

Singapore

Growth remained well above its trend rate for a fourth year in a row, driven largely by a buoyant property market and related construction activity. Inflation accelerated rapidly, reflecting both domestic cost pressures and escalating international prices. A cyclical slowdown is expected in 2008 because of weaker external demand, although domestic demand will be underpinned by the strong property market and a firm labor market. Policies to manage immigration and address an aging population are needed over the longer term.

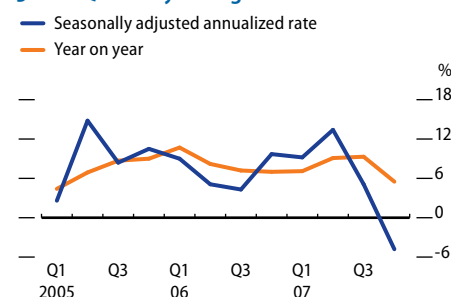
Economic performance

Against the backdrop of a robust Asian economy and a recovery in the domestic property market, GDP expanded by 7.7% in 2007, though momentum eased over the course of the year. GDP fell by 4.8% on a quarter-on-quarter seasonally adjusted annualized basis in the fourth quarter (Figure 3.28.1) owing to sluggish growth in electronics and a decline in pharmaceutical production.

For all of 2007, manufacturing growth slipped to 5.8% from 11.9% in the previous year, mainly due to the weak performance of pharmaceuticals and electronics. The former was affected by the closure of plants for maintenance and to change their product mix, with the result that output of the broader biomedical subsector fell by 0.6%. The latter expanded by a modest 4.0%. Despite strong growth in semiconductors, the production of data storage equipment, consumer electronics, and computer peripherals continued to shrink, reflecting a consolidation of the hard disk industry and relocation of some product manufacturing to lower-cost countries. Still, up by 23.5%, transportation engineering was particularly strong in 2007, boosted by global demand for shipbuilding, ship repairs, and oil-rig building.

After a decade of underperformance, construction emerged as an important growth driver. The property market rebounded as abundant liquidity, the expanding domestic economy, and a large inflow of foreigners boosted demand. An official price index of private residential property surged by 31.0% in the fourth quarter from a year earlier, approaching record levels set in 1996 (Figure 3.28.2). The property market boom spurred construction, which expanded by 20.7%, the fastest pace since 1996. Robust property and construction activity spilled over into financial and business services, as evidenced by strong growth in construction and housing loans. A buoyant stock market and greater volatility in the foreign-exchange market also contributed to the strength of financial services, which grew by 16.9%. Overall, the services sector expanded by 7.8% in 2007 and was the biggest contributor to GDP growth on the supply side.

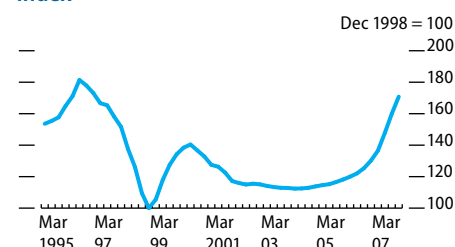
3.28.1 Quarterly GDP growth



Source: Singapore Department of Statistics, available: www.singstat.gov.sg, downloaded 17 March 2008.

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3.28.2 Private residential property price index



Source: CEIC Data Company Ltd., downloaded 17 March 2008.

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In contrast, the export performance was lackluster, despite the generally benign global trade environment. Merchandise exports increased by just 10.1% last year, decelerating from 18.2% in 2006. A sharp decline in electronics exports largely offset gains from rising exports of pharmaceuticals, disk media, and petrochemicals. Although electronics production grew, exports of domestically made electronic products fell by 9.2%, suggesting a fall in export prices and possible inventory buildup. Import growth slowed to 9.5%, in line with the slow export growth as well as moderating investment in machinery and equipment (Figure 3.28.3).

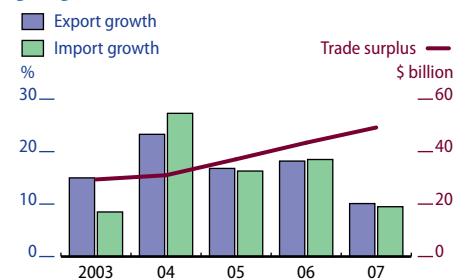
From the view of demand, fixed investment growth accelerated to 20.2% from 13.5% in 2006, largely reflecting a strong rise in construction investment. However, the growth of investment in machinery and equipment lost momentum, partly weighed down by the weak performance of electronics exports. Private consumption rose by 4.4% on the back of continuing strength in the labor market. Overall, domestic demand accounted for 6.7 percentage points of the GDP expansion in 2007, with a contribution of 4.6 percentage points from total investment and 2.1 percentage points from consumption (Figure 3.28.4).

Labor market conditions tightened. Total employment expanded by 9.4% between December 2006 and December 2007, and the unemployment rate fell to a decade low of 2.1%. As a reflection of the tight market, nominal wages rose rapidly, by 6.2%. These wage increases, plus steep hikes in rents and high prices for imported food and oil, fueled inflation pressure. Inflation accelerated from 0.5% in the first quarter to 4.1% in the fourth (Figure 3.28.5). For the year as whole, the consumer price index rose by 2.1%, double the rate of 2006. An increase in the goods and services tax in July also contributed to higher inflation in the second half of 2007.

In the context of sustained economic growth and rising inflation, the Monetary Authority of Singapore maintained its monetary policy of a modest and gradual appreciation of the trade-weighted nominal effective exchange rate, but slightly raised the speed of appreciation from October. Over the year, the Singapore dollar appreciated by 6.4% against the United States (US) dollar. Domestic monetary conditions eased in tandem with US interest rate cuts: the 3-month interbank rate fell by 106 basis points to 2.38% by year-end. The average prime lending rate remained at 5.33% throughout 2007. Domestic credit expanded by 20%, with 42% growth in construction loans and 15% growth in housing loans. In contrast, the weak performance of manufacturing led to a 5.9% contraction in lending there.

Robust economic growth and the buoyant property market also benefited the Government's operating revenues, which rose by 27.0% (excluding capital, investment, and interest income). Government expenditures edged up by 4.9%, resulting in a primary operating fiscal surplus of 3.3% of GDP. In the external accounts, the current account surplus rose to 24.3% of GDP, more than offsetting increased outflows in the financial account driven by local investors' portfolio investment in overseas markets. Consequently, gross international reserves marked a slight gain to US\$163.0 billion by end-2007.

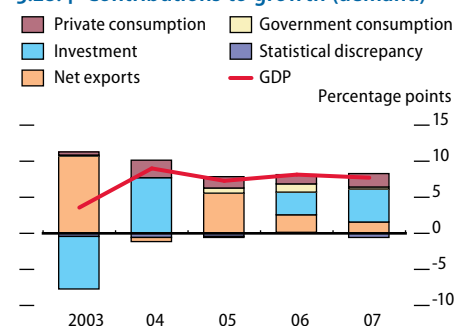
3.28.3 Trade indicators



Source: Singapore Department of Statistics, available: www.singstat.gov.sg, downloaded 17 March 2008.

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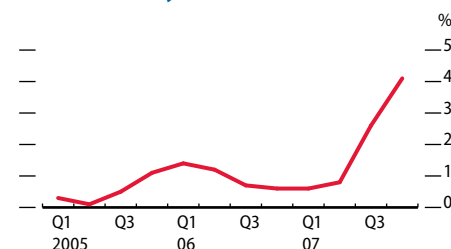
3.28.4 Contributions to growth (demand)



Source: Singapore Department of Statistics, available: www.singstat.gov.sg, downloaded 17 March 2008.

[Click here for figure data](#)

3.28.5 Quarterly inflation



Source: Singapore Department of Statistics, available: www.singstat.gov.sg, downloaded 17 March 2008.

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Economic prospects

Singapore has enjoyed well above-trend economic growth for 4 consecutive years. In 2008, the slowdown in export markets, especially for electronics, and the tight supply of skilled labor will cause the expansion to slow.

Domestic demand that has been driven by the construction boom will help cushion the impact of the slowdown in external demand. Although manufacturing investment is likely to be damped by the weaker export outlook, construction investment will continue to expand at a robust pace in 2008 and 2009. Spurred by strong job creation, large inflows of foreign workers, and low interest rates, underlying demand for property will remain strong. Major projects under construction include two casino-resorts, a large expansion of the financial center, and infrastructure works. Moreover, tight supply of private residential property suggests the pipeline of residential projects will remain large, supporting construction investment well into 2009.

Concerned about intense pressure on construction resources and rapidly rising construction costs (estimated to increase by 20–30% in 2007), the Government has postponed about US\$2.2 billion of public sector projects in the pipeline until at least 2010. In October 2007 the authorities also withdrew a deferred payment scheme to cool the property market. Under this arrangement, a buyer could defer mortgage payments until a property was completed. The impact of these policy changes on construction demand is likely to be modest, though.

Consumer spending is likely to grow steadily, supported by the firm labor market and fiscal transfers to households. Export growth is forecast to moderate to 4.0% in 2008 because of the decelerating global economy, but import growth is likely to pick up, reflecting strong domestic investment demand and rising international commodity prices. Taking these factors into account, GDP growth is forecast to decelerate to 5.2% in 2008, and to move back up to 5.8% in 2009 if global growth revives as expected (Figure 3.28.6). The current account surplus as a ratio to GDP is forecast to stay about 24% in 2008–2009 (Figure 3.28.7).

Fiscal and monetary policies are expected to be generally neutral. The budget for FY2008 (started 1 April 2008) projects a small deficit of 0.3% of GDP, on account of a large increase in special transfers to help mainly low- and middle-income households cope with inflation. In the first half of 2008, inflation is forecast to spurt to about 6% (it was 6.6% year on year in January) because of high global food prices, rising private residential rents, and the tight labor market, before it decelerates to perhaps 4% in the second half as the impact of the increase in the goods and services tax moves out of the picture. That would put year-average inflation at 5.0%. The Monetary Authority is likely to maintain its moderately tight stance, in view of the weaker external outlook and downside risks to growth in 2008.

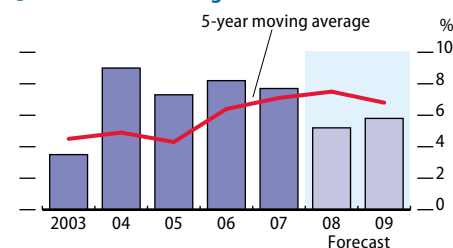
Sector-wise, manufacturing is expected to remain subdued in 2008, largely owing to weak electronics exports. Transport engineering, which is more sensitive to commodity cycles, will likely stay strong, and the volatile biomedical subsector is seen bouncing back from its weak performance in 2007. Construction is forecast to maintain double-digit growth. The softness in manufacturing and exports will have spillover effects on industries with close links to trade, such as transport and

3.28.1 Selected economic indicators

	2008	2009
GDP growth	5.2	5.8
Inflation	5.0	3.3
Current account balance (% of GDP)	23.2	24.0

Source: Staff estimates.

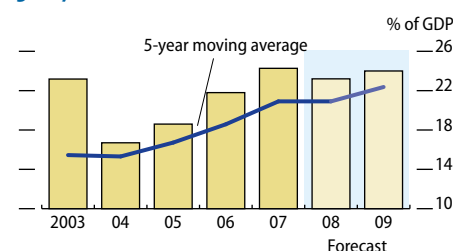
3.28.6 Annual GDP growth



Sources: Asian Development Outlook database; staff estimates.

[Click here for figure data](#)

3.28.7 Current account balance



Sources: Asian Development Outlook database; staff estimates.

[Click here for figure data](#)

storage services. In financial services, generally slower growth in Asia and global financial market turbulence may reduce fund-raising activity, thereby easing growth momentum. However, the foreign exchange market could remain busy and domestic loan growth will be bolstered by property market activity and low interest rates, supporting a still-healthy growth of 8–9% in financial services.

The outlook would be hurt by a more protracted and severe slowdown in the US economy than is currently foreseen. Domestically, rising inflation may prompt the monetary authorities to tighten monetary policy, exerting downward pressures on exports and on the domestic property market. Global economic and financial market turbulence may also erode confidence in the property market, especially at the high end, leading some buyers to hold back on purchases. That would act as a drag on construction and on property-related services.

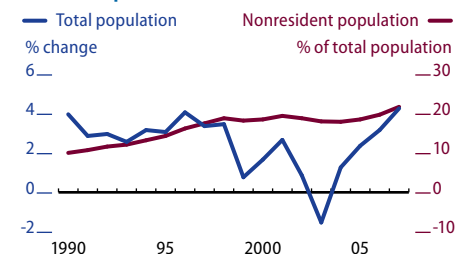
Development challenges

As a city-state of 4.5 million people depending heavily on trade in goods and services, Singapore is highly vulnerable to external shocks. A larger population would enable the country to build domestic demand to help balance fluctuations in external demand. Besides, export-oriented services targeted for expansion such as tourism, entertainment, health care, and education would benefit from a larger domestic market that would help increase scale and thus lower costs. The Government is planning for a substantial increase in population; it has revised its long-term population projection in its planning framework from 5.5 million to 6.5 million.

Given Singapore's low fertility rate, opening the door to immigration is the way to boost the population. Indeed, the number of immigrants has increased rapidly in recent years in response to the tight labor market and an easing of immigration policy (Figure 3.28.8). Yet high rates of immigration can bring social and political strains, especially during economic downturns or if the benefits of economic growth are not felt by the local population. Managing immigration so that it does not cause such strains, leading to demands for a more restrictive immigration policy and subsequent slowdown in population growth, will require careful planning and execution.

The influx of relatively young immigrants is slowing the speed of the aging of the population, but it has not reversed the aging trend. The proportion of residents aged 65 and above is likely to double to about 17% by 2020 from 8.5% in 2007. The Government has instituted some changes in pensions and housing policies to tackle this. Still, any comprehensive, long-term approach requires reforms in pensions, health, employment, and education.

3.28.8 Population indicators



Note: Total population comprises Singapore residents and nonresidents. Nonresident population comprises those who are not Singapore citizens or permanent residents.

Source: Singapore Department of Statistics, available: www.singstat.gov.sg, downloaded 17 March 2008.

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