

COST REVIEW COMMITTEE REPORT (1993)

EXECUTIVE SUMMARY

ACCURACY OF THE CONSUMER PRICE INDEX (CPI)

The Cost Review Committee (CRC) was set up to study the public's concerns regarding the rising cost of living in recent years and to study the accuracy of the CPI.

2. Having examined the CPI in detail, the committee concluded that the method of computing it is sound. The CPI is a general indicator of changes in the prices paid by households for goods and services. All goods and services, like bus fares, total purchase price of cars (including import duties, Additional Registration Fee and Certificates of Entitlement) and cost of hiring a foreign maid (including the foreign maid levy) are included in the CPI.
3. The committee was also of the view that 5-yearly revisions of the weights of the CPI were adequate. However, it recommends that updating of the weights be carried out more rapidly after the collection of data.
4. The committee agreed with the view that different households, with different consumption patterns, may face different inflation rates. Hence, it recommends that separate CPIs be compiled and published for different income groups. These separate indices could be published twice a year to complement the monthly CPI for the overall population.

TRENDS IN COST INCREASES AND INCOME GROWTH

5. During the period 1980-92, Singapore's inflation rate averaged 2.4% per year. In addition, income growth has consistently outstripped increases in prices, resulting in an increase in real wages. Prices of items in four out of the five CPI broad groups (namely, food, clothing, housing, and transport and communication) have also increased at a slower rate than wages. The exception is miscellaneous items which saw a slightly faster rate of price increase compared with income in 1986.
6. When the inflation experiences of different expenditure groups were compared, it was found that lower-expenditure households generally experienced a lower rate of inflation than the general population during the period 1984-92.

COST OF LIVING: AREAS OF CONCERN

7. The committee identified four main areas of concern: health care, housing, education and transport. Health care and education are similar in that they are both labour-intensive services and there have been changes in the government's subsidy policy in recent years. Housing and transport are similar in that they are both related to the limited land supply in Singapore.

Health Care

8. There is strong public concern over the affordability of hospitalisation fees because fees have increased sharply in recent years, particularly in 1989/90. For example, the daily ward charge at the Singapore General Hospital rose by 21-29% for Class A and B1 wards, and by 12-23% at Alexandra and Tan Tock Seng hospitals in 1990 after remaining unchanged since 1984.
9. The fee increases were large for two reasons. First, costs increased due to higher wage costs, and higher costs of new equipment and treatment methods. However, fees were not increased after 1984 because the government did not want to impose a burden on the public during the recession and the wage-restraint period which followed it. As a result, fee increases in 1989/90 were sharper than if the increases were spread out over a longer period.

10. Second, the government set new subsidy rates for the various ward classes which were lower than existing rates. As a result, fees had to be increased to move towards the target subsidy rates. Although the subsidy rates continue to be high for Class B2 and C wards, the public feared that the government would raise fees sharply in future to reach the target quickly.

11. In addition, families also paid more in hospital bills due to a change in disease pattern in Singapore, towards chronic or degenerative conditions like heart disease and cancer which are more costly to treat. There is also demand for more and better health care services because of rising affluence, an ageing population and a population that is more informed and less averse to seeking treatment in hospitals.

Housing

12. The prices of new Housing and Development Board (HDB) flats rose sharply in the last five years. For four-room flats, prices rose by an average of 12% per year between 1988 and 1992, but only 2.5% per year between 1981 and 1988. Like health care, the price increases were not large if evenly spread out over the whole period but were in fact very sharp for those who bought their flats in the last few years.

13. There are four reasons for higher HDB flat prices. First, with the introduction of the Differential Pricing Policy scheme in 1988, prices of more desirable flats (eg, those in choice locations and on higher floors) cost more than less desirable flats. Buyers who chose the most desirable flats paid higher prices than the "average" flat. Second, construction and land costs rose significantly between 1988 and 1992. Third, new flats which have better finishing cost more than older flats. Fourth, the effect of upgrading. Upgrading is proceeding at a rapid pace and accounts for half of the applications for new HDB flats. Younger families are also opting for larger flats.

14. The committee was of the view that the government should focus on providing affordable housing for the lower- and middle-income groups. Subsidies for HDB flats should be focused largely on three- and four-room flats, with some moderate subsidies for five-room flats to help Singaporeans meet their aspirations to upgrade. Subsidies on executive flats should eventually be removed, but at a pace that does not result in sharp increases in prices. The HDB should continue to make available three-room flats, in addition to budget four-room flats, to meet the needs of lower-income households.

15. As for private property, prices rose at an average rate of 13% per year over the last five years. In particular, condominium prices have risen the fastest, at an average rate of 14% per year during this period. These increases coincided with a period of strong economic growth.

16. There are three main reasons for higher private property prices. First, economic growth is strong while the amount of land in Singapore is finite. The amount of land offered for sale each year is planned carefully based on an assessment of long term demand for the various types of properties. Even so, this is unlikely to keep pace with the increases in income and aspirations. As a result, it would be unrealistic to expect that the larger number of households which meet a certain income threshold will be able to own private landed property compared with their counterparts 20 years ago.

17. Second, the increases in HDB flat prices have enabled those who bought their flats before the sharp price increases to sell their flats with significant capital gains and upgrade to private property. Third, fears that private property would become less affordable in the future may have encouraged more people to enter the market in recent years.

Education

18. The committee identified concerns about the affordability of university fees, independent school fees and private tuition costs.

19. University tuition fees were increased sharply, by 30% (for non-medical courses) in 1989 and a further 35-40% in 1991. There were two main reasons for this: an increase in cost (mainly manpower cost) and a reduction in the government's subsidy rate.

20. The committee considered the issue of government subsidy and looked at both the rationale for supporting university graduates as well as the level of that support. The consensus was that the government should continue to subsidise tertiary education since the academic training that these students received would enable them to

contribute more to society.

21. The committee is of the view that the government subsidy rate should not be reduced further to its target of 75% of recurrent cost, but capped at the current 79% of recurrent cost. In this way, future fee increases should be more moderate as they will be due solely to cost increases.

22. Another area of concern was the fees at independent schools. The fees at the eight independent secondary schools range from \$70 to \$200 per month. In comparison, government secondary schools charge school fees of \$5 and miscellaneous fees of \$7 to \$9 per month. Various financial assistance schemes are available to ensure that students from poorer homes can attend independent schools. The committee welcomes the announcement that six secondary schools will become autonomous schools from next January. Such schools will provide an alternative for parents who may not wish to send their children to independent schools.

23. Significant proportions of students take up private tuition, ranging from 20% of post-secondary students to 50% of primary students. Fees range from \$100 to \$200 per month. The committee is of the view that private, one-to-one tuition is expensive, and parents can reduce their financial burden by making use of group tuition programmes offered by community organisations like Mendaki, the Singapore Indian Development Association (Sinda) and the Chinese Development Assistance Council (CDAC), or even private tuition centres.

Transport

24. In public transport, public concerns arose after the increase in bus and Mass Rapid Transit (MRT) fares in October and November 1990 respectively, and the inconvenience and increase in cost suffered by some commuters after network rationalisation. Taxi fares have also been increased on five occasions between 1982 and 1991.

25. As bus fares were increased during the Gulf war, some people wonder why they were not reduced when oil prices fell. The committee found that the reasons for the fare increases were not well-known to the public. Apart from higher oil prices, there were also increases in operating costs (mainly, labour and maintenance) and higher costs of new buses. For the MRT, funds had to be set aside to pay for new equipment in the future.

26. The main reason why bus fares were not increased for 9 years until 1990 is because of the continuous productivity improvements made, for example, switch to one-man-operated buses, the introduction of feeder services to reduce the distance that trunk buses have to ply within the new towns and greater use of double-decker buses. These cost-saving measures, as well as the fall in diesel prices, enabled the bus companies to maintain stable bus fares in the 1980s.

27. However, since these major steps in productivity improvements have already been taken, further measures to raise productivity are likely to be more difficult. Hence the increase in bus fares in 1990. There is one additional productivity measure which can be, and is being taken -- route integration and rationalisation. To maximise usage of the MRT which cost \$5 billion (at current prices) to build, it has been necessary to amend bus routes, where feasible, to channel commuters onto the trains. The integration of bus-MRT services allows the use of resources to be optimised, resulting in lower overall costs for providing an efficient public transport service. This, in turn, means lower fares for commuters.

28. Unfortunately, the first phase of the network rationalisation exercise started in January 1991, soon after the fare increases in late 1990. Given that the MRT fare structure is evenly spaced while the bus fare structure is more simplified and reaches a maximum of 90 cents (for non-airconditioned services), commuters who make long-distance trips on the MRT instead of buses would have to pay more. The 25-cent rebate helps to reduce the financial impact on these commuters but there is still a small proportion of commuters who ended up paying more.

29. Increases in taxi fares have resulted from a combination of cost increases and the need to provide a reasonable increase in income to taxi-drivers. The cost increases come mainly from various government measures to maintain the parity of statutory costs on both taxis and private cars. This is because taxis are inefficient users of road space and even more inefficient carriers of people, since they cruise empty one-third of the time. The committee noted that the desire to own cars would not be reduced even if taxi fares, already low by international standards, are further reduced.

31. Private transport costs have risen mainly because of the government's vehicle restraint measures, especially the Vehicle Quota System. As the size of the vehicle population is fixed under this system, the strong demand is

translated into rising bids for Certificates of Entitlement. Other factors are the appreciation of the Japanese Yen and the Deutschemark, and improvements in the features of new cars, like power steering, central locking and additional safety features.

Impact of the Goods and Services Tax

30. The committee was tasked to study the impact of the Goods and Services Tax (GST) on the cost of living and business costs, and to recommend ways to mitigate its effect on low-income households. It looked at the results of a cross-country study by the International Monetary Fund showing that the imposition of a GST is not inflationary. In most countries, it resulted in a one-off increase in prices, with inflation reverting to its underlying trend thereafter. Similarly, the committee was of the view that the GST is also unlikely to be inflationary, unless there is substantial and sustained profiteering.

31. Public pressure can be effectively brought to bear on errant traders. To keep consumers better-informed, more information on prices can be released by the government and the Consumers' Association of Singapore (CASE).

32. The GST also imposes costs on businesses, both in terms of start-up and learning costs, and the recurrent costs of maintaining the system. The committee found that the experience of New Zealand and the United Kingdom showed that compliance costs were not high, and they were typically in the range of 1-3% of turnover. Furthermore, the percentage fell as turnover increased, that is, compliance costs were lower the bigger the trader. Compliance costs are expected to be even lower in Singapore because our GST system is simple with few exemptions, and we have a higher exemption threshold of S\$1 million turnover, which will exclude most small traders.

BUSINESS COSTS AND COMPETITIVENESS

33. The committee found that there are three main areas of concern for businesses: rising business costs, strength of the Singapore dollar and Singapore's relative competitiveness.

Business Costs

34. Business costs have risen significantly since the recession in 1985/86. This is not unexpected as our resources became more fully deployed when the economy recovered from the recession. This is shown clearly in the trends in the Unit Business Cost index for the manufacturing sector which rose by a cumulative 23% between 1987 and 1992.

35. The underlying cause of cost increases is competition for labour and land. Smaller businesses also tend to face more difficulties in recruiting workers. For labour, the working of market forces is more easily understood; the flip side of higher costs for businesses is higher income for workers. In addition to higher take-home wages, restoration of the employers' Central Provident Fund (CPF) contribution rate and increases in foreign worker levy have also contributed to the increase in labour cost.

Strength of the Singapore Dollar

36. The committee recognises that a strong Singapore dollar has an uneven impact on business costs. The manufacturing sector and tourist trade are more badly affected than, say, the domestic commerce sector. However, a balance has to be struck between maintaining export competitiveness and keeping imported inflation low. A cheaper Singapore dollar need not necessarily lead to lower costs if wage costs rise to compensate for higher inflation.

Relative Competitiveness

37. As competition from other countries becomes keener, every effort should be made to improve productivity in order to maintain our international competitiveness. Cost increases not matched by productivity growth not only erode our competitiveness but would lead to higher inflation.

CONCLUSION

38. After having spent one year studying the issue of rising costs, the committee concluded that the concerns over rising costs stemmed from the steep price increases in the cost of health care, housing, education and transport in recent years. These increases stemmed from a mix of factors, such as the country's resource constraints, the reduction in rates of government subsidies and the timing of public sector fee increases. The growing demand among Singaporeans for higher quality goods and services has also contributed to their having to pay higher costs. The committee therefore recommended several measures that it believes will help keep future cost increases in check.

SUMMARY OF RECOMMENDATIONS

The Consumer Price Index (CPI)

- Separate CPIs should be compiled and published for different income groups. These could be for the lowest 20%, middle 60% and the highest 20% income groups. These separate indices could be published twice a year to complement the monthly CPI for the overall population.
- The imputed rental indicator for HDB flats should be replaced with an indicator that is more representative of market conditions.
- Results from the 1992/93 Household Expenditure Survey should be used to revise the weights of the CPI as soon as possible, in order to maintain the representativeness and relevance of the CPI.
- Consumer organisations such as CASE, with the help of the media, should do more to publicise detailed price information.
- The government should reach out to grassroots organisations, schools and members of the public through simplified brochures, talks and exhibitions to explain the nature and use of the CPI.
- The Department of Statistics should formalise its consultation process during its periodic reviews of the CPI.

Health

- Health care should remain affordable in Singapore. Fee increases, where necessary, should be made gradually.
- There should remain at least one government hospital to allow patients a wider choice.
- Checks should be made on public sector hospitals' acquisition and use of new equipment so as to prevent unnecessary tests which push up costs.
- Organisations like the National Trades Union Congress (NTUC) could consider setting up health management organisations to keep medical costs down.
- Medisave savings should be used prudently.
- Hospitals should improve their public relations to better inform the public about the availability of financial assistance. Financial counselling of patients should also be handled with sensitivity.
- Visiting hours of selected government out-patient clinics should be extended beyond the present hours.

Housing

- The government should focus its building efforts and subsidies on providing affordable housing for the lower- and middle-income groups.
- The HDB should consider making more three-room flats available to the public at posted prices.
- The HDB should continue to build five-room and executive flats to provide affordable upgrading and to act as a benchmark of prices for bigger and better quality flats.
- Subsidies on executive flats should be phased out gradually, taking into account conditions in the property market so that buyers do not face sharp price increases.
- To keep construction costs down, there must be continued efforts to raise the efficiency and productivity of the construction industry.
- The government should monitor the demand situation in the private property market and release adequate land for housing to prevent land prices from rising steeply and thereby raising property prices.

Education

- The government should maintain its subsidy rate for university fees at the current 79% of recurrent expenditure instead of reducing it to 75%, and the universities should control costs.
- Future fee increases, where necessary, should also be made gradually. They should reflect only the increases in underlying costs and not a reduction in government subsidies. Furthermore, future fee increases should be announced well in advance to give families enough time to plan their finances.
- Study loans and bursaries should be made more readily available. The number of awards should be increased and the application procedures should be simplified in order not to discourage applicants.
- Parents should make use of tuition programmes provided by schools and community organisations.

Transport

- Future bus or MRT fare increases should be made in smaller steps, for example, five cents or even one cent instead of 10 cents since the Farecard is now widely used. This would enable the public to adjust gradually to fare increases.
- The reasons for fare increases should be better explained to the public so that it does not get the impression that fare increases are caused by a single, temporary factor like the oil price hike.
- Network rationalisation exercises should not be made at the same time as fare increases and should be phased in over a period.
- Taxi services should not be de-regulated.
- The government should refine its vehicle restraint measures to allow more Singaporeans to own cars, while not adding to congestion. It could do this by introducing Manual Road Pricing and Electronic Road Pricing systems.

The Goods and Services Tax

- To prevent profiteering, the government could flood the market with essential products through organisations which have an interest in keeping consumer prices down, for example, NTUC FairPrice outlets can also act as a reference point for consumers to compare prices.
- CASE should continue to monitor prices and publicise its findings with the help of the media.
- Random checks should be conducted on shops before and after the GST is introduced. Monitoring of prices should begin way before the GST is implemented.
- Singaporeans should form consumer clubs which can act against profiteering by shopkeepers. Residents' Committees and Citizens' Consultative Committees can form a committee to watch and check prices in neighbourhood shops.
- The government should work with consumer groups and retailers to educate traders and the public on how the tax works and how prices will be affected. Dialogue sessions can also be conducted to explain the rationale behind the GST to senior citizens who are less educated.
- Existing laws on consumer protection could be reviewed. The term "profiteering" should be more precisely defined. Licences of errant traders could be suspended or revoked.
- If all else fail, the Price Control Act should be used to check unreasonable and widespread price increases.
- The committee was of the view that there is a need for an independent watchdog body to scrutinise cost increases' and to recommend a more gradual pace of adjustment. CASE is well-placed to perform such a role. Government's funding to CASE should be increased to allow it to play this role.

Measures to Keep Inflation Low

- A free trading environment.
- A strong Singapore dollar.
- Sound macro-economic policy, that is, prudent fiscal policy and a strong commitment to keep inflation low.
- Efforts to maintain productivity growth.
- Government bodies should constantly strive to maximise their efficiency and keep costs down.
- Improvements in the quality of public services should be made at a pace that does not result in high cost increases.
- Better co-ordination to space out public sector cost increases.
- Better dissemination of information.

- Singaporeans' expectations need to be moderated somewhat as the economy becomes more mature.
- CASE should be strengthened to play its role as a consumer watchdog body.
- Cost increases should be made after due consideration of their impact on the lower-income group.