.sg/docs/librariesprovider3/budget2022/download/pdf/annexc4.pdf)

[3] BEPS Pillar 1 re-allocates the profit of the largest and most profitable MNEs, from where activities (e.g, RHQ) are conducted to where consumers are located

[4] Top tier Personal Income Tax rate was raised to 22% in 2017, from 20% previously

[5] See DBS report "Singapore Budget 2022: Refocusing on long-term priorities" dated 27 Jan22

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