Singapore

Growth will gradually accelerate over the next 2 years, with inflation moderating but still higher than average in the past decade and the balance of payments recording large but narrowing surpluses. Prudent economic policies, a flexible labor market, a sound banking system, and substantial foreign exchange reserves will counterbalance adverse developments overseas. As the government implements its growth strategy encouraging firms away from reliance on foreign labor, it should take measures to reduce the impact on small and medium-sized enterprises.

Economic performance

The economy expanded by 1.3% in 2012, down from 5.2% in 2011 in line with continuing challenges in the global economy. Demand slowed dramatically for externally dependent sectors, particularly manufacturing and wholesale and retail trade (Figure 3.29.1). Manufacturing growth was flat as electronics output dipped, owing to weaker demand for non-mobile technologies.

Domestically oriented sectors—construction and business services, in particular—were the main engines of growth in 2012, accounting for half of GDP growth. Construction expanded by 8.2%, supported by robust public and private demand. Sales of private houses jumped 40%, boosted by low interest rates. Strong growth in the business services sector depended heavily on the buoyant real estate market.

Domestic demand remained resilient, mainly due to inventory accumulation, while external demand weakened (Figure 3.29.2). However, consumption growth slowed to 2.2% from 4.6% in 2011 as spending on recreation and culture contracted and public consumption expenditure shrank by 3.6%. Weaker export growth and relatively faster import growth together narrowed net exports by 16.4%.

The economic slowdown took place amid ongoing economic restructuring. The government has adopted the recommendations of the Economic Strategies Committee that emphasize skills, innovation, and productivity as the main sources of growth. It limited the inflow of foreign workers by increasing the levies on nonresident foreign employees and lowering the ceiling on their allowed share in companies’ total workforce. It initiated programs to encourage firms to raise their productivity by increasing the capital–labor ratio and through efficient workflow, rather than by relying on cheap labor. Coupled with low unemployment, these initiatives further tightened the labor market and put upward pressure on wages and inflation. As productivity gains will not happen overnight, slower expansion of the labor force will likely restrain growth.
Inflation remained elevated but moderated somewhat to 4.6% in 2012 from 5.2% in 2011. The largest contributors to inflation in 2012 were housing and transportation, the latter driven by rising prices for vehicle quota premiums (Figure 3.29.3). Food price hikes eased as world prices declined and the Singapore dollar appreciated. Core inflation, which excludes the costs of housing and private road transport, averaged 2.6% in 2012, up from 2.2% in 2011.

Given Singapore’s open capital account and its use of an undisclosed exchange rate band to execute monetary policy, interest rate and money supply developments are largely outside the control of the Monetary Authority of Singapore. To contain inflationary pressures, the authority has maintained a tightening bias since April 2010, leading to an appreciation of the nominal effective exchange rate by 5.9% in 2012, compared with 0.2% in 2011 (Figure 3.29.4). Money supply growth moderated to 7.2% from 10% the previous year as economic activity slowed. Credit expansion decelerated, with credit to the private sector expanding by 17% in 2012, down from 30% in 2011. Interest rates remain lower than those in the US (Figure 3.29.5).

Fiscal and macroprudential measures were tightened in 2012 to complement the central bank’s contractionary stance and discourage speculation in the property market. Stamp duty tax on property purchases were raised from 10% to 15% for foreigners, and introduced at 5% for permanent residents; the loan-to-value ratio for mortgages was lowered from 60% to 50% for a second property.

The government’s fiscal position remained strong in FY2012 (ended 31 March 2013) with revenue performing well and the overall fiscal surplus reaching 1.1% of GDP, almost the same size as in FY2011. Stamp duty collections were buoyed by the strong property market, and receipts from vehicle quota premiums swelled in response to government-imposed supply restrictions (Figure 3.29.6). Development expenditures expanded by 6%, reflecting higher spending on health, education, and transportation. Current expenditure contracted slightly, though the FY2012 budget introduced income support for households and financing facilitation for firms to ease the burden from economic restructuring.

Over the years, the economy has maintained a strong trade balance, with the current account surplus averaging more than 20% of GDP. In 2012, however, the current account surplus eased to 19% of GDP from 23% in 2011 as the surplus declined for both the trade balance and the services account. Overall, the balance of payments posted a surplus of 9% of GDP, up from 6% in 2011, largely due to a narrower deficit in the capital and financial account. Singapore maintains a strong external position, with international reserves covering 8 months of merchandise imports.

**Economic prospects**

GDP is forecast to grow by 2.6% in 2013, near the upper bound of the government’s estimate of 1%–3%, and by 3.7% in 2014. For the rest of the decade, the Ministry of Trade and Industry projects GDP growth to be 3%–4%, which is a marked slowdown from the 6% average growth from 2000 to 2010.
Domestic-oriented sectors will again be the primary drivers of growth this year and the next. Major infrastructure projects and residential construction will generate positive spillovers for other sectors. Cyclically sensitive industries such as manufacturing, wholesale trade, and financial services are expected to post modest growth, reflecting gradual recovery in external demand. Domestic demand will continue to be the main source of growth, on the back of improving fixed investment and a rebound in government expenditure.

Inflation will moderate further but remain above the historical average, owing to tight labor and housing markets (Figure 3.29.7). Overall inflation will likely slow gradually to 3.8% in 2013, within the range of the Monetary Authority of Singapore forecast of 3.5%–4.5% but double the 2% average over the past 2 decades. It is expected to ease to 3.0% in 2014. The forecast assumes that monetary policy will retain its bias toward Singapore dollar appreciation, that measures will be taken to cool the property market and expand housing supply, and that global commodity prices will moderate. Excessive capital inflows may also be a risk for inflation, but the authorities will likely introduce additional macroprudential measures, if necessary.

Singapore has a tradition of fiscal prudence with budget surpluses, except during recessions. Fiscal rules do not allow a cumulative deficit over the term of any one government. The budget for FY2013 estimates another overall fiscal surplus of S$2.4 billion, or 0.7% of GDP and lower than what was recorded in FY2012 (Figure 3.29.8). Authorities expect a slight decline in revenues, as receipts related to transport and the property market fall in the next 2 years. Expenditures are likely to be higher owing to increased outlays for higher education and health.

A slower pace of export growth and a relatively faster rise in imports—as domestic demand expands with government social spending—will likely narrow the current account surplus over the coming years. It is forecast at 16% of GDP in 2013 and 15% in 2014, down from 19% in 2012 (Figure 3.29.9).

The high degree of uncertainty over the global economy poses the highest risk to growth. As a trade-dependent city-state, Singapore will remain at risk from the patchy developments in the US, protracted sovereign-debt crisis in Europe, and moderation in economic growth in the People’s Republic of China. A steep and abrupt correction in property values could cause substantial bank losses, as housing loans account for 31% of total loans. However, Singapore’s strong fiscal position, flexible labor market, well-capitalized banking system, and substantial foreign exchange reserves can provide a buffer if any of these risks materialize.

Policy challenge—supporting small and medium-sized enterprises

Small and medium-sized enterprises (SMEs)—businesses with annual sales of up to S$100 million or up to 200 employees—are an integral part of the Singapore economy. SMEs account for 99% of all enterprises, more than 50% of output, and 70% of employment. Recent years have been particularly challenging for SMEs in Singapore. In addition to weak...
demand in the protracted global recession, SMEs face a labor supply squeeze and rising domestic costs, which are largely induced by the government’s economic restructuring policy. SMEs feel the consequences of these shocks more strongly because of their limited access to finance and their less-developed financial and management capabilities. Recent surveys indicate that profits margins have narrowed, the number of SMEs reporting losses has risen, and enterprises are less optimistic regarding sales, profits, hiring, and capital investment in the coming months.

Recognizing SMEs’ predicament, the FY2013 budget introduces a 3-year package worth S$5.35 billion to help businesses cope with rising costs (Table 3.29.2). It provides incentives for firms to invest in raising productivity and pay correspondingly competitive wages. Other programs specifically for SMEs are being implemented by a government agency facilitating the development and growth of indigenous firms. While these incentives will not fully offset costs in the short run, they provide a buffer for firms adjusting to the economic restructuring program.

The recent economic situation in Singapore, though not as severe as during the 2008–2009 global financial crisis, calls for more attention to the complex challenges that SMEs face. In the short term, SMEs must be willing to trim their margins and pay more for labor while building new business models. The measures announced in FY2013 will be helpful, but more needs to be done. Going forward, the government’s policy of pushing firms toward less reliance on foreign labor, capital deepening, knowledge and systems upgrades, and innovation could be taxing for SMEs. Any shrinkage of the sector would have important unemployment and inequality consequences.

The challenge is to get the right balance such that restructuring toward higher productivity and sustainable growth does not happen at a very high social cost, while ensuring that policies do not encourage long-term dependency. This objective warrants well-targeted and incentive-compatible transfers to the most vulnerable firms, especially microenterprises. Rigorous evaluations of government support are necessary to assess actual impact on SMEs as a guide to policy makers. With a comfortable fiscal cushion, the government is well positioned, despite the sluggish global economy, to push for reforms toward a more sustainable and inclusive growth path that takes SMEs’ requirements into account.

### 3.29.2 Selected budget 2013 measures for SMEs

<table>
<thead>
<tr>
<th>Programs</th>
<th>Details</th>
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<tbody>
<tr>
<td>Wage credit scheme</td>
<td>The government co-funding 40% of the wage increase for a Singaporean employee with a gross monthly salary of up to S$4,000</td>
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<tr>
<td>Productivity and innovation credit bonus</td>
<td>A business spending at least S$5,000 on a credit-qualified activity receiving a matching bonus up to S$15,000</td>
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<tr>
<td>Corporate income tax rebate</td>
<td>Each year, 30% of corporate income tax refunded, subject to a cap of S$30,000 per company</td>
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<tr>
<td>Helping SMEs upgrade productivity, innovation, and capability</td>
<td>Enhanced productivity and innovation credit scheme, Collaborative industry projects, Technology adoption program, Land productivity grant, SME talent program, Workforce and training support</td>
</tr>
<tr>
<td>Helping SMEs tap opportunities for growth and others</td>
<td>Market readiness assistance grant, Enhanced partnerships for capability transformation, Support to enhance companies’ access to financing, Increase in central provident fund and lower contribution rates for low-wage workers, Lower tax on household benefits, Road tax rebate</td>
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SMEs = small and medium-sized enterprises. 
Source: Standards, Productivity, and Innovation Board of Singapore.