# SINGAPORE FOCUS

## Singapore Economy: Deceleration Ahead

| UOB Economic Projections | 2009 | 2010 | 2011F | 2012F |
|---|---|---|---|---|
| GDP | -0.8 | 14.5 | 4.8 | 2.5 |
| CPI (average, y/y %) | 0.6 | 2.8 | 5.1 | 3.2 |
| Unemployment rate (%) | 2.3 | 2.2 | 2.1 | 2.4 |
| Current account (% of GDP) | 19.0 | 22.2 | 19.0 | 16.2 |

- *For the year ahead, the 3M SGD SIBOR looks likely to continue to hold steady at around a rate of 0.4% for an extended period of time, into 2013, mirroring the low Fed funds rate.*
- *Eurozone's debt crisis will continue to persist with no clear solution in place and this will weigh on the SGD. We expect more downside for the SGD in 1Q12, moving to 1.33 from our 4Q11 projection of 1.29. The rest of the year should see some slight strength in the SGD against the USD, as the situation improves albeit slightly, and the USD/SGD to end 2012 at 1.27.*
- *We expect 4Q GDP to contract, at -5.5% q/q saar and 3.5% y/y, following 3Q GDP growth at +1.9% q/q saar, 6.1% y/y. Our 4.8% GDP forecast for 2011 still stands, and 2012 looks likely to grow 2.5%.*
- *Given the much lower domestic GDP outlook for 2012- which we are projecting to grow at 2.5%, the uncertainties in the external environment, as well as moderating inflation, MAS could ease monetary policy from its current "gradual appreciation" slope to a flat, 0% appreciation stance.*

The uncertainty and slowdown in the external environment is taking a toll on the Singapore economy. The question now is whether it would be another financial shock, or a macro economic slowdown. While global policy makers are trying to avert another Lehman crisis, the world is unlikely to be spared from an economic slowdown, as the West undergoes fiscal austerity measures. In Singapore, some of the high-frequency data such as NODX and manufacturing numbers have reflected the macroeconomic slowdown and the government is now projecting growth of 1.0-3.0% for 2012. Downside risk stemming from the European situation could drag the domestic economy further down. As for the local currency, renewed global risk aversion has led to the unwinding of USD/SGD, resulting in the currency pair appreciating to above 1.30 from 1.2009 in late Jul. Going into 2012, our take is that USD/SGD will remain choppy, depending on how the European situation pans out. We expect the SGD to remain weak in 1H-2012, hovering at around 1.33 against the USD, with risk of the pair heading up to 1.35, if the external situation deteriorates, and then strengthening just slightly to 1.27 towards the end of 2012.

### 3M SGD SIBOR To Stay Flat

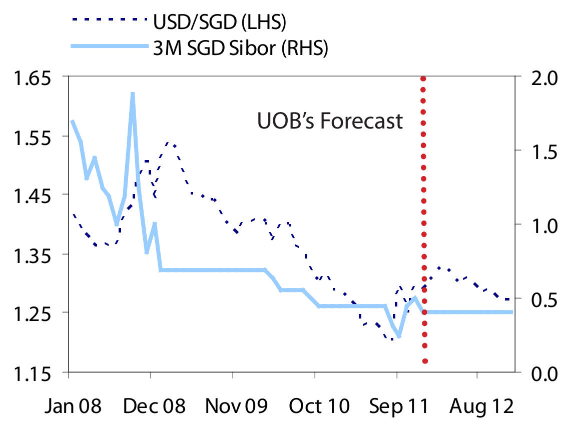
Even though the Swap Offer Rate (SOR) has continued to move up in line with the firmer USD/SGD, with the 3M SOR moving to 0.56 in mid-Dec from a low of -0.19 in early Sep, the SGD SIBOR has stayed relatively steadier, moving up slightly to 0.4 in mid Dec from 0.34 in early Sep. For the year ahead, the 3M SGD SIBOR looks likely to continue to hold steady at around a rate of 0.4% for an extended period of time, into 2013, mirroring the low Fed funds rate. The direction of the SIBOR historically moves in tandem with the US fed funds rate. MAS' current policy of modest and gradual appreciation which sets SGD on a strengthening path should also continue to draw liquidity and keep the interest rate low. However, the risk of SIBOR rising has increased due to greater expectation that the MAS could ease the slope of the SGD NEER policy band further to one of 0% appreciation. The SOR, which is more sensitive to FX market movements could continue to climb higher from its current levels, given the expectation that SGD could continue to weaken from hereon, as well as the MAS possibly loosening monetary policy further.

### USD/SGD

The as yet-unresolved crisis in the Eurozone and risk aversion has shown up in the weakness in Asian currencies and the SGD. Having been on a weakening bias since Sep, we think there is further downside for the local currency going into the 1Q of 2012. Eurozone's debt crisis will continue to persist with no clear solution in place and this will weigh on the SGD. We expect more downside for the SGD in 1Q12, moving to 1.33 from our 4Q11 projection of 1.29.

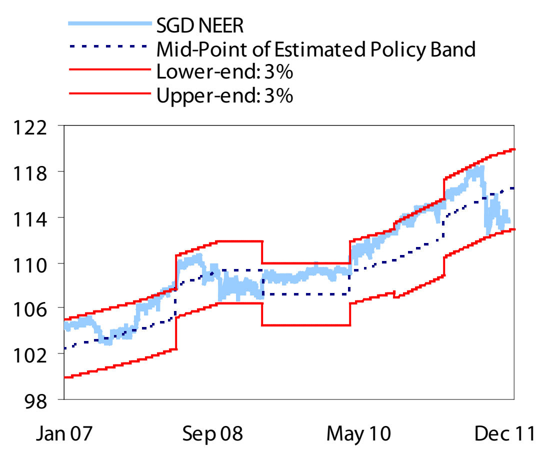
The local currency is also not helped by the domestic economy, which will see moderation in growth to 2.5%, and increases the odds of MAS shifting the policy stance to a 0% appreciation stance in Apr 2012, signaling no strengthening of the SGD NEER. The rest of the year should see some slight strength in the SGD against the USD, as the situation improves albeit slightly, and the USD/SGD to end 2012 at 1.27.

3M SGD SIBOR To Stay Low In 2012




*Source: CEIC, UOB Economic-Treasury Research Estimates*

SGD NEER Staying Firmly At The Bottom Of The Band




*Source: UOB Economic-Treasury Research Estimates*

## GDP Growth Expected To Slow In 2012

Exports have been slow, which will have an impact on the manufacturing sector. Although the latest NODX data surprised on the upside, we think a convincing turnaround is not yet here. Already, the debt crisis in Europe was biting into the growth of export-driven economies, but this was compounded by the severe flooding in Thailand which disrupted supply chains of electronics and automobiles. Our analysis shows that a 1% drop in EU GDP will decrease Singapore's NODX by 2.6%.

Nov NODX expanded 1.6% y/y, 5.9% m/m s/adj, and electronic exports finally grew, albeit marginally, at 0.1% y/y, after 9 consecutive months of decline, while shipments of non-electronics also saw an improvement of 2.4% y/y from a revised -6.9% in Oct. Leading indicators continue to paint a mixed picture of the electronics sector. The US Semi book to bill ratio climbed to 0.83 in Nov compared to 0.74 in Oct, indicating more orders received. But domestic PMI data for Nov had indicated that the electronic sector would still be weak, with the reading dropping to 50.9 in Nov from 52.1 in Oct.

Generally Nov's data came in better than expected, with electronic exports expanding slightly and NODX to key markets not contracting as sharply. Looking ahead too, the first few months of next year could see more positive NODX numbers due to the low base. But we don't think Nov's numbers signals a rebound in NODX, given that external demand for Singapore's exports still remain weak amid stalled US recovery and Eurozone debt problems. Next year will be a year of slow growth for Singapore, given external uncertainties and slower demand.

Manufacturing output for Oct also surged a surprising 24.4% y/y and 14.2% m/m s/adj, with the upside coming from pharmaceutical manufacturing. Excluding biomed output, industrial production would have contracted 11.2% y/y. However, the strength in the pharmaceutical output –which tends to be volatile, masks the weakness in other manufacturing segments.

The last quarter of this year is expected and the whole of next year looks likely to be one of anemic growth. We expect 4Q GDP to contract, at -5.5% q/q saar and 3.5% y/y, following 3Q GDP growth at 6.1% y/y, +1.9% q/q saar. Our 4.8% GDP forecast for 2011 still stands, and 2012 looks likely to grow 2.5%. The manufacturing and services sector are not likely to prove supportive for the economy, given the subdued external demand for Singapore's exports amid global uncertainties, and trade-related services being hit. Sectors which could bear the brunt of the impact include manufacturing, wholesale and retail, transport, financial and business services. Nonetheless, some support will come from the biomedical and tourism-related sectors. The unemployment rate is expected to rise in tandem with the slower economy but should be mitigated by the government measures to tighten inflow of foreign labour. This will mean the domestic labour market should still remain fairly tight and we expect the unemployment rate to climb higher to 2.4% by end 2012.

## Fiscal Responses By The Government

The government already seems to be preparing for the slowdown ahead, subsidising 90% of the training costs for workers in the manufacturing sector-particularly the electronics and electrical industries, in order to stave off retrenchments. Reduced growth stemming from the slower inflow of foreign labour looks likely, with businesses stating that they face constraints on expansion due to labour shortages.

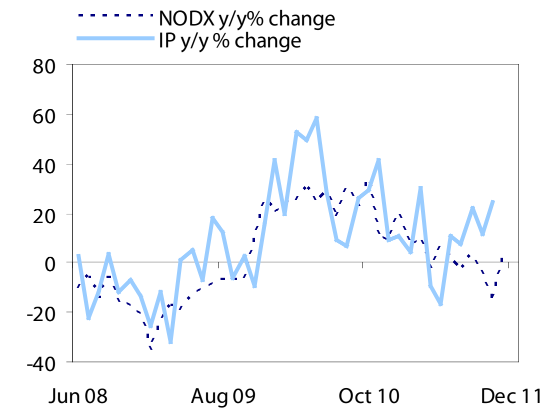
Measures to restrict foreign labour include increasing the salary ceiling for employment passes as well as raising educational qualifications, increasing levy rates for foreign workers. The government also recently scrapped the Employment Pass Eligibility Certificate (EPEC) scheme which allowed foreign graduates to apply for Long-Term Visit Pass (LTVP) for up to one year for their job search. Foreign graduates now get a normal Visit Pass valid for three months only. All these tightening measures are expected to slow the growth of foreigners and PRs, and with the measures these are expected to contribute to a moderation in growth.

Amidst low global interest rates and the risk of further influx of foreign capital, the government has enacted measures to curb the rise of property prices in early Dec. By imposing an additional stamp duty of 10% on foreigners buying residential property, the latest measures are expected to see appetite for properties as investment significantly curbed, especially from non-Singaporean buyers. With foreigners accounting for much of the high-end market, this segment will bear the brunt of the latest rules, rather than the mass market.

## Inflation Remains Elevated, But Should Moderate Slightly On Slowdown In Economy

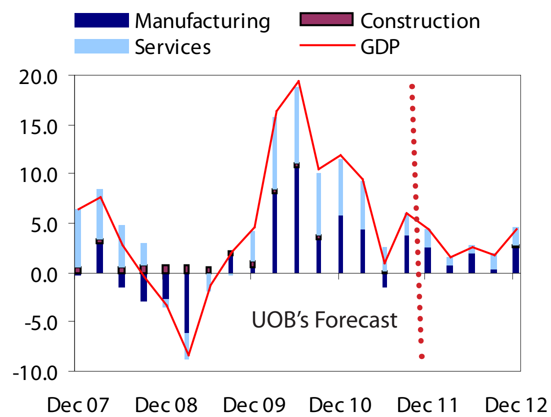
Inflation continues to be strong, but is expected to moderate going into 2012, as slowing growth takes hold. Going into next year, high COE prices will contribute to headline inflation, with the vehicle population growth being lowered, while public transport costs are also going up, on higher taxi fares. But there could be some easing in demand-side

NODX Showed Surprise Rise In Nov, But No Convincing Turnaround Yet



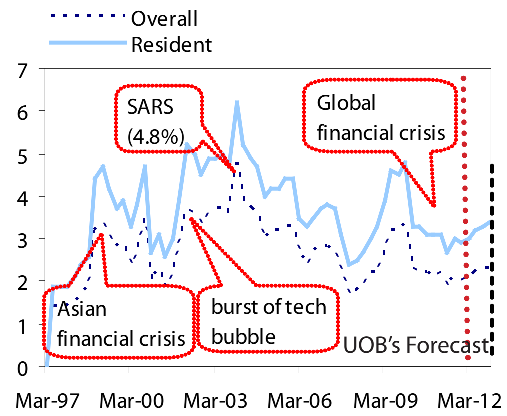

*Source: CEIC*

Growth To Slow To 2.5% In 2012



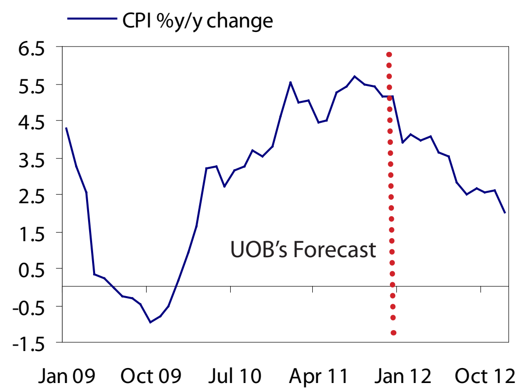

*Source: CEIC, UOB Economic-Treasury Research Estimate*

Unemployment Rate To Climb In 2012




*Source: CEIC, UOB Economic-Treasury Research Estimate*

CPI To Moderate On Slowdown In Economy




*Source: CEIC, UOB Economic-Treasury Research Estimate* inflation amid the slowdown in economic growth, which will impact on the tightness of the domestic labour market. This should see CPI inflation heading down next year. We're projecting inflation to come down to 3.2% for 2012. In Oct, CPI was hovering above 5% y/y, with elevated housing and transport costs continuing to keep inflation high, while food prices also edged up. Core inflation which excludes accommodation and private road transport also headed higher, to 2.3% y/y from 2.1% y/y in Sep. Headline inflation looks likely to moderate from the high of 5.7% in Aug, and should hover around the 5% range for the remainder of the year. Higher accommodation and COE prices as well as costlier food prices due to the Thai floods, could also add to inflationary pressure. But some mitigating factors come in the form of a decrease in electricity tariffs and government rebates on rental and conservancy charges at the end of the year. For 2011, we have pegged CPI inflation at 5.1%, given the still elevated levels of imputed rentals of owner-occupied accommodation and COE prices.

| Singapore Quarterly GDP Moderation Trend | | | | | |
|---|---|---|---|---|---|
| y/y% change | 1Q12F | 2Q12F | 3Q12F | 4Q12F | 2012F |
| Singapore | 1.6 | 2.5 | 1.8 | 4.4 | 2.5 |
| *Source: UOB Economic-Treasury Research Estimates* | | | | | |

## Impact On Monetary Policy

MAS has already started loosening its policy stance in Oct, easing the slope of the monetary policy band to a gradual and modest appreciation, which we have estimated at around 1.5-2.0%, from the slightly steeper angle which we projected at 3.5%. Given the much lower domestic GDP outlook for 2012, which we are projecting to grow at 2.5%, the uncertainties in the external environment, as well as moderating inflation, MAS could ease monetary policy from its current "gradual appreciation" slope to a flat, 0% appreciation stance. As of writing, our model shows the trade-weighted index is currently around 2.3% below the midpoint.