Respond strategically, not tactically

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Singapore is just 10 years away from its second centennial. In these nearly 200 years, it has faced economic adversity and emerged bruised but standing.

The first one was the Great Depression of the early 1930s. The Malayan economy, of which Singapore was then a part, was the world's leading natural rubber producer. Rubber prices collapsed. British rubber plantation owners found themselves stuck with excess labour.

The colonial government had established an immigration and emigration fund contributed by employers out of the wages of their tappers. When the depression struck, the fund was used to meet the cost of repatriating tappers back to India. Our current foreign work permit scheme likewise gives us the same flexibility in a business downturn.

The next challenge came when the prospect of a common market vanished with separation from Malaysia. Against all traditional economic logic, we removed all import tariffs, and freed up exchange controls. There was no way that we could construct a domestic market out of our minuscule size.

The wager paid off. By offering an honest administration and good governance, we were able to attract multinational manufacturing companies and international banks to establish their regional headquarters here. By the mid 1970s, there was full employment. As educational standards rose, skill intensive industries were attracted here.

Then, in 1985, after 20 years of success, a recession struck but it was one of our own making. The high wage policy introduced in the late 1970s to curb job hopping was way overdone. High wage costs and an overvalued currency snipped away at our international competitiveness.

The Government decided to reduce the employers' Central Provident Fund contribution rate from 25 per cent of basic wages to 10 per cent. That cut in CPF contributions was effectively a 15 per cent reduction in the wage bill for an employer.

Introduced in 1955 by the colonial administration as savings for old age, the CPF scheme initially set contributions at modest levels of only 3 per cent from both employer and employee. As our per capita GDP rose, the Government increased the CPF contribution rates to enable Singaporeans to buy their own low-cost HDB flats. Even today, public housing is financed largely through CPF savings.

In 1985, it was clear that a 25 per cent employer's rate of contribution was excessive. It had caused us to be overpriced in world markets. The 15 per cent cut in the employer's contribution rate that was instituted proved enough to restore our competitiveness. Within 18 months, the economy had recovered.

The lesson that can be drawn from the 1985 recession is that any response to an economic crisis should be a strategic one. By reducing the employers' CPF contribution rate to merely 10 per cent across the board, we ignited the dynamics to restructure and transform the whole economy. The move was not targeted at saving individual jobs or particular industries.

There were retrenchments, but the jobs that were lost were no longer internationally competitive with or without the CPF cuts. New businesses moved into Singapore. Today, our industrial structure is more competitive than it was in 1985. There is more knowledge content in our industries and services. They add more value so higher wages can be sustained.

By comparison, the present Jobs Credit scheme in the recently announced 'resilience package' is not a strategic response but merely a tactical one to prevent massive unemployment. By stipulating that an employer can draw on the jobs credit only if it keeps existing employees at their jobs, we risk freezing our industrial and business structures in a time warp.

It is much better for employer CPF contribution rate to be reduced by 9 per cent, the very quantum specified in the jobs credit scheme. This would give employers more flexibility to restructure and transform their businesses.

Firms that cannot do so would naturally fall by the wayside. But this is better than giving uncompetitive enterprises a short reprieve through jobs credit.

Such a CPF cut should also apply to the public service and statutory boards so as to level the playing field for all employers. It is not healthy when young graduates rush to join the public rather than the private sector, unlike the recent past.

The impact of tactical policies is transitory. Using our reserves for a rainy day is another tactical, not strategic, response to the crisis. These reserves play a pivotal role in backing the currency. Being a small and vulnerable economy, the convertibility of the Singapore dollar is our lifeline. Thus the reserves should only be used in extremis such as wartime.

Let us adopt strategic policies, not tactical ones. Though they may be harder to execute, the returns will be better over the long run.

This is a condensed and edited version of a speech given by Mr Ngiam Tong Dow to visiting African policymakers on Feb 16, 2009 at the ***S. Rajaratnam School of International Studies*** *of the Nanyang Technological University where he is Adjunct Professor. He served as Permanent Secretary in several ministries. He is also an SPH director.*