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PRIME MINISTER'S NEW YEAR MESSAGE 1987

Our growth in 1986 is a small 1.9 per cent. Half the economy - manufacturing, transport and communications - has done well. The other half - commerce, financial and business services and construction - remains depressed.

The economy is recovering because we took decisive measures to tackle our economic problems directly. We reduced business costs, including cutting taxes and employers' CPF contributions, and restrained wage increases. Our workers and trade unions have supported these actions. By not flinching from painful policies, Singaporeans have spared themselves higher inflation and a longer recession.

The soft option would have been for no reduction in employers' CPF contributions, no wage restraint, minor cost-cutting. Instead we would have had to accept a drop in the exchange rate of the Singapore dollar as the economy continued to weaken and the foreign exchange markets pushed the Singapore dollar down. The drop would have needed to be sizeable, to achieve the equivalent of a 15 per cent reduction in employers' CPF contributions. This would have led to a high inflation rate of more than 10 per cent, because Singapore imports its food, oil, nearly all manufactured and semi-manufactured products. Then workers' pay and CPF would have appeared the same or even more, but would have been worth less in purchasing power. Instead our inflation rate was less than zero: -1.4 per cent, i.e. each Singapore dollar bought slightly more in 1986 than in 1985. By dealing with the problem head on, we have simplified and shortened the process of adjusting our economy, and have avoided inflation.

External factors, like the appreciation of the yen, have helped. But we would have not been able to take advantage of these favourable developments if we had not set our house in order. If Singapore had not become more competitive, Japanese companies, looking for an external location because of a higher yen, would have skipped Singapore.

The forecast for the region is continued low commodity prices and therefore continued slow growth. Those sectors of the Singapore economy that are linked to the region will not perform well. Our growth rate in 1987 is expected to be only 3-4 per cent. This is not only less than the 6-8 per cent projected for the other Newly Industrialising Countries (NICs), it is also below our own estimated long-term growth rate of 4-6 per cent. It shows that our recovery is not complete.

Ministry of Trade & Industry (MTI) calculations show that although we have improved in competitiveness against the other NICs, we have not fully recovered the competitiveness we enjoyed against them before our high wage increases in 1980-83. We need at least one more year of high productivity growth and wage restraint to close the gap. If their wages go up this year whilst we stay put, the gap will narrow.

At the same time, we must press on with reforming our wage payment system. In a next recession, and there will inevitably be a next one, we are unlikely to have large employers' CPF contributions to cut back. At present we have in-built rigidities in our wage structure. The NWC has endorsed its Subcommittee Report on Wage Reform. Twenty-three large local companies and MNCs, as well as the banking and insurance groups, are already discussing these ideas with their unions. Companies who have not started should do so.

The objectives are to build flexibility into our wage system, and to link workers' rewards to (a) productivity growth, (b) performance of the firm and (c) performance of the individual. Flexibility will increase the survival capacity of companies. It is a safety margin for workers so that they can keep their jobs when companies fare poorly. If they do this, in a next recession, management can reduce costs rather than output, by cutting the flexible component of wages. So we can recover from the recession more quickly, with fewer workers retrenched.

My younger colleagues have diagnosed our economic problems. They decided on cost-cutting and wage restraint to attract new investments, and to create a favourable climate for a total business centre. Union leaders have persuaded and convinced the workers to back this strategy. And our economy is on the mend. But the more difficult part will come next year. Although MTI forecasts 3-4 per cent growth, commerce, financial and business services, and construction are not expected to rebound, and growth will have to come from manufacturing, and transport & communications. To reach a figure of four per cent for the economy as a whole, these two sectors, manufacturing and transport & communications, will have to grow by eight per cent, a high target, achievable only if we keep costs down and productivity up. Therefore, to improve the overall performance of the economy, manufacturing and transport & communications workers will have to moderate their wage expectations.

Workers will feel the pick up by early 1987, when the NWC will be considering the 1987 recommendations. Factories will work more overtime, and hire more workers. Workers will read of better profits in company reports, the result of last year's cost-cutting. They will be tempted to heed the good news and to press for a wage increase.

With output training, if employers in the manufacturing sector relent and become overgenerous, they will become the pace setter. Then wages in other sectors will be forced to follow suit, regardless of their ability to pay. If this happen, our entire strategy for economic recovery will be jeopardized.

The test for our younger generation of Singaporean leaders and workers is whether they can put long-term interests ahead of short-term gains, and by demonstrating wage-restraint discipline, win the confidence of investors.

I wish you all a Happy New Year.

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