Mizuho Flash: Singapore Budget

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MIZUHO

Singapore Budget (2022) Preview: Fiscal SIN

In a Nutshell: Singapore's **Budget 2022** will be forged in **sustainability**, **inclusivity** and **navigability** (SIN). Achieving a budget that ensures **a virtuous economic cycle is dependent on a SIN-ful** (forgive the acronym) **fiscal approach**, it appears. After the exceptional draw-down due to the pandemic, **balancing the overall Budget balance will be a key imperative**. But fortunately, a more gradual glide-path to primary fiscal balance mitigates the risks to growth.

Fiscal consolidation led by diminished need for emergency support as the recovery broadens will be **complemented by an impending** 2%-point GST hike (to 9%). This is projected **to add some S$3.5-$3.8bn annually** (initially), and will propel GST as the second largest contribution (of~20% from 16.6%) to tax revenues after corporate taxes (overtaking personal income tax). In turn, cementing the notion of **fiscal sustainability being reinstated**.

Environmental sustainability, most prominent in a likely hike in carbon taxes (from S$5/tonne to S$10-15/tonne), will nevertheless be far more pervasive as a core of, and not merely an after-thought complement to, economic progress. **Inclusivity** will feature prominently as a conspiracy of *surging asset prices* and *imposing cost-push* **threaten to drive a deleterious wedge that deepens income, and more damagingly, wealth disparities**. Given an already progressive income tax rate brackets, the surge in property values and ease of taxing property, **wealth taxes via property that is being widely speculated** is as sensible as it is pragmatic.

Finally, the **navigability of the Budget** to **enhance socio-economic mobility** on the domestic front, and bestow the ability to **navigate greater economic and geo-political uncertainties** remain **key to virtuous economic outcomes**. Speaking of which, **SGD allure may also be accentuated** *insofar that the Budget reinforces the notion of further MAS tightening;* including re-centring of the S$NEER mid-point higher.

Sustainability

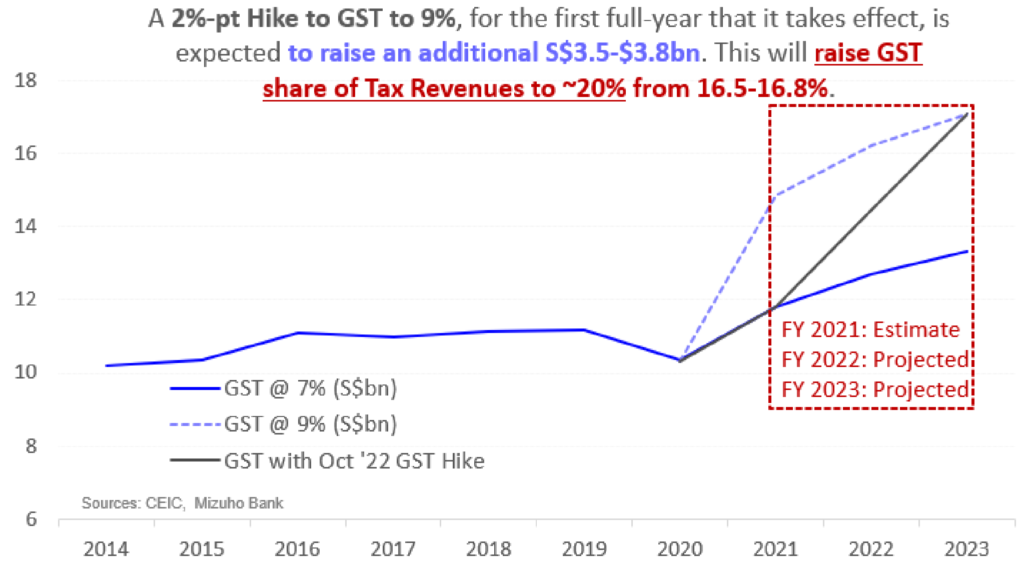
Sustainability will undeniably be a multi-dimensional corner stone of this budget. And there are two prominent aspects to sustainability. One is *fiscal sustainability,* which arguably needs reinstating after a large drawdown from past reserves in response to pandemic; especially given that demographics will impose rapidly escalating healthcare burden. In other words, ensuring that recurring budget commitments are inherently and adequately financing so that risks associated with ballooning fiscal debt may be averted.

The other, *environmental sustainability,* which is not merely a complement, but a critical element, for economic progress and social well-being.

Fiscal Sustainability

Balancing the Budget: After the **exceptional drawdown on past reserves in blowout pandemic budget** (13.8% deficit) in FY2020 **to justifiably save jobs and avert a balance sheet crisis** that transitioned to a supportive FY2021 budget (of a far more measured deficit*) to entrench the recovery, **balancing the books in FY2022 is not only prudent, but arguably necessary**.

But not Breaking the Economy: The **good news is that need not abandon economic support**. Fact is, healthy NIRC (net investment returns contribution) and infrastructure capitalization allow the **overall fiscal position to turn a modest surplus** (Mizuho: 0.2% of GDP) whilst **the underlying fiscal position remains supportive; amid a much gentler glide path to primary deficit consolidation**.



The Poster Boy GST Hike: And the impending **2%-point hike to the GST** (goods and services tax) to 9% (from 7%) will undeniably be **the "Poster Boy" of "wide-based" fiscal providence**. By our estimates, this will **bump-up GST collections by some S$3.5bn-S$3.8bn in the first full year after it takes effect**. As a result of which, *GST will overtake personal incomes tax to be the second largest source of tax revenues* (after corporate taxes) as its *share of tax revenues is raised to around 20%* from ~16.6% (FY2017-2019 average).

Prudent & Progressive: The resultant **widening of the tax base is not just welcome, but desirable**; as reliable revenue offset for foreseeable and significant rise in healthcare burden is consistent with the **fiscally-prudent principle of not resorting to debt financing for recurring expenses**. Moreover, this **inherently regressive** (hitting low income households hardest) **GST hike successfully side-steps risks of being a whipping boy** with a previous created accommodation by means of a **S$6bn "Assurance Package" entailing means-tested, medium-term GST offsets**; which not only ensure low-income households are not worse-off, but holistically render the Budget more progressive.

But Flirting with Inflation Risks: Despite **conviction that this GST hike is needed for fiscal sustainability**, and **comfort with equitable fiscal transfers ensuring progressivity** of tax measures, we have *reservations about the timing the hike to coincide with inflation crescendos amid unpredictable waves of cost-push.* Not because we mistakenly reject the notion of GST as a one-off impact. Rather because despite conceding to GST's impact in isolation, we are *wary of price expectations and second-round effects conspiring to inadvertently compound inflationary outcomes.*

Counter-intuitive One-off Hike: In light of these unknowns, **a counter-intuitive approach of a one-off hike to GST to spare the system of multiple waves of expectations** and **administrative adjustment costs** may be preferable though we are sympathetic to a phased increment that may be looking to temper imminent cost-push impact.

Environmental Sustainability

Environmental sustainability will invariably not feature in just this budget, but will be in the DNA of all budgets to follow. From **longer-term green infrastructure commitments** (*e.g., charging stations for electric vehicles, on-going investments in cleaner modes of mass transport, building codes that are rendered even "greener", preventive engineering to mitigate the threat of rising sea levels*) t**o tax/cost incentives to "nudge" more environmentally-conscious social and economic outcomes**. This time around, this will prominently feature a lift in carbon taxes from S$5/tonne to S$10-15/tonne. But **unlike GST hike, concerns about unintended, adverse second-round inflation impact are a non-issue** as the hike looks set to come into effect only in 2024.

Inclusivity

And if sustainability is the cornerstone, **inclusivity must be the foundation upon which the Budget is designed**. The **importance of which cannot be overstated**, given that a conspiracy of *surging asset prices* (amid exceptional global policy largesse) and *imposing cost-push* **threaten to drive a lasting and damaging wedge that deepen not just income, but more damagingly, wealth disparities**. There is wisdom in appreciating that social cohesion is a pre-condition to durable economic prosperity, and that road must course a path to shared prosperity. To this end, and in budget speak, **"fiscal transfers" will be an important means** to ensure inclusive economic outcomes.

Wealth Tax is the Right Tree(-House): But with **already very progressive income tax brackets**, and apart from perhaps adding another layer of differentiation at the top, the **more effective route to addressing inequality** enroute to establishing **inclusivity**, must entail **some form of wealth taxes**. So, unsurprisingly, **wealth tax is all but a done deal**; especially given that the **wealth inequality is far more serious a problem** than is income disparity, with the *wealthy often **benefit disproportionally more from capital gains** that are exempt from income tax.*

What's more, wealth inequality also **compounds far more dramatically**. And so, **wealth tax** as a means to address is **barking up the right tree**. And speculation is that this will be **in the form of a property-related tax** is as a **sensible** as it is **pragmatic** given a surging property market (that has deepened the disparity) and the ease of implementation (on an unmovable and sizable barometer/source of wealth).

Whereas Estate Duties May be the Missed Opportunity: But while another iteration of a wealth tax that is without a doubt a step in the right direction, it nevertheless falls short. In particular, **given that the demographics will entail unprecedented scale of bequeathing** in the years to follow, **failure to reinstate estate duties** (sensibly measured and with appropriately high exemptions so as not to hit the aspirations of Middle-income families) is undeniably **a missed opportunity to marginally alleviate unfavourably stacked social odds in a land scare city state**.

Neither "Robin" nor Robbing: And **fear of capital flight or dis-advantaging the wealth management sector should not get in the way of a fair and well-thought implementation of wealth/estate taxes**. To be sure, this is **not advocacy of "Robin Hood" type policies** predicated on "robbing" the rich and feed the poor". Far from. Just as how GST should not be seen a regressive tax but appreciated as a progressive tax with the complement of transfers, **wealth taxes should be appreciated as mean to even the playing field and actively ensure socio-economic mobility –** *the only enduring preventative cure against entrenched and deleterious class divisions* that may inadvertently set the stage for tipping point risks with regards to self-defeating "Robin Hood" type populism.

Navigability

And that brings us to the third and critical element of navigability of the Budget. A Budget must have the **navigability** to **not just sufficiently ride out domestic challenges** to the economy and social issues but perhaps maximize its potential for its given social/demographic constraints. In addition, it also entails the **ability to traverse global economic and geo-political uncertainties**.

Socio-Economic Mobility: Clearly **inclusivity in and of itself, is insufficient if solely reliant on "fiscal transfers"**. Rather, **a Budget that enhances socio-economic mobility**, that expressly impresses upon its populous possibilities unlimited and unimpeded by starting points, **over the long-run maximizes on the country's human capital potential**. And the latter ability is a critical pre-condition to achieve **desirable economic outcomes for a resource-constrained economy**. Resultant social cohesion is as much a by-product as it is a contributor to future economic prosperity.

Point being, **a Budget builds on emphasis on equality of access** is, as or more important, to one that attempts to gauge and implement greater equality of outcomes – which tends to be far more fraught with complexities and pitfalls. And to that end, the focus on programs such as SkillsFuture, re-training, and efforts to alleviate entrenched disadvantages in education (across varying socio-economic backgrounds) remain critical.

Future Capacity & Capability: Equally, a Budget that **builds on capacity and capabilities** across various fields/spectrums and modular in nature so as **to successfully navigate a rapidly changing global economic and geo-political** landscape helps build resilience.

To this end, the **longer-term approach to infrastructure investments, financing and capitalization** will help align longer-term goals to the Budget. Further, **dynamic tax-subsidy shifts to incentivise new and high-potential industries**, with a view of acquiring capabilities, will also be critical in the context of the global minimum tax initiatives. In addition, financial/upskilling initiatives ensuring that SMEs can scale up and go regional to achieve scale up as well as tap on evolving regional manufacturing eco-systems must also remain a key aspect of the Budget.

Virtuous SIN & SGD

Our view is that the budget will by and large achieve that which it sets out to. That is, a **fiscal strategy rooted in sustainability, inclusivity and navigability** (SIN). And the **virtuous economic outcomes from SIN** will lend to a more positive economic outlook. In turn, this will **reinforce our view of further tightening by the MAS** (with a likely loftier re-centring of the S$NEER mid-point in April followed by further slope increments in October), which, all else equal, will **correspond to a sinfully appealing SGD**. Especially if interest in Singapore's infrastructure bonds add to inflows from foreign investors.

** We estimate FY2021 would show a deficit of 1.8%, smaller than the 2.1% deficit projected by the MoF.*

S$bn	Actual		Budget	*Mizuho Est.*	
	FY 2019	FY 2020	FY 2021	FY 2021	FY 2022
Operating Revenues	74.3	64.6	76.6	78.7	87.0
% of GDP	14.5%	13.8%	14.7%	15.1%	15.6%
Income (I/C) Tax*	32.5	30.6	34.5	34.5	37.5
Asset Taxes^	4.8	3.1	4.7	4.7	5.1
Tax on MV	2.4	2.2	2.5	2.6	2.8
Customs & Excise	3.3	3.5	3.8	3.9	4.3
Betting Taxes	2.6	1.8	2.4	2.4	2.7
Stamp Duties	4.2	3.7	4.3	4.8	5.2
GST	11.2	9.9	11.3	11.8	14.4
COE	2.9	2.3	2.3	3.1	3.5
Others**	10.4	7.5	10.8	10.8	11.5
Total Expenditure	75.3	94.1	102.3	101.7	104.0
% of GDP	**14.8%**	**20.1%**	**19.7%**	**19.5%**	**18.7%**
Operating Expenses	58.7	77.6	82.5	82.5	84.1
Development Expenses	16.7	16.4	19.9	19.3	19.9
Primary Balance	-1.1	-29.4	-25.7	-23.1	-17.0
% of GDP	**-0.2%**	**-6.3%**	**-4.9%**	**-4.4%**	**-3.1%**
Less Special Transfers	15.1	53.6	4.9	7.1	5.8
Add: NIRC***	17.0	18.1	19.6	20	22
Overall Balance	0.8	-64.9	-11.0	-10.2	-1.1
% of GDP	**0.2%**	**-13.8%**	**-2.1%**	**-2.0%**	**-0.2%**
Add: Capitalisation of Significant Infrastructure				0.6	2.4
Overall Fiscal Position	0.8	-64.9	-11.0	-9.6	1.3
% of GDP	**0.2%**	**-13.8%**	**-2.1%**	**-1.8%**	**0.2%**

* includes Corporate Tax, Personal Income Tax, Witholding Tax and Statutory Board Contribution
^ Predominantly Property Tax
** includes Other Tax, Fee & Charges and Other Receipts
*** Net Investment Returns Contribution