

BUDGET STATEMENT 2004
BUILDING A FUTURE OF OPPORTUNITY

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PART I – OUTLOOK AND CHALLENGES

Mr Speaker, Sir

2003 – Ending on a Positive Note

1.1 I beg to move that this Parliament approves the financial policy of the Government for the financial year 1st April 2004 to 31st March 2005.

1.2 In the last six years, the Singapore economy experienced more volatility and uncertainty than it had encountered over the previous 30 years. Beginning with the Asian Financial Crisis in 1997, a series of external shocks buffeted our economy and ended a decade of uninterrupted growth. We were all hoping for a quick turnaround last year, as our economy had bounced back quickly from previous downturns. But SARS and the war in Iraq dashed our hopes. We had a very difficult first half.

1.3 But the economy showed clear signs of turning around towards the end of the year. In the fourth quarter, GDP expanded by 4.9% compared to the previous year. On an annualised quarter-on-quarter basis, GDP grew by 11%, with the manufacturing sector expanding by 17% and the services sector by 11%. This brought growth for the whole year to 1.1%. The recovery was reflected in increased exports, investments, and employment.

1.4 Both manufacturing and services benefited from an increasingly favourable external environment. As the recoveries in the US, Europe and Japan gained momentum, their appetite for imports increased. Our non-oil domestic exports grew by 15% in 2003, driven by pharmaceuticals, chemicals and semiconductors. Strong external demand also caused the wholesale and retail sector to grow by 6.7%.

1.5 Foreign direct investments (FDI) began to return to the region as the fears and uncertainties from SARS and the Iraq war subsided. Last year, Singapore attracted \$7.5 billion of fixed asset investments in the manufacturing sector and \$1.9 billion of annual business spending in the services sector. These investments will generate \$8.6 billion in value-added each year for the economy.

1.6 Employment also improved. More jobs opened up as companies regained the confidence to start hiring again. About 12,000 jobs were created in the second half of 2003, partially making up for the 30,000

jobs lost in the first half. The seasonally adjusted unemployment rate dropped from the peak of 5.5% in September to 4.5% in December 2003.

1.7 Macroeconomic policies helped support the economy. MAS maintained a neutral policy stance for the trade-weighted exchange rate of the Singapore dollar, after re-centering the policy band at a lower level. The Government introduced two off-budget fiscal packages to support the economy, and help households and businesses tide through a difficult period. We had a SARS relief package in May, and another package to accompany the CPF changes in September. These prompt measures helped to maintain confidence, buffer the shocks, and boost economic activity. In the absence of support from monetary and fiscal policies, GDP growth last year might have been flat instead of 1.1%.

2004 – Gathering Momentum

1.8 Our recovery is picking up. There is a palpable optimism among Singaporeans and businesses. The December Straits Times Consumer Confidence Index surged 82 points to 294, bringing it close to its levels in 2000, when the economy was growing strongly. Retail sales in December rose by 21% month-on-month and 10% year-on-year.

1.9 We have revised our growth forecast for this year upwards to 3.5-5.5%. But we have to look beyond the cyclical pickup in our growth rate, and achieve sustained long-term growth by transforming our economy. That will depend on our ability to carry through our economic restructuring, upgrade our industries, and create new and better jobs to replace the old jobs that are being phased out. Our commitment to restructuring is a key reason why analysts and investors are confident about Singapore's long-term prospects, and why MNCs still want to put their projects in Singapore.

1.10 The Economic Review Committee's recommendations, the CPF changes, the cut in direct taxes, and wage reform lay the foundations for a globalised, diversified, and entrepreneurial economy. These fundamental changes reflect our resolve to stay relevant in an increasingly competitive world. Let me review our progress in restructuring, and what more needs to be done.

Growing Manufacturing and Services

1.11 First, we continue to grow the manufacturing and services sectors. We are strengthening our position as a global business hub and one of the most attractive places in Asia for investments and talent.

1.12 Singapore remains competitive as a manufacturing location, especially for high-tech, high value-added activities. In the past year, many MNCs have either committed to expand their existing activities, or to establish regional headquarters in Singapore. For example, Hewlett-Packard recently decided to invest another US\$1 billion in the next five years to expand its operations. ST Microelectronics has announced \$425 million of new investment commitments; Seagate Technologies announced a \$200 million investment in recording media and \$300 million in high-end hard disk drives; and Agilent Technologies has committed to another \$156 million of investments.

1.13 However, overall the manufacturing sector is not likely to generate many more jobs. MNCs are shifting to higher value-added, less labour-intensive activities, and will increase output per worker rather than hire more workers. So to create jobs for Singaporeans, we also need to put strong emphasis on the services sector. We are developing established services such as trading and logistics, info-communications technology, financial services and tourism; while fostering emerging services such as education, healthcare and the creative sector.

1.14 More so than manufacturing, a vibrant services sector depends on people – including foreign professionals, executives, businessmen, technicians, tourists and consumers – being able to travel in and out of Singapore with minimum hassle. In particular, we must facilitate travel for visitors from ASEAN, as well as from China and India.

1.15 Singapore does not require entry visas for visitors from most countries. The Immigration and Checkpoints Authority (ICA) has reviewed our remaining visa requirements. As a result, we lifted visa requirements for visitors from Cambodia, Laos and Vietnam last year. We have also made it easier for businessmen to obtain long-term Multiple Journey Visas (MJVs), valid for up to five years. We will allow reputable Chinese and Indian companies to recommend their own staff for MJVs. Social visitors from the PRC are now granted visas valid for up to five weeks compared to three weeks before, while the period of stay granted is now up to 30 days, double the previous 14 days. Similar facilities are also granted for visitors from India, Myanmar and the Commonwealth of Independent States. Since the beginning of this year, we have proliferated the visa application points for PRC travellers, from 67 branch offices operated by 3 appointed travel agents, to 322 branch offices operated by 43 appointed travel agents across China. ICA is exploring other innovative measures, such as on-line visa applications, to facilitate the entry of bona fide visitors to Singapore.

1.16 The easier visa rules will attract more tourists here. Visitor arrivals have already recovered to pre-SARS levels. This year STB expects 7.6 million visitors, up from 6.1 million last year. STB is stepping up marketing efforts to regional countries such as China, India, and ASEAN. Last year saw the largest foreign direct investment in a visitor attraction in Singapore – the \$200 million “Singapore Flyer”. Sentosa Development Corp has also drawn up a ten-year, \$8 billion plan to revamp and refresh Sentosa. It has been aggressively drawing in projects and has already attracted about \$500 million of new investments, half of them from the private sector.

1.17 We have also done well promoting other service industries. Globally, many MNCs are centralising and outsourcing their corporate functions. To save costs and ensure business continuity, banks are relocating many functions, traditionally performed in New York, London and Tokyo, elsewhere in the world. India is attracting many call centres and business process outsourcing (BPO) operations. Singapore is not a competitive location for call centres, but we are an attractive site for support centres hosting higher-end activities, particularly for financial institutions. Over the past year ten banks, including Credit Suisse First Boston and Barclays Capital, have centralised their regional and even global processing operations here.

1.18 Outside the financial sector, we attracted over 30 shared services and BPO projects last year. For example, Europe’s largest software company SAP chose Singapore as the launch market for its Shared Services Centre in the Asia Pacific. Polaris and IBM have set up disaster recovery operations here. Toyota Tsusho, ExxonMobil and DFS are all using Singapore as a centre for shared services and business continuity activities.

1.19 In healthcare, EDB has launched the *Singapore Medicine* initiative to develop Singapore into a leading destination for healthcare services. *Singapore Medicine* will bring together the efforts of many public sector agencies, including MOH and STB. One pre-condition to make Singapore a regional medical hub is to have enough doctors, particularly specialists, who can practise in Singapore. To ensure this, MOH has expanded the list of recognised foreign universities and medical schools from 24 to 71. To alleviate the shortage of nurses, MOH will continue to recruit nurses from diverse sources, and streamline the recognition of nursing qualifications from the Philippines, Myanmar, China and Indonesia. In addition, MOH will relax many current restrictions on advertising by healthcare institutions so that they can promote themselves

in the region. A new set of Publicity Rules will be gazetted within the next few months.

Labour Market Reforms

1.20 The second strategy we are pursuing is to reform our labour market so that companies and workers can respond to fast-changing business conditions. The CPF changes and the ongoing push for wage reform are important parts of this effort. They will help to preserve existing jobs and create new ones for Singaporeans.

CPF Changes

1.21 We made major changes to our CPF scheme last year to maintain our cost competitiveness. Employer contribution rates were reduced, and the CPF salary ceiling will be brought down in steps. This has lightened the burden on employers and made Singapore workers more competitive. At the same time we are raising the CPF Minimum Sum and tightening withdrawal rules at age 55, so that Singaporeans will be better prepared for their retirement needs.

Wage Flexibility

1.22 The CPF changes are long term structural adjustments, not tactical responses to transient conditions. They will strengthen our competitiveness, but we still cannot be sure that our wage levels will never become too high again one day. Should this happen, we should not bank on another large cut in CPF rates to restore our competitiveness, as we did in 1985 and 1998. The CPF is a blunt tool for cost reduction. And now that we have reduced the rate to 33%, there is less room for further reduction. This makes it more important to have flexible wage structures, so that companies can respond quickly to changes in the business environment. This will help companies stay viable and preserve jobs in a severe downturn, while giving them the confidence to reward workers and increase employment in good times.

1.23 I am happy that the tripartite Taskforce on Wage Restructuring has given strong backing to wage reform. Its report explains clearly how companies can implement wage restructuring for greater flexibility and competitiveness. Achieving wage flexibility will require strong commitment from employers, unions and workers. Employers must put in place schemes that link remuneration to individual and company performances. Unions must take a broad long-term view of workers' interests, and persuade them of the benefits of these changes. Finally, workers must recognise that in a more volatile and competitive

environment, flexible wage structures offer the best chance of job security. We must make a concerted effort to achieve our wage reform targets.

Training and Upgrading

1.24 Even as the economy recovers, we must not let up on retraining and upgrading our workers. This will enable our workers to seize new opportunities and adapt to the changing needs of the economy.

1.25 The Singapore Workforce Development Agency (WDA) will strive to upgrade the skills of workers, especially those with secondary education or less, so that they can stay employable and take on new, higher-skilled jobs. WDA will launch new training programmes, and make it easier for workers to enrol in them. There will also be programmes for professionals, managers and executives, so that they can support the upgrading of their industries.

1.26 These programmes are partly financed by the Skills Development Fund (SDF), which employers contribute to through the Skills Development Levy (SDL). The 1% levy applies to all workers with a gross monthly salary of \$1,500 or less. The current levy rate and salary ceiling are not enough for the SDF to cover its annual commitments. Had the Government not injected \$500 million into the SDF in 2001, the fund might have been exhausted by now.

1.27 Over the next five years, WDA estimates that the SDF's annual commitment will rise from \$120 million for 600,000 training places in FY03 to \$176 million for 766,000 places in FY08. MOM will therefore raise the SDL salary ceiling from \$1,500 to \$1,800 with effect from 1 July 2004. The levy rate will stay at 1%. This will increase SDF's income by \$22 million per year.

Foreign Workers

1.28 When the Asian Crisis struck, the Government reduced foreign worker levy rates temporarily, to save costs for employers. As the economy recovers, the Government needs to progressively adjust levy rates to reflect the prevailing market conditions.

1.29 The levy for skilled Work Permit holders is currently \$30, reduced from \$100 previously. As part of the changes to the foreign worker scheme for the construction sector, MOM increased the construction skilled worker levy to \$50 with effect from 1 July 2004. In line with this, MOM will also raise the skilled worker levy rate to \$50 in all other

sectors, with effect from 1 July 2004. The levy rates for unskilled workers will remain unchanged.

1.30 For our economy to grow, companies must be able to recruit skilled workers. The higher value and skill-based industries we are attracting all depend heavily on skilled workers, technicians and professionals. A particular concern is manpower at the diploma and post-secondary level. If we lack these middle-tier skilled workers – whether local or foreign – we will choke off the growth of these industries or drive them elsewhere. The shortfalls are already evident in healthcare where there is an acute shortage of nurses, in the IT industry where we lack computer programmers and IT technicians, and in aerospace and pharmaceuticals.

1.31 MOM will modify the current work pass system to meet this demand for middle-level skilled manpower. We will introduce a new category of work passes, called ‘S’ passes, to replace the current ‘Q2’ passes.

1.32 The main criteria for an ‘S’ pass will be a minimum salary of \$1,800 and an acceptable tertiary qualification. MOM will supplement these two criteria with a system of points, to take into account experience, skills and job type when assessing eligibility. The ‘S’ pass will be subject to a quota, to begin with 5%, as well as a levy, initially set at \$50. The scheme will be implemented from 1 July 2004.

Encouraging Entrepreneurship

1.33 A third major strategy is to boost entrepreneurship. This process takes time, because we are not just changing Government rules, but seeking to shift mindsets. The Government is doing its utmost to foster a conducive environment for entrepreneurship. The Action Community for Entrepreneurship (ACE), chaired by Minister of State Mr Raymond Lim, is nurturing entrepreneurship, pursuing entrepreneurship promotion programmes, and acting as the interface between the private sector and Government.

1.34 A key hurdle facing start-ups is financing. The Government is helping start-ups gain access to financing. EDB’s Start-up Enterprise Development Scheme (SEEDS) helps early-stage start-ups with equity financing. Every dollar raised by a start-up from third-party investors will be matched by EDB up to a maximum of \$300,000. In two years SEEDS has raised nearly \$59 million – \$27.3 million from Government and \$31.6 million from the private sector – to support 103 innovative

start-ups. We also recently established Deal Flow Connection, an online portal that helps link up entrepreneurs with financial institutions, venture capitalists and angel investors.

1.35 The Government is also helping our entrepreneurs to venture beyond our shores. We have negotiated many FTAs, including those with key economic partners like the US and Japan, to improve access to these markets. Our businessmen can now tender for projects contracted out by the governments of our FTA partners, on an equal footing with their local companies. IE Singapore actively promotes the development of Singapore's external wing. It helps local enterprises take advantage of government-to-government agreements such as air services agreements, investment guarantee agreements, and avoidance of double taxation agreements. IE Singapore also recently launched the iPartners Programme to encourage companies to band together when venturing overseas. Already, this programme has helped three consortia of Singapore companies to venture into East Asia, Africa and the Middle East.

1.36 To bring in entrepreneurial talent, MOM launched the EntrePass Scheme. Entrepreneurs can set up operations in Singapore on the basis of their business plans, rather than academic qualifications or salary.

1.37 The Government is also reviewing its rules and licensing requirements to ensure that bureaucracy does not stifle enterprise in Singapore. To date, the Pro-Enterprise Panel has reviewed 1080 suggestions, of which it has accepted 57%. The Rules Review Panel is also making headway. In the past year, the Panel reviewed 2913 rules, 23% of the total. It removed 373 rules, updated 772, and re-affirmed the remaining 1818. By 2005, public agencies will have reviewed all their existing rules, to remove outdated ones and streamline the rest. It does not mean that the job is then done. Thereafter, it will be time to start reviewing all the rules again. Our plan is to review all rules regularly, on a rolling five-year cycle.

1.38 However, the Government can only do so much to create a Best for Business environment. Ultimately, entrepreneurs need to take their own risks and develop their own ideas, in order to create and seize new opportunities in overseas markets. Entrepreneurship is, ultimately, a challenge for our whole society.

Enhancing Competition

1.39 A fourth major strategy is to promote competition and free markets in all sectors of the economy. Competition spurs firms to be more

efficient and innovative, and more responsive to customer needs. It prepares our firms to be internationally competitive and to hold their own in the region. Consumers enjoy wider choice and better products and services, and often lower prices. The economy as a whole gains from higher productivity and more efficient allocation of resources, and in the longer term also from more innovation and job creation.

1.40 This is why our basic economic stance is pro-competition. Right from the start, Singapore was a free port. For trade in goods, when we first began industrialising in the 1960s, we did impose entry barriers and import tariffs to protect domestic industries, but we soon abandoned this infant industry argument and shifted to an open competitive regime.

1.41 For services, we pursued the same policy of open competition in wholesale and retail trade, IT and business services. In other industries like telecommunications and power generation, we used to operate vertically integrated state-owned monopolies, like many other countries. But in the last 10 years we have moved a long way from that model. We privatised statutory boards, deregulated the industries and opened them up to competition. In the financial sector too, we have liberalised and freed up, causing a major transformation of the industry.

1.42 However, fostering competition is not always the same as taking a passive, hands-off approach. Sometimes we need to intervene to structure the industry to allow competition. Otherwise instead of healthy competition, we may end up with one or two players wielding monopoly power to the detriment of consumers.

1.43 Take the telecommunications industry as an example, which is now fully liberalised. Competition in that market has increased significantly, especially in mobile and wholesale international call services. But IDA still needs to act as a referee, because several segments of the telecommunications market are not or cannot be effectively competitive, as in the case of “last mile” access infrastructure. IDA’s role is to guard against abuses of market power, and to set rules which help smaller players connect to infrastructure provided by larger players. IDA’s regulations seek to keep the market contestable, and ensure that competition produces benefits for consumers over the long-run.

1.44 Or take the power industry. Singapore Power was an integrated monopoly operator, generating, distributing and selling electricity and gas to every home and factory. To introduce competition, we first had to split up Singapore Power into several different companies, create the right regulatory framework and set up the Energy Market Authority (EMA) to

oversee the industry. We made each power plant a separate generating company (genco), competing against other plants. We created a sophisticated mechanism for the gencos to bid to sell electricity into the grid, called the pooling and settlement system. As for the power grid, which is a natural monopoly, we made it a separate, tightly regulated company. Only then were we ready to have different suppliers compete to sell electricity to consumers, starting with the large consumers. The process has taken eight years, and is still not quite complete.

1.45 Our small domestic market is an important practical constraint to promoting competition in industries where scale is important. So we have only three local banks, two media groups and two public transport operators. Our market simply cannot support more players. We cannot manage such industries in the same way as we would the retail trade with thousands of players. We have to accept that in these circumstances limited competition or even sometimes a single operator is the best arrangement, and find other ways to prevent the companies from exploiting their position or becoming inefficient and uncompetitive.

1.46 The container port business is such an industry. In this case, the relevant market extends beyond Singapore. Today transshipment is an international business. Within our neighbourhood alone, Tanjong Pelapas, Port Klang and Laem Chabang, are all vying to replace PSA as the hub port for Southeast Asia. Competition in the port industry is not really domestic but takes place on a regional or even global stage.

1.47 The Government is determined to consolidate Singapore's status as a hub port. The Maritime and Port Authority (MPA) has approved PSA's application for land to build five new berths at Pasir Panjang Terminal to support its growth in container traffic. This will allow PSA to strengthen its competitive position in the international arena.

1.48 Jurong Port will continue to operate at its existing facilities in Jurong, where it can handle one million containers a year. Given the intense regional competition, Jurong Port will not for now expand its container capacity by building additional berths at Pasir Panjang, but will review this decision when conditions change.

1.49 However, MPA has not granted PSA a monopoly on container operations in Singapore, nor will it do so. The port industry is dynamic. If and when industry conditions make greater local competition necessary, and new operators judge it viable to enter the business, the Government will not stand in the way.

1.50 This year, MTI will be proposing to Parliament a competition law covering most sectors of the economy. To complement the liberalisation and deregulation of our economy, we need a means to stop companies from engaging in anti-competitive behaviour and undoing the benefits of efficient and innovative markets. The competition law will adopt a pragmatic approach. It will take into account differences in the various sectors, in terms of their industry structure and stage of market development. It will not burden businesses with unnecessary regulatory costs. Such an important initiative will need inputs from businesses and the public. A draft version of the law will be released soon for public consultation.

Building on Our Fundamentals

1.51 We face formidable challenges in restructuring and upgrading our economy, and coping with shocks and uncertainties in our external environment. But our capacity to overcome these challenges is much greater than ever before. Our financial resources are larger. Our infrastructure and physical assets are better developed. Over the years, our workforce has become better educated and more highly skilled.

1.52 As we develop new capabilities and strategies, we must continue to build on and make the most of our strengths. Three fundamentals have been the pillars of Singapore's success and will allow us to sustain our growth and prosperity. These pillars are:

- i. Effective Government. A Government that delivers sound public finances, responsive fiscal policies that help to stabilise the economy, and good financial practices that ensure value for money in public spending.
- ii. A Strong Society. A resilient and cohesive population, and a strong social compact between Government and the people that helps see us through good and bad times together.
- iii. A Land of Opportunity. A place where every individual has the chance to be the best he can be, a home where people want to raise their families, an economy which attracts talent and investments, and a centre for businesses to pursue new and exciting opportunities.

1.53 The Government's financial and budget policies will bolster these three fundamentals.

PART II – EFFECTIVE GOVERNMENT

Importance of Sound Public Finance

2.1 One of the most important contributions any Government can make to economic growth and resilience is to put public finances on a sound footing. A balanced budget and a trim and efficient public sector will make for stable macroeconomic conditions and a pro-business climate. Only then can the private sector grow and create wealth for the people.

2.2 Fiscal prudence has been a hallmark of Singapore’s economic management. Some people accuse us of being too prudent, but we must continue to maintain fiscal prudence, despite stronger spending pressures and tighter budgets. We will spend more in a downturn if we need to, even if it means going into temporary deficit, as we have done in the past two years. But we must never fall into the trap of structural budget deficits, with a permanent shortfall of revenue. On average, over the course of the business cycle, we aim to accumulate a modest surplus, putting aside something in good years so that we have some savings to draw upon in bad years.

Living Within Our Means

2.3 In order to live within our means, we must keep Government expenses in check. This means confining the Government to essential functions and preventing the bureaucracy from bloating up. This will also free up talent and resources for the private sector, and create space for private initiative and enterprise.

2.4 The Ministry of Finance (MOF) controls the budgets of ministries by capping their spending as a percentage of GDP. To provide some stability in spending from year to year, the budgets are pegged to a six-year average of GDP growth. And to provide flexibility, MOF allows ministries to take advances from future years’ budgets, and accumulate and carry forward unused funds to subsequent years. This way, ministries can plan on a multi-year basis instead of being limited by yearly expenditure limits.

2.5 MOF will also extract ‘productivity dividends’ from the operating budgets of all ministries, with effect from FY04. Instead of allowing ministry budgets to grow at the same rate as GDP, MOF will reduce the ministry budgets by a percentage equal to the productivity growth rate, and collect the sums into a central pool. The aim is to encourage

ministries to improve their productivity by at least as much as the private sector, and to free up resources to fund new priority projects. For example, MOE will receive additional funds for preschool education and special needs education, while MITA will receive funds to develop the creative industries.

Revised FY 2003 Budget Estimates

2.6 I will now review the FY03 Budget. I refer Members to the second column of the budget statistics table on the screens and in your Handout.

Table 1: Budget Statistics for FY 2003 and FY 2004
(figures rounded off in \$ billions)

	Estimated FY 2003	Revised FY 2003	Estimated FY 2004
	\$'b	\$'b	\$'b
OPERATING REVENUE	26.6	25.6	28.3
Tax Revenue	22.0	21.6	24.6
Fees & Charges	4.5	3.8	3.6
Others	0.1	0.2	0.1
Less:			
TOTAL EXPENDITURE	29.9	28.8	30.4
Operating Expenditure	20.4	20.0	20.8
Development Expenditure	9.5	8.8	9.6
SURPLUS/(DEFICIT)	(3.3)	(3.2)	(2.1)
Less:			
SPECIAL TRANSFERS	0.6	0.6	0.9
Economic Restructuring Shares	0.6	0.6	0.9
Add:			
NET INVESTMENT INCOME CONTRIBUTION	3.0	2.0	2.3
<i>BUDGET SURPLUS/(DEFICIT)</i>	<i>(0.9)</i>	<i>(1.8)</i>	<i>(0.7)</i>

2.7 When I presented the budget last year, I estimated operating revenue at \$26.6 billion and total expenditure at \$29.9 billion. With Special Transfers of \$600 million to provide for the ERS and Net Investment Income (NII) Contribution of \$3 billion, the projected deficit was \$900 million.

2.8 As the third column of the table shows, the revised operating revenue and total expenditure both turned out about \$1 billion less than budgeted. There was also a \$1 billion shortfall in NII Contribution. The revised Budget Deficit is \$1.8 billion or 1.1% of GDP.

2.9 The revised FY03 expenditure is \$1.1 billion or 0.7% of GDP lower than the budgeted amount, mainly reflecting lower expenditure on development projects across-the-board. This was due to lower contract costs and construction delays, as well as cancellation or deferment of projects. The more significant items of under or deferred expenditure are MND's SERS programme (\$59 million), the Singapore Management University campus (about \$60 million) and the new Supreme Court building (\$58 million). While about \$600 million worth of construction projects were brought forward in the September 2003 off-budget package, most will start only in FY04 and have thus not led to an increase in spending in FY03.

2.10 The revised FY03 budget estimates also include supplementary estimates of about \$125 million for six Heads of Expenditure, the bulk of which goes to MTI (\$61 million) for the Utilities Save scheme, which was extended in the September package.

Projected FY 2004 Fiscal Position

2.11 The Government faces a very tight fiscal position in FY04. Operating revenues should rise, but so will spending needs. Despite the improved economy, we still project a budget deficit.

2.12 To reduce the revenue shortfall, I am permanently cutting by 2% the budget caps of all ministries except MINDEF, from this financial year. This will save about \$450 million a year. More importantly, it will instil financial discipline by encouraging ministries to reprioritise their projects and cut non-essential expenditures.

2.13 I am treating MINDEF differently from the other ministries because defence provides the peace and security that Singapore needs for economic progress. Government has therefore for many years been prepared to spend up to 6% of GDP on defence. In practice, in recent

years defence spending has been 4.5% to 5% of GDP. I will maintain this policy.

2.14 The 2% expenditure cut will trim the projected FY04 budget deficit to \$700 million, smaller than the \$1.8 billion deficit in FY03. This is not inappropriate, as the economic recovery is still in its early stages. But I intend to balance the budget by FY05, assuming the recovery continues on track.

2.15 It would therefore be prudent for all ministries to assume that their budgets will continue to be tight, and that they will need to find more economies and do more with less. Barring exceptional conditions, next year (FY05) I intend to apply a further across-the-board cut of 2% on average in the budget cap of each ministry, except MINDEF. I am confident that ministries will make full use of this early notice to adjust their plans and work within the resources available.

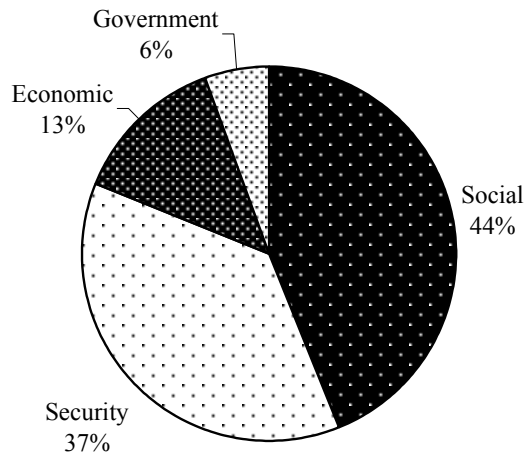
2.16 Let me now present the FY04 Budget, which is summarised in the last column of the table.

2.17 Projected operating revenue is \$28.3 billion or 16.6% of GDP. Receipts from GST are estimated to increase by \$700 million as a result of the increase in the GST rate from 4% to 5%. Collection from property taxes is also projected to increase by \$400 million because the concession period for rebates ended in December 2003, while statutory boards' contributions in lieu of tax are projected to increase by \$776 million.

2.18 The total supported expenditure is \$30.4 billion or 17.9% of GDP. This is an increase of \$1.6 billion or 5.6% from the FY03 revised expenditure. Larger budgets for MINDEF and MOT account for two-thirds of this increase. MINDEF has to incur additional expenditure for new functions that need to be undertaken due to the current security situation. MOT requires additional funds to finance the construction of the Circle Line and the Kallang-Paya Lebar Expressway.

2.19 The sectoral distribution of the budget remains largely unchanged, with the largest share of the budget still going to Social Development (44.0%), followed by Security and External Relations (37.0%), Economic Development (13.4%) and Government Administration (5.6%).

Chart 1: Sectoral Shares of FY 2004 Budget



2.20 After Special Transfers of \$900 million, mainly for the third tranche of ERS, and NII Contribution of \$2.3 billion, we expect a Budget Deficit of \$700 million or 0.45% of GDP.

Ensuring Value for Money in Public Spending

2.21 It is not enough that we restrain our overall expenditures to live within our means. We must also extract maximum value for money in what we spend. We do this through three initiatives: Best Sourcing, the Cut Waste Panel, and Economy Drive.

Best Sourcing

2.22 Last year, I announced that MOF would introduce Best Sourcing for new services. Best Sourcing requires public sector agencies to undertake “market-testing” so as to compare the cost of providing their services in-house against the cost of having private sector vendors provide the services. If the private sector vendor can deliver the services more economically, it will be engaged to do so. The public sector agency will then discontinue the function, and either redeploy or release the affected staff.

2.23 The services that are being market-tested include facilities management, IT services, business investigation, enforcement, and procurement functions. Agencies which have started Best Sourcing include MOH, URA and HDB. The functions that they have “best sourced” and subsequently contracted out in FY03 resulted in \$17 million worth of contracts for the private sector. The annual cost savings from

outsourcing these functions are estimated to be \$1.8 million per year. The numbers are still small, but it is an encouraging start.

2.24 In FY04, we will extend the Best Sourcing programme to non-core functions. An overall target of 5% of the value of non-core functions will be market-tested this year by ministries, Organs of State and statutory boards. Public sector agencies are understandably cautious, but MOF will encourage them to be bolder and move faster, so as to benefit earlier from Best Sourcing, without affecting the smooth delivery of services to the public.

Cut Waste Panel

2.25 The Cut Waste Panel was established last year to seek feedback from the public on how the public sector can reduce wasteful practices, remove frills and reap savings in the delivery of public services. The response has been overwhelming. So far we have received more than 2,200 suggestions. I am not sure how many are from the MPs. The Panel, chaired by the Head of Civil Service, agreed with almost 85% of the suggestions and feedback. Many suggestions had already been implemented earlier though the public may not have been aware of them. But we also received valuable new suggestions. For example, one writer pointed out that even after late payments for foreign worker levy had been cleared, the Work Permit Department was still sending reminders via registered mail, which was a waste of money. The Department has responded to this suggestion by developing a more efficient tracking method to ensure that once a late payment is settled, reminders are no longer sent out. This has saved \$187,000 a year. The Cut Waste Panel is an on-going effort and we look forward to more suggestions from the public.

Economy Drive

2.26 The Cut Waste exercise and Best Sourcing programme are but parts of a wider Economy Drive for the whole public sector, launched in May last year.

2.27 Public officers at all levels have contributed ideas. The aim is not to cut expenditure arbitrarily but to inculcate a stronger 'value for money' mindset in the public sector. The Economy Drive is critical in this new era of fiscal constraints. The only way to meet future challenges and afford new programmes is to get more out of every dollar we spend.

2.28 The Economy Drive has produced some encouraging results. For FY03 up till December 03, it had achieved savings of about \$475 million. Let me give you some examples.

2.29 MOE saved about \$30 million in FY03 by revising the norms and standards (such as space requirements and design features) for school buildings.

2.30 MINDEF saved about \$24 million in FY03 by revamping the training system for NSmen to achieve a reduction in In-Camp Training days without compromising the operational readiness of the SAF.

2.31 MOF and its statutory boards have saved about \$19 million by re-configuring IT infrastructures, freezing headcount, and restraining rise in wage costs.

2.32 The Economy Drive will not compromise the effectiveness of public service. Agencies will continue to deliver quality public services. However, excessively high standards inevitably lead to unnecessary costs. Every dollar saved is a dollar that can be released to meet new and pressing demands. Hence, we will review public programmes and expenditure more critically than before, and scale back or remove those which are less useful or not cost-effective.

Excellence in Service Delivery

2.33 A cost efficient way of delivering many public services is through electronic means, or e-Government. The \$1.3 billion 2nd E-Government Action Plan (EGAP-II) from 2003 to 2005 will build on the success of the first plan. Practically all 1,600 public services that can be delivered electronically have become e-services. EGAP-II will provide the public even better and faster online public services by integrating different agencies' processes. For example, a common bill payment website will be implemented, where the public can pay both Government and private sector bills online.

2.34 For those who have difficulty using online services, there is an e-Citizen Helper Service available in 22 e-Clubs found at community centres, community clubs and void decks. The Government will extend this Helper Service to ensure access for all Singaporeans. Other e-Citizen outlets already in operation include 8 NTUC Income premises and 2 Office1 Cybermarts.

2.35 For businesses, the Government has also developed an online portal – Business eTown (www.business.gov.sg). This is a

comprehensive repository of G2B content and e-services that will be especially helpful to SMEs that lack administrative resources. The portal will provide links to Government services such as licence applications, and information on tax incentives, assistance schemes, and business opportunities with the Government and abroad.

2.36 The Government will also make greater use of e-Government as a channel for public consultation. We have established an online consultation portal where public agencies post consultation papers to seek feedback and ideas. From there the public can see, at a glance, all the on-going discussions.

Divesting Non-core and Non-strategic Activities

2.37 Keeping Government lean and trim also means divesting activities that are no longer core or strategic to the public sector. I announced last year that the ministries would conduct a review of their companies every three years, so as to determine which should be retained, and which can be divested. The ministries have completed the first review. A number of statutory board companies, for example HDBay and Cleantech Services, have been identified as no longer relevant to the ministries and have been divested. More will be divested within the next few years.

2.38 The Temasek Charter spells out the *raison d'être* of Temasek Holdings and its companies. The role of Temasek is to grow companies with international or regional potential, provide stewardship for companies that the Government needs to own for strategic reasons, and divest those which have no international growth potential or are no longer strategic.

2.39 In 2003, Temasek fully or partially divested its stakes in 12 companies. SingTel has divested 69% of its wholly-owned subsidiary, SingPost, through an Initial Public Offering (IPO). Other divestments include the sale of CPG Corp (formerly PWD Corp) in April 2003, and Temasek's remaining 10% stake in 98 Holdings in October 2003. In January this year, Temasek completed a \$2.1 billion placement of SingTel related securities, thus reducing its shareholding in SingTel by up to 5%. Annex A lists the divestments by Temasek over the last year.

2.40 Temasek will continue to consolidate and rationalise its stable of companies. It will divest those that are no longer relevant to its mission, at the right time, at a fair price, without unsettling the market, and after installing a competent team to manage the companies after divestment.

Enabling Initiative and Enterprise

2.41 As much as the Government strives to be lean and effective, we must recognise that the state by itself cannot create wealth or jobs. Neither can it force citizens to adopt an enterprising mindset. But the Government can and will create the environment for private enterprise to flourish, for investments to take place, and for individuals to realise their dreams. This in turn will create jobs and wealth.

2.42 Ultimately, our success will depend on the flexibility, nimbleness and fortitude of all Singaporeans. The Government will put in place policies and measures to equip and prepare us for the challenges that will come our way. But each of us must seize the initiative to pursue and realise our aspirations.

2.43 The last few years have shown how uncertain and volatile a world we live in, but also how much difference resolute leadership and cohesive response makes. Despite the severe storm, we avoided any social or political unrest. Instead we pulled together, restructured our economy and prepared for the next wave of growth.

2.44 The next crisis, and there will bound to be one, will be very different from the last. But I am confident that when it happens, we will again muster the resolve, cohesion and the ingenuity to overcome it.

PART III – STRONG SOCIETY

Building a Strong Society

3.1 After effective government, the next important fundamental for Singapore’s survival and success is a strong society. Stable families, social cohesion, racial and religious harmony, secure homes and streets – these make Singapore a strong society and an attractive place in which to live, work, and play.

3.2 A strong society is marked by a high degree of self-reliance, resilience and social responsibility. The migrants from China, India, and the Malay archipelago who built modern Singapore relied on themselves, their families, and their communities to make a living against great odds. These values of self-reliance and social responsibility will become even more relevant in future. Local communities and the people sector must launch more self-help initiatives, and take on a larger role in society.

3.3 Government will provide a safety net for those who cannot help themselves and cannot find help elsewhere. We walk a fine line here. If we offer too much protection to citizens, it weakens their resilience and saps their spirit to survive on their own. Our social safety nets must therefore be carefully targeted, and must not undermine our will to work and to improve ourselves. Subsidies should focus on those who need them most, and in areas which yield the most public good. Means testing will therefore become an important feature in providing public services and social assistance.

3.4 Let me elaborate on our social policies in four areas:

- Achieving excellence in higher education;
- Keeping healthcare affordable;
- Building the next generation; and
- Ensuring adequate finances for retirement.

Achieving Excellence in Higher Education

3.5 Our education system has enabled a growing number of our citizens to benefit from higher education. 35% of our working adult

population now have either a university degree or a polytechnic diploma, triple the 12% just 10 years ago. Today, 60% of each cohort graduate from a local polytechnic or university. As our schools improve, more students will qualify for university admission. The proportion of each cohort entering local universities will increase from 21% today to 25% by 2010.

3.6 However, good university education is not cheap. One-quarter (24%) of our education budget goes to the university sector. More students entering university, more good professors, and more overseas attachments for students can only mean more spending on university education. The Government's total spending (operating and development expenditure) on universities has already grown from \$1.11 billion in 1998 to \$1.56 billion in 2002, a 41% increase in five years, mainly because of larger student enrolments. If this trend continues, we will be forced to squeeze resources from primary and secondary education in order to fund university education.

3.7 This is not desirable. From the economic point of view, universal primary and secondary education benefits society much more than it benefits individuals. Society as a whole is better off when everyone is literate, equipped with basic skills, and able to become a good citizen. He can be a good colleague, good neighbour, good fellow national serviceman. The whole society gains. Hence it is sound public policy to subsidise primary and secondary education heavily. In contrast, the benefit of a university education accrues mostly to the individual. A rigorous and relevant university degree will make the graduate more employable, and enable him to earn much more during his working life. Furthermore, only the top 25% of the cohort will make it to university, unlike schools, polytechnics or institutes of technical education. The argument for funding university education heavily from general taxation is therefore much weaker.

3.8 From the universities' perspective, it is better for them to be less reliant on the Government for funding. The more universities raise their own funds from fees and donations, the more autonomous they will be, the more flexibly they can respond to student needs and market demands, and the better placed they are to achieve academic excellence. This has been the experience all over the world. In the UK and Europe, universities are funded mainly through government grants, and the result has been mediocrity and declining standards. In contrast, US universities have to compete actively for both state and private funding, on the basis of quality. American students pay higher fees, and take student loans to a much larger extent than European students. The US universities have

produced peaks of excellence unmatched in any other country, and higher standards overall. The US is a large country and its multi-tiered model of state and private universities cannot be replicated here. But we should move in the direction of greater competition and self-reliance to allow our universities to achieve excellence.

3.9 It is therefore fair to ask undergraduates to pay for a larger part of their university education themselves. They do not necessarily have to pay while studying, but can do so later when they are working and earning stable incomes. With this approach, no student should miss a university education because he cannot afford it. We will make sure of this through generous scholarships to outstanding undergraduates, bursaries for those from low-income homes, and student loans readily available to all who need them. That we can promise.

3.10 Our current formula is for undergraduates to pay 25% of the operating costs of university education. The Government pays for the remaining 75%, and also bears in full the infrastructure costs of our universities, which is substantial. Going forward, we need to establish a more sustainable and equitable cost-sharing formula between the state and university students.

3.11 There will be no university fee increases this academic year. However, MOE and the universities are reviewing the basis for setting university fees in future, and expect to reach some conclusions this year.

Keeping Healthcare Affordable

3.12 Our publicly funded hospitals provide quality care to all Singaporeans, at an affordable cost. But advances in medical technology, while enhancing healthcare, continue to push up its cost. For example, in 1990, the standard treatment for blocked heart arteries was angioplasty. By 2000, it had progressed to angioplasty with stents. This has lowered the recurrence of blood vessel blockage but has tripled the cost of treatment from \$1,300 to \$3,500.

3.13 Our ageing population will put further pressure on the healthcare system and on our ability to finance good healthcare for all Singaporeans. MOH will do its best to contain medical inflation. This requires cooperation and understanding from all stakeholders in the healthcare system. Providers have to cut out inefficiencies and frills. Patients have to be realistic in their expectations. And all Singaporeans should adopt healthy lifestyles.

3.14 Ultimately, Singaporeans have to be responsible for themselves and not rely on the Government to provide for every need. Our healthcare financing framework, based on the 3Ms – Medisave, MediShield and Medifund – has fostered an ethic of self-reliance, kept healthcare spending down, and served us well.

Medisave for Self-Employed

3.15 Originally the self-employed did not fall within this 3M framework, because they did not contribute to Medisave. But in 1992 the Government amended the CPF Act to require self-employed individuals who earn above a certain salary – currently \$6,000 a year – to make compulsory contributions to their Medisave accounts. We wanted to make sure that the self-employed regularly put aside savings for their health needs and not expose themselves to unnecessary financial risk when they or their families fall ill.

3.16 However, compliance has been patchy. Only 47% of self-employed CPF members have paid their full Medisave contributions. Another 36% have made partial payments, while 17% have not contributed at all, which means that about half of the self-employed are storing up bigger problems for themselves in future by not contributing fully to their Medisave.

3.17 Henceforth, the CPF Board will enforce Medisave contributions more strictly for self-employed Singaporeans, just as it does with other employers and employees, to ensure that self-employed Singaporeans set aside enough for their health needs.

Health Insurance and MediShield

3.18 With medical costs increasing, so will the risk that large healthcare expenses will exhaust one's own savings. Health insurance schemes can help stretch our Medisave dollars through better pooling of risks. We should therefore supplement Medisave with health insurance schemes which are properly designed to avoid the "buffet-lunch abuses" so common in other countries. This will help us to realise portable employer-provided medical benefits. MOH is also examining how we can enhance the coverage of MediShield, to give Singaporeans better protection against large bills from catastrophic illnesses.

Means Testing

3.19 Besides relying more on medical insurance, we also need to target our healthcare subsidies more precisely, to reach those who need them

most. Nationally, one-third of the total healthcare expenditure is financed by the Government. In hospitals, many services are subsidised even more. For example, all patients in Class C wards are subsidised 80% of the cost of their stay.

3.20 Currently, we link the level of subsidies to the class of ward. We do not take into account the patient's ability to pay. A poor patient in a Class C ward enjoys the same 80% subsidy as a high-income patient, even though he needs the subsidy much more.

3.21 If we continue subsidising healthcare this way, one of two things will happen. Either the Government will have to spend a lot more on healthcare – which means raising taxes, or it must lower the quality of healthcare provided to all Singaporeans. Neither is desirable.

3.22 The Feedback Group has proposed pegging the amount of subsidy to the financial status of the patient rather than the class of ward, in other words, means testing. It will be more difficult to implement, as we will have to assess the financial means of each patient. But means testing is ultimately more efficient and equitable as it will enable us to focus subsidies on those who need them, and so make the most of our healthcare budget.

3.23 Means testing is not new. We already practise it in the step-down care sector. In community hospitals, nursing homes and home nursing, patients' incomes are assessed to determine the subsidies they receive. Means testing is also used for primary care services for the elderly who seek treatment in private clinics, through the Primary Care Partnership Scheme. Eligible patients pay the same fees as they would if they had visited the polyclinics. These schemes have been well received and accepted.

3.24 MOH is studying how to extend means testing to general hospitals. MOH will proceed cautiously, so as to gain more experience with means testing and give patients time to adjust. It will need to determine where best to start, because hospital services span a wide range, from inpatient care to day surgery to specialist outpatient care.

3.25 Even with means testing, a high-income patient can opt for B2 or C class treatment, and pay less than for A or B1 class treatment. But when he does so, he will be subsidised less than a poorer patient getting B2 or C class treatment. And I think that is fair.

Medisave and Medifund Top-ups

3.26 Even with means testing and enhanced medical insurance, some older Singaporeans will face difficulties in coping with increased medical expenditure and paying their MediShield and EldersShield premiums. Older Singaporeans were midway through their working lives when the Medisave Scheme started in 1984. As a result, they have lower Medisave balances than younger workers. Furthermore, workers aged 50 to 55 will face deeper CPF employer contribution rate cuts in the next two years.

3.27 I have therefore decided to top up the Medisave accounts of Singaporeans aged 50 and above. The amount ranges from \$50 to \$200, and will vary based on age of the recipient and his existing Medisave balance, as shown on the screens. This will cost the Government \$104 million.

Table 2: Medisave Top-ups to Singaporeans 50 years old and above

Age	Medisave Balance (as at 1 January 2004)		
	< \$5,000	\$5,000 - < \$10,000	≥ \$10,000
50-59	\$150	\$100	\$50
≥ 60	\$200	\$150	\$100

3.28 I will also be injecting an additional \$100 million into Medifund to help needy patients who cannot afford to pay their hospital bills even after subsidies. This injection will bring the total size of Medifund to its targeted size of \$1 billion.

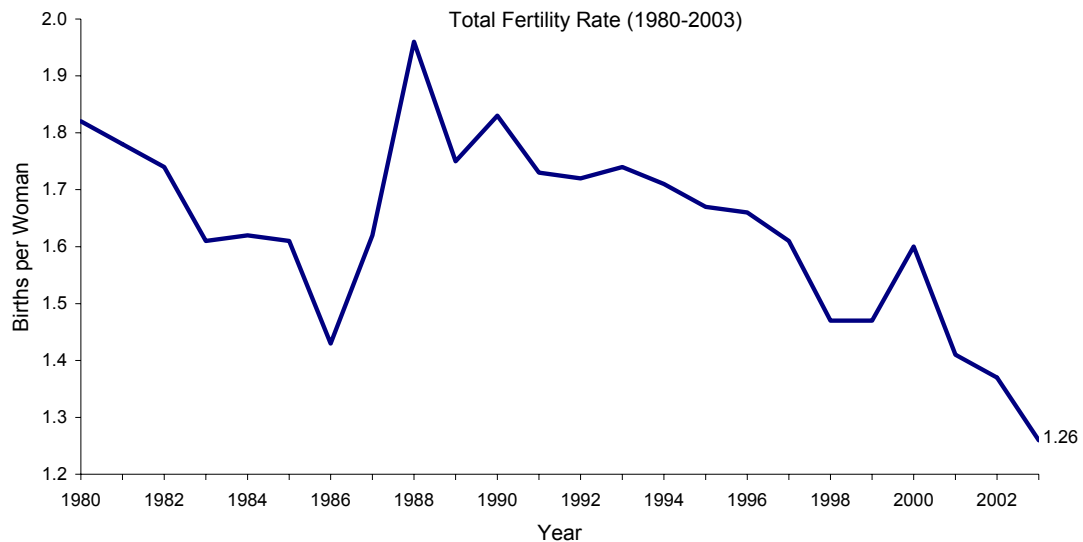
Building the Next Generation

3.29 Our children embody our hopes for the future. Singapore's birth rate is way below replacement level and falling. This is a serious problem. A declining birth rate will sap the vitality and resilience of our country.

3.30 Over the years, we have introduced many measures to encourage and support parenthood. After our first package in 1987, the total fertility rate (TFR), which reflects the number of children a woman is expected to have during her lifetime, jumped up to 1.96, as seen in the chart. This was partly because 1988 was a "Dragon" year, but the impact of the package was felt through the first half of the 1990s. Unfortunately the effect seems to have worn off over time, and the underlying trend of a falling TFR has reasserted itself. By the next "Dragon" year in 2000, the TFR had declined to 1.60. I am not sure what the next dragon will be. It may be a lizard! The Baby Bonus scheme and further generous tax

incentives introduced in 2000 have failed to reverse this trend. We give out over \$200 million annually in tax reliefs and rebates, and more than \$100 million has been disbursed under the Baby Bonus scheme. Yet the TFR for 2003 dropped to a historic low of 1.26. This is one of the lowest birth rates in the world. Only 36,000 babies were born last year, far fewer than the 50,000 babies we need to replace ourselves.

Chart 2: Total Fertility Rate



3.31 The accelerated decline in TFR since 1998 was partly caused by economic uncertainty – these were the years of the Asian financial crisis and the two recessions. But the underlying downtrend in birth rates is real and will continue unless we take decisive steps now.

3.32 Our existing measures are not enough. We must take a more comprehensive approach to solving this problem. We must encourage young people to marry and marry earlier, and make it easier for young couples to start and raise a family. And we have to take a long-term view. The impact of our policies on birth rates may not be felt immediately, because changing attitudes, mindsets and practices takes time and patience.

3.33 We need to shift social attitudes towards having children, even while we recognise that having children is a very personal decision which couples have to make for themselves. There is no single magic solution. The approach must be both holistic and coherent, addressing parents'

concerns from childbirth through the years of bringing up their children. As these are complex issues that require thorough discussion and deliberation, the Government will study them in depth over the next few months, before deciding on the most effective set of measures. Today I shall set out the principles that will guide our thinking.

3.34 Firstly, the aim of our measures must be not just to produce more children, but to produce the next generation of Singapore citizens. We want to grow the total population of Singapore, but equally important, we also have to reproduce and maintain the core group of citizens who will build and defend our country, and without whom we would not be a nation. Thus our measures must focus on encouraging more Singapore citizen babies.

3.35 Secondly, the problem is more serious for the mothers who are more educated and earn higher incomes. The higher the woman's career attainment, the less likely she is to get married and the fewer children she is likely to have. This is true not just of graduates, but also of women with secondary education. It is understandable because the more a woman is able to earn a living, the heavier the opportunity cost to her of having children. Therefore while our measures must cover all families, we must especially make sure that the incentives are effective for the better qualified women.

3.36 Thirdly, while encouraging procreation is critical, realistically it will be very hard to raise our TFR back to the replacement level of 2.1. Even other countries which have managed to reverse falling birth rates have not achieved replacement fertility. We therefore need to boost our population through other ways. In particular, we need to open our doors to immigrants who can contribute to Singapore. After getting them here, we need to help them settle down and integrate into our society. We need the right policies to encourage them first to become permanent residents (PRs), and then to take up citizenship. This means treating PRs and citizens differently, so that PRs have incentives to take up the privileges and responsibilities of being Singaporeans.

3.37 As for specific measures to encourage procreation, a comprehensive approach should include adequate support facilities such as infant and child care arrangements, better balance between work and family life, and of course financial help measures.

3.38 To start with, we have to consider the issue of maternity leave. We have hitherto been reluctant to increase statutory maternity leave. But many working mothers feel that the current two months is too short. A

major worry of working mothers is that they will have too little time with their children, particularly in the first few months after birth which are crucial to bonding mother and child. We may need to extend the period of maternity leave, but without overburdening employers with added costs.

3.39 Next, when the mother returns to work, she will often want to put her child in affordable and reliable child care facilities. The Government already subsidises child care, but infant care is more expensive. We will therefore look into providing more financial help for infant care.

3.40 Next, we need to strike a better balance between work and family life. Many couples cite the lack of family time and flexible working arrangements as an impediment to having more children. As an employer, the Government will review civil service work arrangements, without affecting essential public services. We will set a clear example to companies of how employers can create a work environment that is supportive of families.

3.41 Finally, while families should not have babies just because of financial incentives, tax reliefs and rebates for parents and working mothers appreciably lighten the financial burden of bringing up children. We need to simplify and enhance the existing tax incentives, to make them more accessible and attractive to couples. In fact, I find them quite hard to understand too. I think my wife has figured them out.

3.42 Two civil service teams visited Europe recently to study how other countries are tackling their falling birth rates. One went to Italy, the Netherlands and France, and the other to Norway and Sweden. Norway and Sweden have one model. They are both welfare states and they have succeeded in bringing their birth rates up. Netherlands and France have succeeded in bringing their birth rates up. Italy has not. We wanted to know why one worked and the other did not. We will study the lessons drawn and come up with our own measures. As several ministries are involved, I have tasked Mr Lim Hng Kiang, Minister in the Prime Minister's Office, to take charge and to make specific proposals. He will be assisted by an inter-ministry civil service Working Committee on Population chaired by Mr Eddie Teo, Permanent Secretary in the Prime Minister's Office. I have asked the committee to complete its work before National Day.

Adequate Finances for Retirement

3.43 With the ageing of our population, we have to ensure that working people put aside enough resources to support themselves in their old age. Today, most of the elderly in Singapore receive some financial support from their children. But longer life spans, rising singlehood, and low fertility rates are making it harder for old people to rely on their children for support. There is a pressing need to make sure that Singaporeans are self-reliant and financially independent in their old age.

3.44 Under the CPF Minimum Sum Topping-Up Scheme, individuals are allowed to make top-ups to the CPF Retirement Accounts belonging to themselves, their spouses, parents and grandparents. They can make top-ups in cash or out of their CPF Ordinary Account, up to the Minimum Sum in the Retirement Account. Currently, individuals making such cash top-ups enjoy a tax relief of up to \$6,000 per year.

3.45 With lower CPF contributions and the higher CPF Minimum Sum, we want to encourage more people to voluntarily top up their own or their family members' Retirement Accounts. I am therefore raising the tax relief ceiling on cash top-ups from \$6,000 to \$7,000, with effect from YA 2005.

3.46 Non-working spouses, such as full-time housewives, may also be financially vulnerable in their later years. At present, individuals are not entitled to any tax relief when they make cash top-ups to the Retirement Accounts of their non-working spouses. We should encourage individuals who have the means to contribute to the financial security of their non-working spouses to do so. I will therefore be extending the tax relief to individuals making cash top-ups to non-working spouses who are 55 years old and older, and who earned not more than \$2,000 in the preceding year.

3.47 I hope these steps will help bolster the financial resilience of Singaporean families.

PART IV – LAND OF OPPORTUNITY

Making Singapore a Land of Opportunity

4.1 Singapore is what it is today because it has been a land of opportunity for enterprising people from all over Asia. Our attractions are unique. We are at the crossroads of East and West, a modern, cosmopolitan city connected to the world of finance and business, yet rooted in the ancient cultures of our forebears. We offer a vibrant economy where people can earn a good living, a stable society where they can raise strong families, and opportunities for all to build a brighter future. And now with Asia on the rise, we must remake Singapore as a land of opportunity.

A Competitive Tax Regime

Reducing Corporate Income Tax

4.2 A key element of our efforts to remake Singapore is a globally competitive tax regime. Lower direct taxes encourage businesses to make new investments and individuals to work hard and achieve. In 2002, Government accepted the ERC's recommendation to lower the corporate tax rate to 20% by Year of Assessment (YA) 2005 and as the first step, brought it down to 22%.

4.3 I have decided to reduce the corporate income tax rate to 20% with effect from YA 2005. This is expected to cost the Government \$800 million annually. It will make Singapore a more attractive business hub, encourage new investments, and spur entrepreneurship.

Deferring the Reduction of Personal Income Tax

4.4 The Government had also set the target of lowering the top personal income tax rate to 20% by YA 2005. While this remains our target, the unexpectedly difficult economic conditions in the last two years have forced us to reconsider the timing of the reduction.

4.5 First, our spending commitments have increased, as I explained earlier. To balance the budget by next year, we not only need to tighten our spending, but also to husband our tax revenues.

4.6 Second, the delay in raising the GST rate to 5% has dented Government revenues. The extra year taken to phase in the GST increase cost \$700 million in revenue foregone, more than the \$425 million that

would be lost annually if we reduced the top personal income tax rate to 20%.

4.7 Third, while we expect stronger growth this year, we are not certain if this will be sustained into FY05 and FY06. Should the US economy slow down after the Presidential election, our growth and fiscal position will be affected.

4.8 I have therefore decided to defer lowering personal income taxes for the time being. However, a 20% top personal income tax rate remains the Government's goal. The Government will watch the budgetary position and economic outlook carefully, and will reduce personal taxes as soon as conditions permit.

Exempting Individuals' Foreign-sourced Income

4.9 Currently, foreign-sourced income received in Singapore by Singapore resident individuals is subject to tax unless specifically exempted. Last year, I announced a foreign-sourced income exemption regime under which foreign dividends, branch profits and service income are exempt from tax. This mainly benefits companies, with individuals benefiting only insofar as they earn dividends or service income from abroad.

4.10 The ERC had recommended that all foreign-sourced personal income remitted to Singapore be exempted from tax too. This would encourage Singapore resident individuals to remit their offshore funds to Singapore for investment and management. This in turn would boost our private wealth management industry.

4.11 I have therefore decided to exempt from tax all foreign-sourced income received in Singapore by resident individuals from YA 2005. With this change, Singapore will now tax individuals on a purely territorial basis.

Exempting Individuals' Singapore-sourced Investment Income

4.12 I have also decided to exempt from tax all Singapore-sourced investment income derived directly by individuals from financial instruments. This will help ensure that the exemption of foreign-sourced income does not bias individuals against investments in Singapore instruments. More importantly, it will align the tax treatment of different kinds of investment income, and encourage individuals to save and plan for their retirement.

4.13 The tax exemption for all financial instruments other than standard deposits, for example bonds, annuities and unit trusts, will take effect from YA 2005. For standard deposits, last year I announced a partial tax exemption on interest income for YA 2005, to be followed by full exemption from YA 2006 onwards. These arrangements still stand.

4.14 These two changes – exempting individuals’ foreign-sourced income and exempting Singapore-sourced investment income derived by individuals – will cost the Government about \$42 million each year. Details of the scope of both exemptions are set out in Annex B.

Promoting Singapore as a Business Hub

Regional HQ incentive

4.15 To be a land of opportunity, Singapore must continue to be the choice location in Asia for MNCs to base their HQ operations. But we face increasing competition from within and outside the region. I have decided to extend the maximum duration of the existing Regional HQ scheme from three to five years, with immediate effect. Companies that have already been here for more than a year will now also be eligible for this scheme. This will strengthen Singapore’s reputation as a prime location for HQ operations and attract more HQ companies to Singapore.

Pioneer Incentive

4.16 We must also attract and root new MNC activities in Singapore, to create new jobs and opportunities. This is why, even as we diversify our economy and build up our domestic sector, we must stay attractive to MNCs. But competition for MNC investments has increased in the last decade, making EDB’s task more challenging than ever.

4.17 Our response is two-fold. First, our workforce must have the skills and expertise to undertake more knowledge-intensive and higher value-added activities. Second, the package of tax incentives that we offer to MNCs making large investments in Singapore must remain attractive. To this end, I have decided to extend the maximum duration for the pioneer incentive from 10 to 15 years, with immediate effect.

Withholding Taxes on Royalty Payments

4.18 Exploiting new knowledge and ideas is important if Singapore companies are to compete internationally. As our economy upgrades, more Singapore companies will develop their business by exploiting Intellectual Property (IP). Much IP is held outside Singapore and our

companies have to pay royalties to the IP owners to be licensed to use them. Withholding taxes on royalties is a business cost that will discourage Singapore companies from exploiting IP.

4.19 I have therefore decided to lower the withholding tax on royalty payments from 15% to 10% with effect from 1 January 2005. This will be of greatest help to smaller businesses that are not enjoying any of the existing incentives for royalty payments. Withholding tax is usually an item for negotiation in avoidance of double taxation agreements, but we are taking a unilateral step in our own interest to spur our transition to a knowledge-based economy.

Encouraging Entrepreneurship

Tax Exemption for New Companies

4.20 New companies represent our hopes for a more entrepreneurial economy. Government will give these start-ups every opportunity to thrive and succeed. I have therefore decided to fully exempt from tax the first \$100,000 of normal chargeable income (excluding Singapore dividends). This exemption will apply to new companies for each of their first three years of assessment that fall within the period YA 2005 to YA 2009. This, together with the current partial tax exemption feature of our corporate tax regime, underscores our commitment to keep statutory costs on entrepreneurs as low as possible. Details of this scheme are provided at Annex C.

Financing for Start-Ups

4.21 One of the key pre-occupations of new enterprises is access to financing. Currently, the Technopreneur Investment Incentive (TII) encourages private angel investors to fund high-tech start-ups. But not all successful start-ups need to be high-tech. Some succeed by selling mundane items, from coffee, sushi to hamburgers, in innovative ways. I have decided to expand the current Technopreneur Investment Incentive (TII) to include all forms of start-ups and not just high-tech start-ups. The TII will be renamed *Enterprise Investment Incentive* (EII). Investors in start-ups awarded the EII will enjoy tax deductions for losses incurred if these companies fail, or if they have to sell their shares at a loss. The EII is expected to cost Government \$36 million each year.

4.22 The Government will also embark on a SME loan securitisation project this year to help a wider pool of SMEs gain access to financing.

Promoting Financial Services

4.23 In financial services, we have a unique opportunity to become the private wealth management centre of Asia, serving high net worth individuals from the region and beyond. The industry estimates that there are 1.8 million high net worth individuals in the Asia-Pacific region, with private wealth totalling US\$5.7 trillion. This wealth will grow even more, with the rapidly rising incomes and high savings rates in the region. Our strong economic fundamentals, socio-political stability, efficient legal infrastructure, and sound regulatory regime place us in a good position to service their needs.

4.24 We have done well so far. Existing private banking players have expanded their activities in Singapore. We continue to attract new players, who bring a diversity of new products and business models that have added depth and range to our financial markets. Employment in this industry has nearly doubled over the past three years. The tax exemption of individuals' foreign-sourced income and Singapore-sourced investment income that I have just announced will make Singapore even more attractive as a wealth management hub.

4.25 As financial sector activities are continually changing and ever mobile, we have updated our existing incentives to keep them relevant and help maintain Singapore's attractiveness as a leading financial centre. Among other changes, I have decided to enhance our incentives to promote the short-term debt market, the structured finance market, processing services for financial institutions, commodity derivatives trading, secondary loans trading, and SGX trading. (Details are at Annex D.)

4.26 I have also decided to expand the scope of income that will be exempted for Designated Unit Trusts (DUTs) and the tax exemption schemes for foreign investors and foreign trusts. Examples of income covered by this expansion in scope are rental and discount income derived from outside Singapore and received in Singapore. (Details of these enhancements are at Annex D.)

Other Tax Changes

Approved International Shipping Enterprise Scheme

4.27 To retain and attract international ship owners and operators to operate from Singapore, the current Approved International Shipping Enterprise (AIS) scheme will be expanded. Currently, the onshore charter income of an AIS company is not tax exempt, except when the

charter income is received from another AIS company. With effect from YA 2005, all onshore charter income received by an AIS company will be tax exempt.

Streamlining the Processing of Estate Duty

4.28 I am streamlining the processing of estate duty. For deaths occurring on or after 1 January 2005, the first six months from the date of death will now be an interest free period. Administrators/Executors will now have six months to file a complete return before interest starts accruing. Also, after the Notice of Assessment has been issued by IRAS, a grace period of 30 days will be provided for payment of estate duty where no penalty is levied. The penalty only kicks in after the grace period expires. This new arrangement ensures that administrators/executors are not unduly penalised if they co-operate with IRAS to file complete returns and make payment promptly.

Motor-Vehicle Taxes

4.29 To lower the upfront costs of car ownership, I have decided to reduce the Additional Registration Fee (ARF) from 130% to 110% of Open Market Value (OMV). This will apply to cars with COEs obtained from the first COE bidding exercise in March 2004 onwards.

4.30 Taxis and cars have previously been taxed differently. Our policy has been to progressively harmonise the ARF and Excise Duty (ED) that they pay. Thus I am raising the ED for taxis from the current 10% of OMV to 20% of OMV, the same rate as that for cars. This will be effective today. Taken together with the ARF cut, new taxis will still enjoy a net reduction in upfront taxes of 10% of OMV.

Liquor Duties

4.31 To rationalise our liquor taxes and to bring them in line with our international obligations, I am raising the excise duties on certain types of liquor and reducing them for others. The new rates will take effect today and are set out at Annex E.

4.32 Currently, Singapore Customs assesses the duty on liquors based on standard sizes. Most liquors are sold in standard sizes, but brandy, whisky and sake occasionally come in non-standard size bottles. Singapore Customs will therefore stop the practice of assessing liquor duty based on standard bottle sizes, and instead assess liquor duty based on exact volume. The removal of standard sizing will save the liquor industry about \$3.7 million in duties each year.

Tobacco Duties

4.33 A local study by NUS shows that healthcare, absenteeism and loss of productivity stemming from smoking-related diseases cost between \$700 million and \$800 million in 1997. I have decided to further raise the excise duties on all tobacco products with effect from today to discourage smoking, especially among our young. Excise duty on cigarettes will go up from \$255 per 1,000 sticks to \$293 per 1,000 sticks. I am also harmonising the excise duties on other tobacco products with cigarettes. The new duties are at Annex F.

Overall FY 2004 Fiscal Position

4.34 Mr Speaker, Sir, this Budget will deliver \$1 billion of tax savings and Medisave and Medifund benefits for businesses and individuals. It will support our economic recovery this year. More importantly, these measures will build long-lasting competitive advantages for the economy, enhance our capacity to deliver good public services particularly in healthcare and education, and provide more help for families with dependents. The tax changes and incentives I have announced will increase the deficit from the \$750 million projected in the FY04 Budget Book to \$1.35 billion. The Government is able to finance this deficit from funds accumulated in its current term and will not need to draw on past reserves.

PART V – CONCLUSION

5.1 2003 was a tough year, but we emerged from it stronger. Our response to SARS demonstrated our resilience as a people. We are well-placed to ride the upturn in the global economy this year. Most importantly, we have what it takes to sustain Singapore's dynamism and growth over the long term.

5.2 But we must also be prepared to encounter more shocks and uncertainties. Fresh terrorist attacks could undermine confidence in the region. New diseases more dangerous than SARS or avian influenza may emerge. China and India will pose fresh challenges as they continue to open up to the world.

5.3 Our strategy in this environment of growing competition is to keep our economy open and continually enhance our competitiveness. This means upgrading our skills, making our wages more flexible, encouraging entrepreneurship, and promoting free markets. We must not seek to shield ourselves from competition but to meet it and excel.

5.4 We are on the right track. We are lowering taxes, spending only on essentials, and maintaining a prudent fiscal position. We are creating the conditions for new businesses and enterprises to flourish while building on our strengths in manufacturing and services. And we are creating opportunities for enterprising Singaporeans, while targeting social safety nets at the truly needy who lack other means of support.

5.5 Looking ahead, there is much to be hopeful about. We are at the heart of a resurgent Asia, midway between the booming economies of China and India. Opportunities abound in the region and beyond. The Government will play its part to make things possible. And I have every confidence that Singaporeans will seek these opportunities, grab the openings and create new possibilities for ourselves. We will adjust to change, overcome adversity, and confront challenges courageously and imaginatively. We will press on with confidence, and reach out for success. Together, as one Singapore, we will build a future of opportunity for ourselves and our children.

5.6 Mr Speaker, Sir, I beg to move.