Zero GST for basic goods? Bad idea

By Mukul Asher

What would be the effect of implementing a zero per cent Goods and Services Tax (GST) rate for basic commodities? Would it help to lower the cost of living for lower-income families in Singapore? What other measures should be implemented to help Singaporeans cope with high inflation?

Singaporeans are experiencing inflation higher than what they are used to. In April, the Consumer Price Index was 4.3 per cent, higher than a year ago, and inflationary pressures are expected to continue in the coming months.

Many people assume that doing away with the Goods and Services Tax on basic commodities such as rice and bread will help low-income households to cope with inflation.

But the case for excluding these commodities from the tax is weak. If this were done, there would be three major consequences:

First, GST revenue would drop. To make up for the shortfall, the current GST rate of 7 per cent would need to be increased. The Government might also cut the GST-related packages designed to help households.

Second, households will switch from the commodities subject to GST to the items that are not taxed. This shift in demand could push up the prices of basic commodities, partially defeating the purpose of exempting them from the tax.

Third, the change would further complicate GST administration and auditing. This is because GST is levied only on the value added (sales minus purchases) at manufacturing, wholesale and retail levels.

Making basic commodities GST-free would not only increase the cost of administering the tax but also make it more expensive for businesses to comply with GST regulations.

The average rate of GST/VAT (value-added tax) in member countries of the Organisation for Economic Cooperation and Development last year was 18 per cent.

Singapore’s GST rate of 7 per cent is low by international standards. It is only when the standard rate of GST exceeds 10 per cent that a lower – or zero – rate for basic commodities may be worth considering.

What else can be done to help households deal with inflation? Here are a few suggestions.

Write in to stask@sphe.com.sg with whatever questions you might have on economics, international or domestic. Each week, one or two questions will be selected to be answered by a panel of National University of Singapore economists.

Public-sector agencies, many of which operate in markets with limited price competition, affect the prices of many goods and services significantly. There is merit in reviewing in a more rigorous and integrated manner the pricing decisions that these agencies make.

The Competition Commission of Singapore, set up to enforce provisions of the 2004 Competition Act, including promoting and sustaining competitive pricing, could play a major role in such a review.

The second measure concerns the range of choices for consumers. There should be greater efforts to preserve cheaper options. For example, is there a need to redevelop hawker centres, wet markets or older parts of the city if this increases business costs and, therefore, prices?

Finally, households should not wait for the authorities to introduce measures to cushion the effects of inflation. By paying attention to what they buy, consumers can get better value for their money.

The writer is professor of public policy at the Lee Kuan Yew School of Public Policy.