The Foreign Worker Levy in Singapore’s Industrial Sector: Efficacy and Issues

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Introduction

Economic development in Singapore has two aspects: quantitative and qualitative. For a small open city state, its economic achievement is well emplaced in very credible growth rates. Over the period 1960 to 1987, its real gross domestic product (GDP at 1985 market prices) grew at an average annual rate of 8.3% (Singapore National Accounts, 1987). On a comparative basis, Singapore achieved an average annual growth in GDP of 5.3% over the period 1980 to 1986 which was higher than 4.8% in both Thailand and Malaysia but lower than 5.9% in Hong Kong (World Development Report, 1988). Its growth rate in 1985 dived to -1.6% but recovered to 1.8% and 8.8% in 1986 and 1987 respectively. It bounced back to a double-digit 10.9% for 1988. The prognosis for 1989 is more modest with an official forecast of 6% of 7%.

Qualitatively, economic development has been accompanied by economic restructuring, first from traditional entrepot functions to modern manufacturing-cum-service activities. The manufacturing sector has been transformed from low value-added labour-intensive activities to high value-added capital-intensive industries. But until the second phase of industrial upgrading from 1979, economic growth in the 1970s had been horizontal without high total factor productivity growth (Tsao, 1985 and Toh 1985). The much desired substitution of capital for labour has not quite taken place. The “one big mistake” made by Singapore was not to have pushed enough for higher wages after the first oil shock (Straits Times, 10 March 1984). In compromising to keep wages in hand until 1979, it was estimated that Singapore lost 6% in productivity increase, one consequence of which is the influx of foreign workers.

That Singapore’s structural diversification has been accompanied by a reliance on foreign workers could be seen from the increase from a total of 72,590 non-citizen and non-resident (foreign) workers in 1970 to 119,483 in 1980 (Census of Population, 1970 and 1980). These constituted 11.15% and
11.09% of the total labour force respectively. Currently, there is an estimated pool of 150,000 foreign workers or 12% of the labour force. An official view expressed in 1987 was that the foreign labour force should be no more than 25% of the total labour force but no absolute number was set (Straits Times, 1 September 1987).

The demand for foreign workers is greater in faster growing sectors. Whereas the bulk of foreign workers was absorbed by the construction industry before 1984, the majority has since gravitated to the manufacturing sector. Productivity in the manufacturing sector fell from 3.5% in 1987 to 2.9% in 1988, below the official target of 3% to 4%. In 1988, foreign workers accounted for one-half of the jobs created in the manufacturing sector and contributed 2.8 percentage points to overall growth compared with the 3.8 percentage points contribution by local workers. This suggests that the high economic growth in 1988, as in earlier years, had been made possible by a generous inflow of unskilled foreign workers.

The government's concern with the economic, social and political costs of foreign workers has resulted in a number of mechanisms to control and regulate their inflow into Singapore. The chief of these is the foreign worker levy (FWL) introduced in April 1982.

The main aim of this paper is to provide an economic analysis of the effectiveness of the FWL in achieving its two interrelated objectives, in consideration of Singapore's resource constraints. The first of these objectives is to reduce the dependence on unskilled workers. The second is to expedite economic restructuring or the transition of labour-intensive production to more capital- and skill-intensive methods of production. The analysis is undertaken using the framework presented in Section II. The issues arising from the economic analysis and our assessment of the economic impact of the FWL are discussed in Section III. The final section attempts to consider some alternative mechanisms and policy refinements though it is appreciated that any policy suggestion must be economically, administratively as well as politically compatible.

The Economics and Issues of the Foreign Worker Levy

Scope and Objectives of the FWL

Singapore has no xenophobia toward foreign labour, having started with an immigrant stock and its development being highly dependent on foreign investment, technology and markets. However, one should note a distinction between the continuing open-door policy for skilled, professional and technological manpower as against the phasing out of foreign unskilled workers (Lee, 1982, in Jayakumar, ed, pp. 12 – 13). Foreign workers come into