

Instead of drawing from Temasek's dividends, the Government will now use Temasek's long-term expected return to compute its contribution. This includes consideration of dividends, but also of realised and unrealised capital gains.



The substantial addition to the net investment returns contributions reflects the large capital-gains component of Temasek's equity-dominated portfolio returns.
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Paying for that surge in Budget spending

By **CHAN KOK HOE**
FOR THE STRAITS TIMES

BUDGET 2015 calls for a massive \$11 billion rise in expenditure on the previous year.

While substantial grants are planned for the middle class, the poor and elderly, innovative businesses and workers keen on skill mastery, a large proportion of the increased spending has gone towards improving Singapore's transport and logistics infrastructure.

Development expenditure will increase by more than 40 per cent over FY2014 and is expected to grow to \$30 billion by the end of the decade. By then, overall spending will have reached 19.5 per cent of gross domestic product.

How does the Government plan to pay for all of this? For the current Budget year, the Government has eschewed tax increases, choosing instead to run a deficit of \$6.7 billion, or 1.7 per cent of gross domestic product (GDP).

Both the corporate income tax and the goods and services tax (GST) are unchanged. A sizeable \$717 million rebate will result in personal income tax receipts falling in FY2015. While top personal income tax rates are due to rise in 2017, this is designed to raise only sufficient funds to cover the \$350-million-a-year Silver Support Scheme (for the elderly poor).

Deficit spending is made possible because the Government holds

ample current reserves. Indeed, the report on FY2014's fiscal position reveals a substantial boost to current reserves. The Government incurred a deficit of \$130 million, which was \$1 billion smaller than initially estimated. The FY2013 Budget surplus has also received an upward revision – it is now \$5 billion, rather than \$3.9 billion.

That revisions tend to improve the fiscal position is unsurprising. The Government has a track record of being prudent and conservative in its Budget estimates, often underestimating revenues and overestimating expenditures. But it is worthy to note that the revision for FY2014 is considerably lower than the \$1.5 billion to \$3 billion that analysts from OCBC, DBS and UOB had expected.

It also marks the third consecutive year of declining revisions. It is likely that the Government has improved the accuracy in its estimates, though the fact that 2014 economic growth was almost exactly as projected also helped.

These upward adjustments boost current reserves to about \$15 billion, which is more than sufficient to finance the \$6.67 billion projected deficit.

The remaining current reserves could help finance another Budget deficit in FY2016, but not beyond. This is because the next general election must be held by January 2017, and current reserves must be transferred to past reserves when the Government's current

term ends.

Temasek boost to budget revenue

THE bulk of the needed revenue increases beyond FY2016 will come from higher net investment returns contributions (NIRC).

Under the Net Investment Returns (NIR) Framework in the Constitution, the Government is allowed to draw up to 50 per cent of the long-term expected returns on investments managed by GIC and the Monetary Authority of Singapore, plus up to 50 per cent of investment income from other sources, including dividends issued by Temasek Holdings.

The finance minister revealed in Parliament last April that the Government uses the full 50 per cent limit in its budgeting.

Higher NIRC, together with the adjustments to top personal tax rates, will add yearly revenues equal to 1 per cent of GDP. Since the NIRC for FY2015 is estimated to be \$8.94 billion, this suggests that the Government expects the NIRC for FY2016 to be close to \$13 billion, or about 3 per cent of GDP. This would make the NIRC a larger contributor to revenues than the GST.

This dramatic rise in the NIRC comes from including Temasek Holdings in the full NIR Framework.

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long-term expected returns to compute its contribution. This includes consideration of dividends, but also of realised and unrealised capital gains. The substantial addition to the NIRC reflects the large capital-gains component of Temasek's equity-dominated portfolio returns.

Will tax rates rise in FY2017?

THE larger NIRC, together with increases in revenues from an economy growing at 3 per cent a year, will be sufficient to pay for the increased spending. But without additional revenues, the Government may no longer be able to run sizeable Budget surpluses.

Because the Constitution disallows it from borrowing to pay for expenditures, and it cannot tap past reserves without the President's approval, the Government needs to run Budget surpluses to generate fiscal breathing room.

Unless the economy is unusually buoyant or long-term net investment returns recover to pre-2007 levels, there is a decent chance that the Government may have to revisit the issue of raising tax rates in FY2017.

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