Euler Hermes Economic Research

Country Report

Singapore

Turning point

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Mahamoud Islam
mahamoud.islam@eulerhermes.com

Executive summary

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- Growth lost steam in H1 2014 on the back of lower investment and government expenditures, along with under-performance of external trade. GDP growth is projected to recover progressively in H2, benefitting from the pick-up in global demand.
- Innovation and productivity will be pivotal to ensure future growth as potential economic growth is expected to decrease on the back of an aging population. Public finances will be supportive.
- The monetary policy committee will focus on stabilizing rising inflation pressures, limiting the pass through from wages and imported inflation.

External conditions to determine growth

Singapore is one of the most open economies in the world: it is a regional and global hub for trade and financial services. Although generally positive for growth, this also makes the economy highly vulnerable to external effects such as the slowdown in global trade seen since 2012: real GDP growth decelerated sharply from +6.1% in 2011 to +3.9% in 2013.

GDP growth stabilized in Q1 at 4.9%. External trade continues to be the main driver of growth with exports accelerating. Domestic demand proved resilient, supported by private consumption. Government expenditure decreased and investment recorded its second consecutive quarter of negative growth. Strong acceleration in Q2 is unlikely. Latest export data was weak (-1.5% y/y in May), industrial production and retail sales as well. Moreover, global demand recovery was not as buoyant as desired, with Japan on hold due to sales taxes and China in rebalancing mode.

Going forward, rising global demand coupled with strong domestic fundamentals (sound labor market, rising wages) will support a progressive pick up in H2. EH expects economic activity to grow by +3.7% in 2014 and +4% in 2015.

Table 1: Key economic forecasts

	2012	2013	2014	2015
GDP	2.5	3.9	3.7	4.0
Consumer Spending	3.9	2.6	2.9	3.0
Government Spending	-0.1	9.9	-0.6	2.0
Investment	8.9	-1.9	1.5	3.6
Stocks	*1.2*	*0.7*	*0.6*	*0.0*
Exports	1.5	3.6	4.9	5.0
Imports	3.1	3.1	4.6	4.7
Net Exports	*-2.4*	*1.8*	*1.7*	*1.9*

Sources: Euler Hermes

Innovation and productivity will be key to keeping the pace

Singapore is one of the most innovative countries in the world. With (i) strong expenditure in human capital, (ii) good ranking in competitiveness in business environment surveys and a (iii) solid position in the global value chain, the country is often mentioned as an example of healthy growth. However, this icon is currently facing structural headwinds. Potential growth is dampened by an aging population and tough foreign worker rules, as the latter fosters further slowdown in the labor force. Therefore, in order to enhance future growth, the government announced a range of initiatives, including infrastructure projects and large tax incentives for companies that innovate.

Solid public finances to give some leeway

The public-sector debt stands at a rather high level of just over 100% of GDP, however it is currently not a cause for concern as it has been entirely domestic debt since 1995, and the government has a strong external position such that it enjoys an overall net creditor position. Moreover, if needed, the government is able to tap into the large reserves held by the MAS and into the Government of Singapore Investment Corporation (a sovereign wealth fund). In 2013, the country recorded a budget surplus (budget authorities' definition) of 1% of GDP, higher than initially projected, due to stronger revenues than expected and delayed public expenditures. For 2014, the authorities expect that the budget will fall into a small deficit (-0.3% of GDP) due to the implementation of measures aiming to boost firm's productivity and innovation, in addition to strengthening social safety nets and improving social mobility.

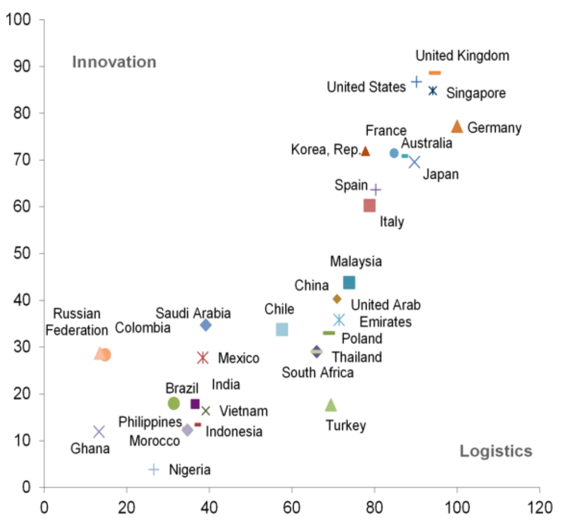
Monetary policy to focus on restraining inflationary pressures

In line with rising MAS Core inflation (+1.9% in April), the monetary authority of Singapore (MAS) decided last April to maintain a gradual and modest appreciation rate of the policy band, tied to a trade weighted exchange rate (NEER policy band). This policy stance should limit rising inflationary pressures stemming from domestic sources (rising wages) and external ones (imported inflation). Therefore, inflation is expected to decelerate to 2.5%. Exchange rates are expected to appreciate gradually, but this won't affect export performance as its structure lays mainly on products with high value added.

Large liquidity to ensure financial stability

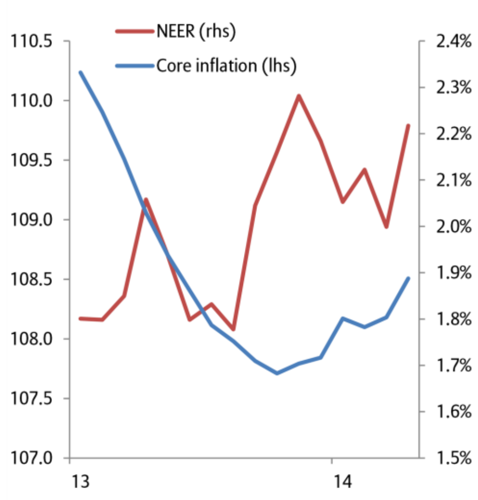
Singapore has over 25 consecutive years of huge current account surpluses, standing at 18.3% of GDP in 2013. The country also enjoys continuous high inflows of FDI (+12.4% of GDP in 2013), while net portfolio investments are negative. This allows the country to continuously increase its reserves, covering 8.8 months of imports in 2013.

Chart 1: Innovation and logistics index



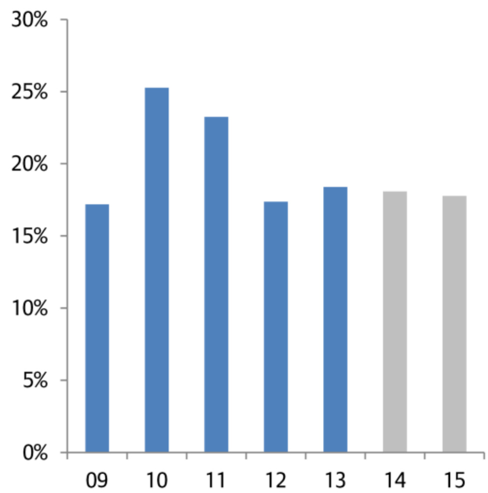
Sources: IHS Global Insight, Euler Hermes

Chart 2: Nominal effective exchange rate and core inflation



Sources: IHS Global Insight, Euler Hermes

Chart 3: Current account (% of GDP)



Sources: IHS Global Insight, Euler Hermes

General Information

GDP	USD274.701bn (World ranking 35, World Bank 2012)
Population	5.31 million (World ranking 115, World Bank 2012)
Form of state	Parliamentary Republic
Head of government	LEE Hsien Loong
Next elections	2016, legislative

Strengths

- Stable political system and effective policymaking
- High income country and Advanced Economy, that serves as a regional and global hub for trade and financial services
- Good track record of sound and flexible economic policies
- Strong external position with a long history of current account surpluses, ample foreign exchange reserves, and low external debt levels
- Very strong business environment
- Solid banking sector

Weaknesses

- Very high export dependency
- Economic growth volatility
- Supply-side driven rapid rise in housing costs

Trade structure

By destination / origin

Exports		Rank		Imports
Malaysia	14%	1	10%	United States
Hong Kong	13%	2	10%	Malaysia
Indonesia	11%	3	9%	China
China	11%	4	9%	Japan
United States	5%	5	8%	Other Gulf

By product

Exports		Rank		Imports
Refined Petroleum Products	30%	1	26%	Refined Petroleum Products
Electronic Components	21%	2	12%	Crude Oil
Computer Equipment	8%	3	10%	Electronic Components
Electrical Apparatus	4%	4	4%	Computer Equipment
Basic Organic Chemicals	4%	5	4%	Telecommunications Equipment

Source: Chelem

Risk Dimensions

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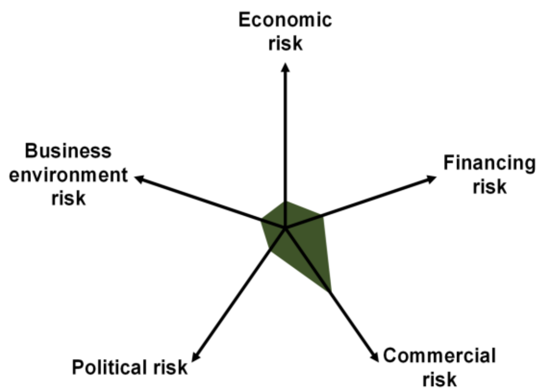

Source: Euler Hermes

Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com