SINGAPORE

TOH MUN-HENG

National University of Singapore

2002: WEAK RECOVERY

After contracting by 2.4 per cent in 2001, the Singapore economy managed to recover to positive growth of 2.2 per cent in 2002. recovery was attributed to improvement in foreign economic environment, but industrial restructuring and re-orientation of business strategies of domestic companies also facilitated the recovery.

Net exports were the main source of demand growth. Domestic exports reversed the decline in 2001 to grow by 0.8 per cent in 2002. Re-exports grew by 4.9 per cent in 2002 with a pick-up in the global electronic industry and increased in demand from major Asian countries, particularly China. Total trade grew by 1.5 per cent in 2002 compared to a 9.4 per cent decline in 2001.

Private consumption expenditure continued to expand, growing by 1.7 per cent in 2002, slower than in 2001 owing to job losses and the perception of an uncertain economic environment abroad. Investment demand also fell by 9.7 per cent in 2002.

Manufacturing was the best performer, recording growth of 8.3 per cent with diversification of the industrial structure from electronics. The output of the chemicals and biomedical clusters accounted for 31.3 per cent of total manufacturing output in 2002, up from 24.2 per cent in 2001. The combined output was just a shade lower than electronics' 32.3 per cent share in 2002, which was down from 38 per cent in 2001.

Positive growth was also recorded for the transportation and communication sector, wholesale and retail trade and business services.

Despite a slight increase in tourist arrivals, the hotel and restaurant sector contracted by almost 3 per cent. This contraction could be due the predominance of weak domestic demand. The financial services sector also recorded a lacklustre performance, contracting by 4.8 per cent amidst declining stockbroking and investment activities and diminished buoyancy in insurance services and purchases.

The Singapore labour market remained soft in 2002 because of the slow recovery in external demand. The unemployment rate increased from 3.3 per cent to 4.5 per cent in 2002, although the number of retrenchments declined. More unemployed people signed up for the Skills Redevelopment Program. Job fairs co-organised by grass-roots communities and business enterprises have become an important institution to help the unemployed secure jobs.

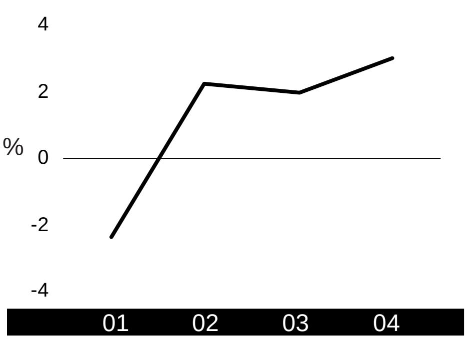
The general price level declined in 2002 but only by 0.4 per cent.

2003–04: EXPANSIONARY POLICY

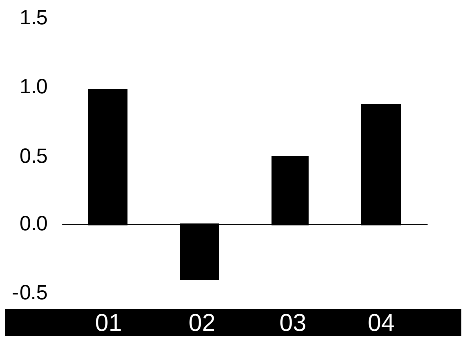
The government will maintain its expansionary fiscal policy stance in 2003. The government budget deficit was S$2.7 billion in 2001 and S$1.4 billion in 2002. These are rare occurrences given the government's long-standing prudent fiscal policy.

The government is committed to bring down both corporate and personal income tax rates to 20 per cent within three years. The increase in Goods and

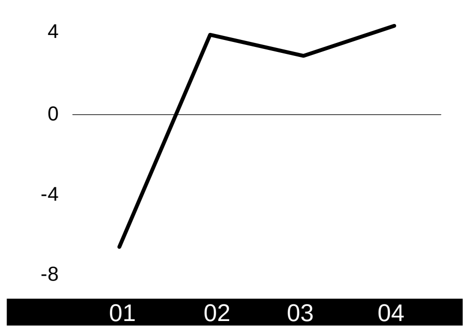
GDP growth



CPI inflation



Export growth



Services Tax from 3 per cent to 4 per cent will occur on 1 January 2003, and a further rise from 4 per cent to 5 per cent will take place in January 2004. The comprehensive GST offset package, comprising the Economic Restructuring Shares (ERS) and rebates on rentals and Service and Conservancy Charges, remains unchanged as announced in Budget 2002 and helps to ensure that most households will be no worse off as a result of the hike in GST for the next five years.

The restoration of the CPF (social security) contribution rate has also been deferred for two years. This is one of the main recommendations submitted by the Economic Review Committee (ERC) in their Final Report on long-term strategies to restructure the economy. The services sector should be expanded by tapping on new, exportable services, like health care, education and creative industries, while promoting growth in established areas like trading, logistics, info-communication technology, financial services and tourism. Fiscal incentives have been designed to expand the scope of the financial sector and to promote research and development (R&D) activities in Singapore (see chart). From 2003, qualifying investment income of foreign investors from funds managed by all fund managers in Singapore will be exempt from tax. As companies were increasingly collaborating in R&D projects with offshore affiliates or outfits of other companies, further tax deductions were introduced for expenses incurred on R&D that would lead to the ownership of intellectual property in Singapore.

Monetary policy will be kept neutral with the nominal effective exchange rate to follow a zero per cent appreciation policy path within a band. During 2002, the Singapore currency appreciated against the US dollar and currencies linked to it, but depreciated against the Euro, the Pound Sterling and the Yen. Depreciation of the Singapore dollar was suggested as a way to boost exports, but the decision was held back because of the island's high dependency on imports. A stable currency also helps maintain price stability and supports Singapore's efforts to become a regional financial hub.

Singapore attracted S$9 billion worth of investment commitments in fixed assets in the manufacturing sector in 2002. Foreign sources accounted for 78 per cent of the total investment commitments. Active promotional efforts were rewarded with success in attracting foreign investment projects in pharmaceuticals, chemicals and biomedical sciences, besides electronics.

Singapore has not relented in its efforts to promote trade through means other than the WTO. It is busily negotiating and fostering bilateral trade agreements with trading partners who have similar interests to Singapore with a view to deepening economic cooperation, assisting home-grown companies to expand internationally, and establishing trading norms that are consistent with WTO but are nonetheless value-adding to the contracting parties.

SARS AND OTHER RISKS

In Singapore, decisive actions were taken after March 2003 to contain the spread of SARS. Schools were closed and people who had come in contact with SARS patients, or were showing symptoms of the disease, were quarantined. Tourist and airline industries have nonetheless been adversely affected by these events. Aviation-related companies have asked their employees to take vacation leave and be prepared for wage cuts and possible retrenchments.

The unemployment rate was 4.5 per cent in the first quarter of 2003, and is likely to rise by another 1 per cent in the next 9 months. The National Wage Council had convened and recommended that employers and workers should opt for pay cuts to save jobs. The government endorsed the NWC's recommendations and has led by cutting the salaries of ministers and top civil servants by 10 per cent.

So far only one multinational company (Motorola) in Singapore has stopped production—in this was only briefly—because of SARS concerns. Further budgetary relief to help the business sector and low income households is likely to be made available if the economic situation deteriorates.

The expansion of the Chinese economy over the last couple of years had helped the recovery and growth of several Southeast Asian economies. The growth of the Chinese economy may be dented in 2003 if the outbreak of SARS is not brought under control.

Terrorism is a further concern after the end of the US–Iraq conflict. This is of no help to the devastated international travel industry.

These factors add to uncertainty, making the forecast subject to a wider margin of error. Taking into account both external influences and domestic efforts made to sustain growth, the Singapore economy is expected to grow at a rate of 2.0 per cent for the year 2003, and at 3.0 per cent for 2004. The inflation rate is expected to remain relatively low at 0.50 per cent for 2003 and 0.9 per cent in 2004.

Internal rates of return on R&D activity, 1990–2001

R&D has contributed greatly to Singapore's industrial development. Gross expenditure on R&D increased from 0.9 per cent of GDP in 1990 to 2.1 per cent in 2001. Life sciences and information and communications technology services recorded the highest and second highest internal rates of return.