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Schemes Work Hand in Hand to Boost Wages

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REACTIONS TO SINGAPORE BUDGET 2013

Three academics give their take on how this year's Budget helps both workers and companies in the push for higher productivity

Schemes work hand in hand to boost wages

By HOON HIAN TECK
FOR THE STRAITS TIMES

IN THE first three decades or so of Singapore's economic development after independence, the big lift in Singaporeans' average standard of living occurred with equity.

Market forces pulled up the wages of the relatively less skilled by more than the wages of the skilled so the wage gap narrowed.

In the past decade, however, wages of workers at the bottom of the income distribution saw little growth after accounting for inflation. Policy intervention is therefore necessary to boost the earnings of low-wage workers and to strengthen social cohesion.

The question is how best to boost the earnings of low-wage workers? The Workfare Income Supplement (WIS) scheme in 2007 provided one answer.

It is to give income supplements to older low-wage workers, on condition that they hold a job.

In this respect, the WIS is different from a negative income tax, made famous by the late economics Nobel laureate Milton Friedman, which would provide an income supplement even if a person did not work and so had zero income. With a negative income tax, there is a pure wealth effect and no substitution effect towards work – that is, people are wealthier but not any more inclined to work.

Holding a job provides many non-pecuniary rewards such as engagement with colleagues and job satisfaction. Research also shows that the cost of long-term unemployment goes beyond just the loss of wages. The long-term unemployed also suffer non-monetary costs, such as quality of life.

With the WIS, the Government steps in to boost the worker's earnings while providing the incentive to hold a job. In Budget 2013, the maximum monthly income threshold for a WIS payout is raised from $1,700 to $1,900.

This gives incentives for more low-wage workers to take up the training opportunity provided by the Workfare Training Support scheme, without fearing that the higher pay they command after training would disqualify them from WIS payouts.

The larger share of WIS payouts given in the form of cash, from 29 per cent to 40 per cent, helps alleviate cashflow problems faced by low-wage workers. The increase in the amount of WIS payouts by 25 to 50 per cent will raise the take-home pay of low-wage workers. Central Provident Fund contribution rates by employers and employees will go up, boosting their retirement incomes as well. Overall, the WIS enhancements announced in Budget 2013 strengthen Singapore's social safety nets without weakening the incentive to hold a job.

It is a basic lesson in economics that high pay can only be sustained by sufficiently high labour productivity.

Singapore's reliance on the inflow of global ideas and technology, particularly in the manufacturing sector, delivered overall labour productivity growth until the past decade when the services sector further expanded.

While productivity levels in manufacturing are high by global standards, they remain low in many industries within the services sector that is dominated by small and medium-sized enterprises (SMEs).

The Wage Credit Scheme (WCS) introduced in Budget 2013 is an innovative policy instrument that works in tandem with the Productivity and Innovation Credit (PIC) scheme to help SMEs on their journey to becoming more productive. The WCS co-pays 40 per cent of wage increases for workers earning up to $4,000, for three years.

How does the WCS work? Suppose a firm, encouraged by the enhancement of the PIC scheme that subsidises capital investment, chooses to automate a labour-intensive process. As a result of the automation, suppose that a worker's labour productivity is raised by 10 per cent. In normal circumstances, with an additional worker being able to contribute 10 per cent more to the firm's revenue because of the automation, the wage that it can afford to pay the worker and yet stay competitive is increased by 10 per cent. But with the WCS, the Government covers 40 per cent of this wage increase, leaving the firm with a higher profit.

The higher profitability may encourage the firm to further increase its capital investment, which would create a second-round effect of further increasing wages. Thus, there is a potential multiplier effect that leaves the firm more productive and paying its workers more.

Since the WCS is in force only from 2013 to 2015, some firms that might already have future plans to mechanise or innovate might choose to bring forward their investment plans.

Like a pair of scissors, we need two blades to work well. The WIS scheme, by supplementing a worker's wage, shifts out his labour supply. The WCS, in giving firms incentives to boost labour productivity in order to enjoy the wage credit, acts to shift out labour demand.

This is an innovative and business-friendly policy instrument that has the potential to boost the pay of low- to medium- wage workers while stimulating employment.

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Workfare recipient Y.K. Tang, 63, showing her handicrafts. With the WIS income cap raised, more could go for training without fearing that the higher pay they get after that would disqualify them from WIS payouts. ST PHOTO: KUA CHEE SIONG

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