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# Does Singapore Need Economic Restructuring II or Another 'Wage Revolution'?

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Economic Growth Centre, NTU.

# DOES SINGAPORE NEED ECONOMIC RESTRUCTURING II OR ANOTHER ‘WAGE REVOLUTION’?<sup>1</sup>

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## Abstract

In this paper, Professor Lim first discusses the circumstances that led to the urgent need to embark on the Economic Restructuring I in 1979 and assesses the *modus operandi* used then to achieve the restructuring objective. He then compares the changed circumstances of today's economy, which has a new set of problems and priorities. He advocates another formal economic restructuring exercise (Economic Restructuring II) and proposes recommendations to restructure the present economy. His iconoclastic and likely to be controversial recommendations are based on the economic principles used in the Economic Restructuring I, but with the additional objectives of checking the trend of rising income inequality and lessening the over-reliance of cheap foreign labour import.

Keywords: Economic restructuring; income inequality; labour market; foreign workers

JEL Classification: O29, D63, J21

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Prelude

*Ill fares the land, to hast'ning ills a prey,  
Where wealth accumulates, and men decay.*

Oliver Goldsmith  
“*The Deserted Village*”

**Economic Conditions in Singapore in late 1970s**

(surfeit of low-wage workers)

- \* Low-wage occupations: *ubiquitous*
- \* Low-wage manufacturing: *common*
- \* General technology level: *low, very low*
- \* Women employment: *low*
- \* General under-employment: *rife*
- \* Wind of change in East Asia, particularly China

**Economic Restructuring I (1979 – 81)**

Singapore went through a formal economic restructuring exercise for three years, 1979 – 81, during which:

- (1) Wage rates were increased across-the-board cumulatively by 20% per year;
- (2) A portion of the wage increase went to CPF through increases in employers’ and employees’ contributions;
- (3) Another portion of the wage increase, 4% of wages below a certain level, went to a newly-created tripartite-run Skills Development Fund;
- (4) The new Skills Development Fund Advisory Council oversaw the administration of the Fund with twin objectives
  - (i) Substantial across-the-board subsidy for *training and re-training* of employees at all levels opened to all employers in Singapore.
  - (ii) A common-playing-field substantial subsidy for the mechanization of the production processes opened to all employers in Singapore.

### **Need and Objective of ER I**

The overall objective of the restructuring exercise was to move the old traditional economy from a low-skilled, low-value-added and highly-labour-intensive structure to a high-skilled, high-value-added, and more technology and more knowledge-based new economy. The need for restructuring was urgent in view of increasing competition from new emerging and developing economies in East Asia particularly following the opening-up and the robust new industrialization programme of the People's Republic of China since 1978.

### **Five-Point Observations on ER I**

Five general observations of the first formal economic restructuring exercise (1979-81) will be made here.

- (1) It was self-funded, or strictly speaking, funded by the employers, not by the Government through higher taxes or from quantitative easing, or from accumulated reserves or otherwise.
- (2) The exercise was very focused with only one Government-appointed tripartite agency, the Skills Development Fund Advisory Council, overseeing the exercise.
- (3) The “means” for the restructuring objective was also much focused. The means were only two: one, mechanization, that is, the substitution of capital for labour, and two, training and re-training of workers, particularly technologically replaced workers.
- (4) Even the training and mechanization programmes were highly focused: mechanized and trained to meet the anticipated demand of the employers; not training for the sake of training and mechanization for the sake of mechanization.
- (5) Lastly, the *modus operandi* was through inducement, incentives and disincentives programmes, and not direction. Market forces were given a full reign. The Skills Development Fund was merely providing the direction, the support, the philip and the accelerator. The SDF merely provided the GPS.

### **Success of ER I**

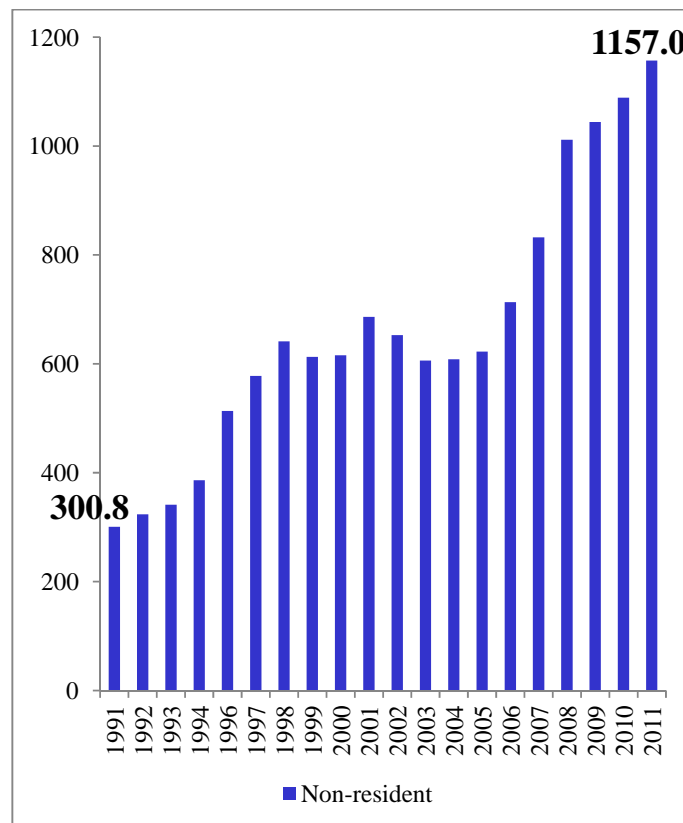
Despite some teething problems, the then considered bold and iconoclastic restructuring exercise was a great success. Real GDP displayed high real growth rates of 9.4% in 1979, 10.0% in 1980 and 10.7% in 1981. After 1981, the built-in restructuring momentum continued unabated until the regional recession year of 1985.

### **Subsequent Low-Wage Labour Import**

Since 1985, fearing that the Singapore economy would become internationally uncompetitive, we gradually and imperceptibly eased the moratorium on the intake of lowly-paid, lowly-skilled foreign labour. Non-resident labour force increased steadily from 300.8 thousand in 1991 to 1.157 million in 2011, as shown in Diagram 1, which is based on published official statistics. GDP, as expected, expanded *pari passu*, as impressively as the inflow of lowly-paid foreign labour.

Diagram 1

**Increasing Supply of Non-resident Labour Force ('000)**



Source: CEIC database (retrieved on 15 Feb 2012)

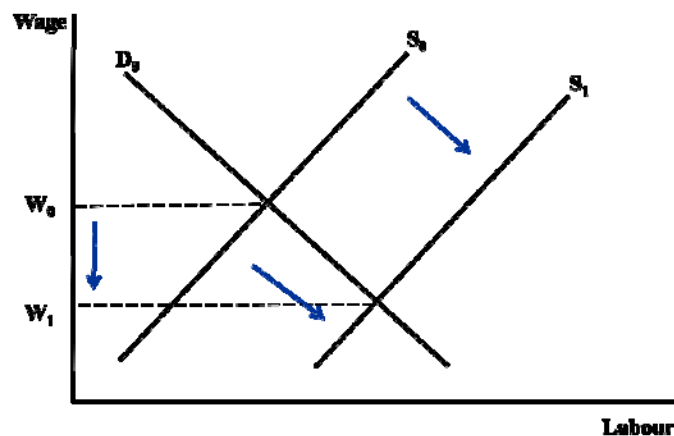
It cannot be over-stated that successful economic restructuring can only take place with a moratorium on cheap labour import. There is, as you know, an unlimited supply of lowly-paid foreign labour in our region. One cannot substitute capital for labour, if labour is cheap. That was why the NWC in 1979 recommended a cumulative 20% increase in labour cost per year for the restructuring years of 1979-81.

### Adverse Impact on Domestic Wage Rates

Below is a simplified diagram to illustrate this often forgotten simple principle of price in relation to supply and demand. Diagram 2 shows that an increase in the supply of labour, *ceteris paribus*, brings down the wage rate from  $W_0$  to  $W_1$ .

Diagram 2

#### Wage Rates and Labour Supply



#### Different Perspectives

**耕田欲雨刈欲晴，去得顺风来者怨**

*Rainy days are preferred when crops are growing, sunny days are preferred when harvesting.*

*If you are moving in the direction of the wind when you are leaving, those who are coming in the opposite direction will be complaining.*

### **Does Singapore Need Economic Restructuring II?**

Do we need another economic restructuring now in 2012, as opposed to the one we had in 1979, 33 years ago? Political, economic and social conditions then and now differ strikingly. Our per capita income then in 1979 was US\$4,071, one of the lowest in the world and in 2011, US\$50,123, one of the highest in the world. The level of technological advance too has been dramatic, from, for example, as shown in Diagram 3, a coolie carrying a bag of rice at his back in a tongkang at the mouth of the Singapore River to one of the first-rate, world-class containerized ports in the world. Then, we had a reservoir of untapped, under-utilized and mis-utilized domestic labour force with a very low participation rate of female labour. Now the female participation rate has become so high that the real problem and the real casualty is the serious decline in family formation, which is a pointer to our future succession, population renewal and survival.

Diagram 3



**Source: Copyright Singapore Press Holdings)  
Prime Minister Lee Hsien Loong's National Day Rally Speech, 16 August 2009**





**Source: Singapore PSA, *Portview*, 1Q 2012, pg 22**

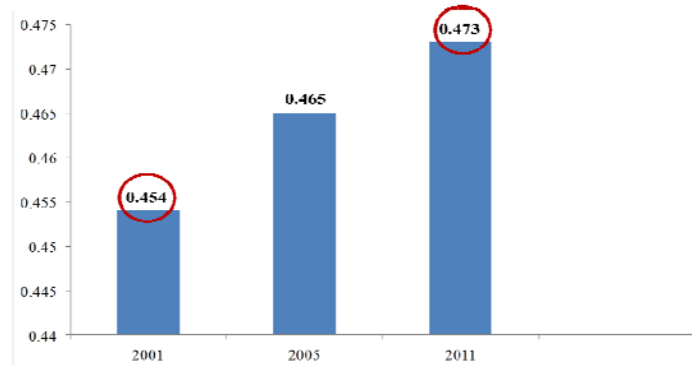
However, the distinguished presiding Chairman of this meeting, Mr Ho Kwon Ping, said not too long ago that Singapore needed another wage revolution to complete the 1979-81 successful wage revolution. He added that the first wage revolution had been most successful only in the manufacturing sector, but not in the other sectors, such as in the construction industry, the retail trade sector and the household sector. We all are aware now that we have 1.157 million non-resident workers, not like in 1979. However, I must hasten to add that I am thankful that these foreign workers have chosen Singapore to work, instead of other countries, and that it is not their fault or shortcoming that our employers, out of sheer necessity, have chosen to employ them to work here in Singapore.

### **Increasing Income Inequality, Another Achilles' Heel**

In recent decades, consequent on globalization and technological advance in a largely market-oriented global economic system, the world economy, particularly in advanced and emerging economies, has been faced with increasing and disconcerting income inequality. Much of the research work in this field has been very ably done by the OECD, the IMF, the World Bank and by the ILO. In Singapore, the twin pulls of income inequality have taken on the pull away from the centre by both the lowest-income and the highest income groups, pulling away from the centre at both ends in the opposite directions by the two groups. The global contagion forces pull up the highest income groups whilst the increasing inflow of much cheaper foreign labour pulls down the lowest income groups. Singapore's fairly bad Gini-coefficient, as shown in Diagram 4, thus exacerbated further from 0.454 in 2001 to 0.473 in 2011. The  $P_{90}/P_{10}$  index, another frequently used measure of income inequality,

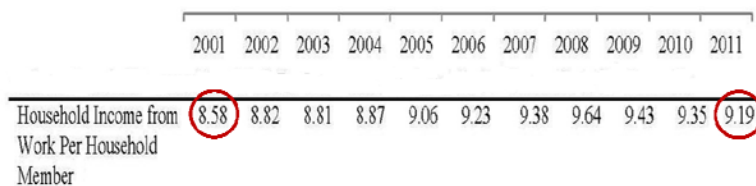
increased from the already high index of 8.58 in 2001 to 9.19 in 2011, as shown in Diagram 5. A Gini-coefficient of 0.5 is normally considered a dangerous line to reach, far less to cross, and we have reached 0.473, according to official estimates, in 2011.

Diagram 4  
**Gini coefficient Among Employed Households  
 2001, 2005 and 2011**



Source: *Key Household Characteristics and Household Income Trends*, 2011, p. 16

Diagram 5  
**Ratio of Household Income From Work Per Household Member  
 at the 90<sup>th</sup> Percentile to 10<sup>th</sup> Percentile**



Source: *Key Household Characteristics and Household Income Trends*, 2011, p. 16

On Singapore’s increasing Gini Coefficient in the last decade or so, it may interest you to note that in 1985, when the Third Edition of one of our best-selling Economics College Texts “*Economic Structure and Organisation*” was written, the Gini Coefficient, as shown on page 303 in Chapter 8 “Income Distribution”, actually showed a declining tendency, reaching 0.422 by 1980, as opposed to the present 0.473. Individual and company income taxes then were much higher and there were inheritance taxes. There was no GST then. Besides, NWC

was recommending quantitative guidelines with dollar quantum favouring the lower income groups in percentage terms.

Diagram 6

<b>Year</b>	<b>Gini Coefficient</b>
1966	0.494
1973	0.474
1975	0.459
1980	0.422

### **Solution to Problems of the Two Achilles' Heels?**

As a solution to the new problems of increasing income inequality and the excessive reliance on cheap foreign labour import, I would like to propose Economic Restructuring II operational for three years, with the following six features.

#### **(1) Sizable Pay Increase for Lowest Income Workers**

One, that all workers' pay below \$1500 per month be cumulatively increased by 15% in year one, 15% in year two and 20% in year three. This increase is applicable to all workers, local or foreign, if he or she draws a pay of less than S\$1500 per month. A dollar quantum is also to be included in the increase pay package.

#### **(2) Part of Pay Increase to SDF and RA**

Two, that one third of the increase pay package be channelled to the Skills Development Fund, one-third in the form of take-home pay and the other third to CPF Retirement Account (RA). For foreign workers, it will take the form of ex-gratia payment upon leaving Singapore on expiry of tenure. The SDF should be re-activated, re-vitalized and re-invigorated to perform the functions of (1) training and re-training of workers, (2) mechanization and technological upgrading and (3) better employment of labour through re-designing in labour use. The restructuring momentum has to be re-generated and sustained. The buzzwords should continue to be "use one worker instead of two".

(3) **Moratorium on Pay of Highest Income Groups**

Three, **those who receive \$15,000 a month or more will have their wages or salaries frozen for three years only during former Economic Restructuring II.** There is no proposal for a pay-cut or a pay-ceiling or super-taxes for high-flyers, only a moratorium on pay increase for three years. The intention is not to frighten the geese that lay the golden eggs. No Wall Street protests of the kind in the US should ever be envisaged. Company income tax then was 40%, now 17%. The maximum personal income tax then was 55%, now 20%.

(4) **Moderation for Middle Income Groups**

Four, **those whose pay is between \$1,500 per month and \$15,000 a month will receive a quarter to a third of those less than \$1,500 per month.** A portion should still go to the much inadequate CPF Retirement Account.

(5) **Government Co-Payment of SDF**

Fifth, the state (or the Government) should contribute to the SDF on a 1 to 1 quid pro quo basis to demonstrate tripartite commitment, participation and responsibility in the new economic restructuring process.

(6) **Involvement of NWC Absolutely Necessary**

Six and lastly, like in Economic Restructuring I, the *modus operandi* of Economic Restructuring II, including the operational details, should be discussed and decided upon by the tripartite National Wages Council, which has to forge consensus by the three tripartite social partners, as in 1979.

**Restatement of Objectives ER II**

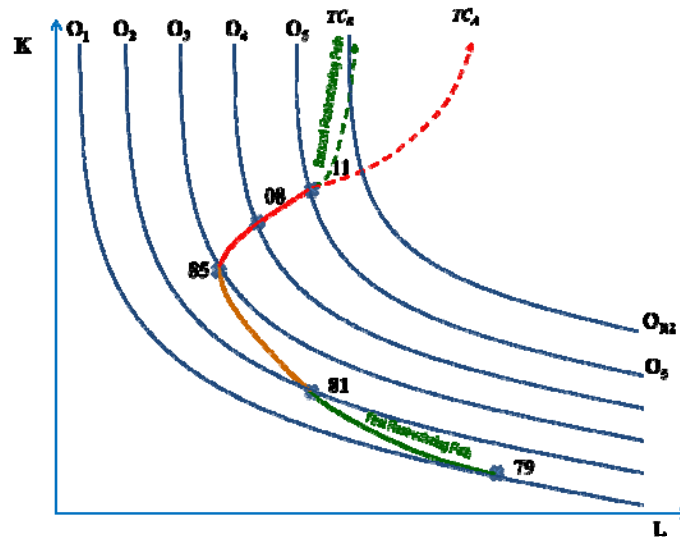
In other words, **the basic objectives of Economic Restructuring II are (a) to check and to halt and if possible to reverse somewhat the disturbing increasing income inequality trend, (b) to increase productivity, total factor productivity, as a growth target and (c) to check and to halt the trend towards increasing reliance on very much cheaper imported labour to generate quantitative GDP growth.** The overall objective must be, and should be, to enhance further the quality of life of all those who live and work in Singapore, and in particular, for those whose home and country is Singapore. With ER II, we will have a stronger, more robust, and more productive economy and a fairer, more just

society. With ER2, hopefully, our very low and embarrassing Wage/GDP ratio can return to a less embarrassing position in three years.

### **Economic Restructuring Models I and II**

Let me now put the first and the second restructuring model in a simple diagrammatic form to round-off this presentation. The curves in Diagram 7 are isoquant curves. They show factor proportions between capital and labour. The higher the curve the higher is the output. The model is not drawn to scale. Only inflexion years are shown. We moved successfully from 1979 to 1981 in the first restructuring exercise. We gradually changed our course after the economic trauma of 1985. If we continue at the present course without the slowing down or curtailment of lowly-paid foreign labour import, our GDP will take on the route of Transformation Curve A with all the negative implications on income distribution, increasing demand for public services, and congestion. If we restructure our economy following the first model, *mutatis mutandis*, our economy would move along  $TC_B$ . I opt for  $TC_B$ .  $TC_B$  also implies a slight improvement to the Gini coefficient which, as has been stated, has shown a disturbing deteriorating trend. Economic Restructuring II, if successfully carried out, also means the lessening of the need for increasing taxation, including GST to meet the multi-faceted needs for subsidies and transfers. Economic Restructuring II hits the basic ER problem on the head.

Diagram 7  
Restructuring Model I and II



$TC_A$  means transformation curve A

$TC_B$  means transformation curve B

### Concluding Remarks

Finally, it is much more difficult to have national economic restructuring now than three decades ago. The politico-economic and the socio-economic environment have changed. But what has not changed, however, is that we still have *effective tripartism* and we still have a *government* and the *civil service* that are among the best in the world in cleanness, integrity and ability. Economic restructuring needs a national will. Do we have it now, as we had it then, a little more than three decades ago, but now, we are faced with a new set of economic problems, which may be called the problems of economic success? Previously, we called Growth with Equity. Now, we call Inclusive Growth. I have no doubt that Economic Restructuring II will bring Inclusive Growth to a more respectable and a more meaningful level. I recognise, however, that Economic Restructuring II as proposed by me is but one way of achieving the aims of Inclusive Growth, probably, in my view, the best way.

We were the first country in the world to have the then bold and iconoclastic Economic Restructuring I some 33 years ago and we will be the first country in the world now to have a formal Economic Restructuring II, also bold and iconoclastic and for another three years.

Postscript

*Ring out the grief that saps the mind,  
Ring in the nobler modes of life,  
Ring out the want, the care, the sin,  
The faithless coldness of the times,  
Ring in the larger heart, the kindlier hand,  
Ring in the love of truth and right,  
Ring in the common love of good.*

Adapted from  
Lord Alfred Tennyson  
“*Ring Out the Old,  
Ring In the New*”

Thank you for coming and listening.