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SINGAPORE: HIGHLIGHTS OF FY 2002/03 BUDGET

No surprises from the latest budget announcement, with the govt more or less adopted most of the ERC recommendations. Key focus was the expected corporate and income tax cuts to 20% over the next three years and hikes in GST to 5% from 3%. What came as a surprise, however, is the magnitude of the tax cut. The republic's corporate tax rate was cut by 2.5% points to 22% for this FY, while income tax rate was shaved off by 4% points to 22%. In line with the expected economic recovery (the govt took the opportunity to revise up its GDP growth forecast to 2-4% from 1-3% previously), the expected GST hike will be implemented on 01 Jan 2003. Similar to 1994 (when the GST was first implemented), the govt has promised a slew of measures for the next 5 years to alleviate its impact on poorer Singaporeans.

In all, a budget to help re-make Singapore into an even more conducive place for foreign companies and talents, so as to alleviate the current unemployment problem. Unemployment was already up at 15-yr high of 4.5% s/adj in Q1-02, and is expected to hit 5.5-6.0% later this year, as the current structural unemployment becomes more visible.

Impact on GDP growth

The question is whether the tax changes will be attractive enough to keep foreign companies and talents within the republic's border. Well, it is probably hard to quantify. First, tax structure is only one of the factors in foreign companies' decision making process. For now, all eyes will be on other ERC's recommendations (particularly the CPF system). This will be out over the next two months. Second, amid the intense global competition, 'cost' in Singapore is definitely an issue. Certainly, close to 40% of the manufacturing companies in Singapore gear towards the cost sensitive electronics sector has only aggravated matters. In this area, Singapore is definitely playing a losing game as compared to other emerging economies such as China and other SE Asian economies. However, for now, the first class infrastructure and telecommunication network should remain as attractions, and perhaps provide a longer runway for Singapore. But, China and other SE Asian economies are fast catching, which means that Singapore will have to aggressively move up the value-added ladder to stay viable.

But in terms of impact on this year's GDP growth, the firmer than expected Q1-02 GDP growth, plus Singaporeans front loading their purchases of big-ticket items ahead of the 01 Jan 2003 deadline should help prop up GDP growth in the final quarter of this year. Nevertheless, we are maintaining our growth forecast of 3.5% for this year. Although we are quite comfortable about US growth prospects, outlook for the global electronics industry remain uncertain. Latest global semicon figure said nothing more than a bottoming out story.

Impact on STI and SGD:

The former has more or less priced in the budget measures. With trade accounting for 3.5 times of GDP, global demand is likely to have a bigger impact on the STI performance

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in the months ahead. On the latter, we doubt the revised Q1-02 GDP growth figures will result in a change in MAS monetary policy given the lack of inflationary pressure. We maintain that monetary policy will remain in their current mode till next year. Although SGD NEER is already at the strong end of our estimation of the MAS policy band, USD/SGD is expected to remain soft over the next few weeks unless we see a turnaround in the current broad USD weakness. For now, unless USD/JPY and EUR/USD break 126.50 and 0.91, USD/SGD should hold above 1.80.

Following are highlights of recession-hit Singapore's 2002/03 budget delivered by Deputy PM and Fin Min Lee Hsien Loong in parliament on Friday. Complied from various newswires.

ECONOMIC CONDITIONS

- *The external environment has picked up over the past few months.*
- *Growth will be slower and more volatile in future.*

GROWTH PROJECTION RISED UPWARDS

- *In light of the improving global environment, the govt has revised up its growth projection to **2-4% from 1-3% previously**. The govt has also revised up its Q1-02 GDP growth to 7.7% s/adj vs 3.5% previously. This equates to **1.9-2.0%y/y** contraction for Q1-02 vs the flash estimate of **-2.6%y/y.***

GOVT SPENDING

- *Surpluses likely to shrink even without any tax cuts.*
- *Government will keep public-spending below 20% of GDP.*
- *The govt clocked a deficit of $1.4bn in FY 2001/02. Expects budget surplus of $0.9bn in FY 2002/03.*
- *Government will not dip into reserves for fiscal 2001.*

TAXES/REVENUES

- *The government has accepted the recommendations of the ERC committee to remake the Singapore economy.*
- *Corporate and top personal income tax rates to be lowered to **20% by 2004** budget year, barring major changes in the political and economic climate.*
- *Goods and services tax (GST) to be raised to **5% from 3% (effective 01 Jan 2003).** For the year of assessment, corporate tax rate will be cut by **2.5% points to 22%,** while top income tax bracket will be shaved by **4% points to 22%.***
- *The GST increase will raise 0.8% of GDP and make up just half of the revenue to be lost from the planned top tax rate cuts.*
- *Government revenue will dip by S$1.2bn per year (or 0.9%of GDP)*
- *A comprehensive offset package will ensure most households will be no worse off.*
- *The package will "offset completely" at least five years' worth of additional tax payable by most families.*

GOVERNMENT-LINKED COMPANIES (GLCs)

- *Government to keep strategic stakes in aviation and power, but state-linked firms must be able to compete.*
- *Government will not favour GLCs with special privileges or hidden subsidies.*
- *The government hopes to list GLCs that are still wholly owned in the future.*

THE CPF SYSTEM

- *No decision on state pension scheme yet. This, we suspect, will be out over the next two months.*
- *Any changes to CPF savings will be done 'very carefully, after full consultations and without causing disruptions either to CPF members or the property market'.*