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SINGAPORE AND THE GLOBAL RECESSION

Abstract: The author looks at problems and decisions faced by Singapore in the light of the global recession which had its roots in the financial crisis of 2007. He analyses the deteriorating situation Singapore's economy found itself in at the time as the level of international trade decreased together with the global demand. He discusses the factors which caused this to be the harshest economic shock Singapore has experienced in over 20 years and explains why this had such a devastating effect on all sectors of the economy. The author also looks at micro- and macroeconomic policies used by the Singaporean Government to try to fight back the forces impeding growth and tries to comment to what degree these were successful.

Keywords: Singapore, global recession, FDI, competitiveness, growth.

1. Introduction

The aim of this paper is to examine how the economy of Singapore was affected by the turbulent changes in the world's business cycle which hit the downturn at the end of 2008. Singapore economy, probably the most open in the world in terms of trade and financial flows, as well as the biggest trade hub in South East Asia serves as a good indicator of the "wellbeing" of Asian and world trade flows and hence their economic condition. Three key questions will be reviewed: how did the financial crisis influence the growth of Singapore's economy, what were its consequences and how did it shape Singapore's macroeconomic policies.

This essay is made of five parts: introduction, three main sections, conclusion and bibliography. The second section will give a short historic overview of Singapore's economic development and how, over the decades, it responded to the global business trends. This section will, also, illustrate the character of the global crisis that began in late 2008. Third part will analyse Singapore's GDP, foreign trade, individual economic sectors and the nature of Singapore's domestic consumption and investment. Fourth section will discuss the macroeconomic factors which cause Singapore's economy to be prone or immune to the outside economic shocks. It will also discuss the effectiveness of government's policies taken in the light of changing economic conditions. The conclusion will try to foresee what the year 2010 and the next will be like for Singapore and what steps might possibly be taken by the city-state to cushion any future effects of negative fluctuations in the global business cycle.

2. Singapore's development – recession in historical context

Ever since gaining its autonomy in 1960 Singapore has been seen by many as a perfect case study of a free market, open economy. Bold and well-suited economic policies placed the country on a rapid growth path. The most admired aspect of this long-term growth is its enduring continuity.

In its 50-year history Singapore experienced negative economic growth only 5 times. Thanks to that almost uninterrupted, steady growth it has turned from a less economically developed country to a country with a *per capita* income close to that of Western Europe.[1]

Despite its good economic record and rigorous adherence to pro-growth, macroeconomic policies Singapore has been faced, for the fifth time, with economic challenges halting its growth. An economic slow down is not an unusual phenomenon in itself. Both the economic theory and practical experience show that after a period of growth comes a decline in general business activity. But the case of Singapore is not a typical one.

Firstly, during its 38 years after gaining sovereignty, Singapore had only 2 short lasting recessions. In the following 11 years, however, it suffered 3 of them.[2]

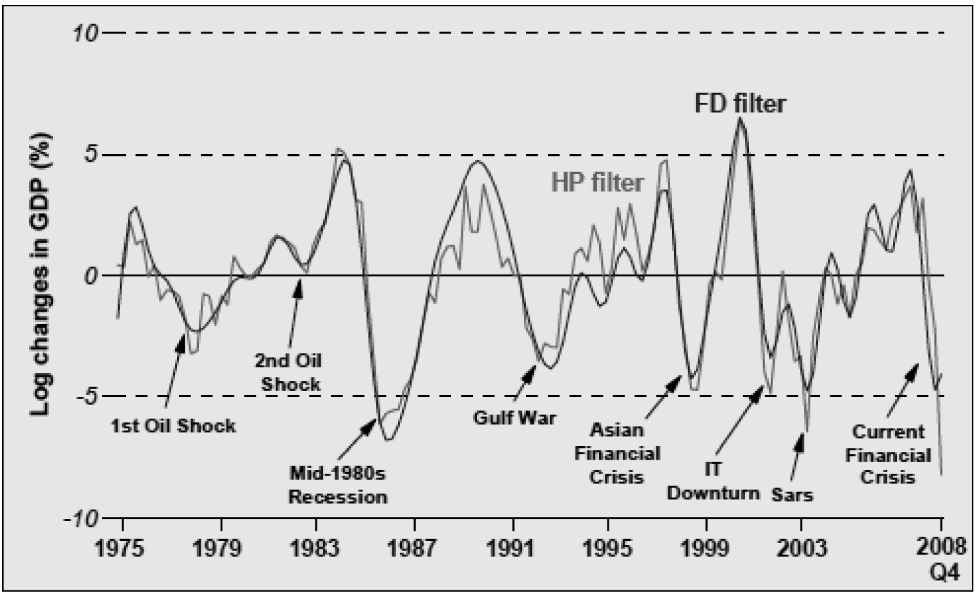

Figure 1. Singapore business cycle

Source: Special Feature A – Sectoral, Industry and Employment Business Cycles in Singapore, *Macroeconomic Review*, Monetary Authority of Singapore, April 2009.

[1] World Data Bank database, World Bank.
[2] Singapore Department of Statistics, *National Accounts*.

Figure 1 illustrates Singapore's business cycle starting from mid 1970s up to 2008.[3] It does show more than 5 downturns and their causes, however, only the five mentioned resulted in negative GDP growth over two or more quarters. The others did cause a deceleration of growth but never resulted in a recession. For example, in 2003 during the outbreak of SARS in Asia, Singapore's annual growth reached 3.8% with inflation 0.5%. The result many countries would be happy with even in times of up-turn in their business cycles.

Secondly, apart from the first (recession in 1964, not shown on the graph), all recessions resulted directly from outside economic shocks. The recession of 1985 was caused by the world's oil crisis. The recession of 1998 came as a result of the Asian financial crisis. In 2001 the downturn happened after the burst of the internet bubble. These three recessions were of relatively small scale comparing to the economic difficulties the country has been faced with since the end of 2007.

Singapore's third recession in just over a decade was caused by the global economic slump. The global slump had its beginnings in the boom-bust-cycle in the United States subprime mortgage market – a relatively small part of the US financial sector. Due to its severity, however, it spread throughout the whole of US financial sector, quickly spilling over to the financial sector of the United Kingdom and then onwards affecting the global financial sector and causing its crisis. The magnitude of this was so severe that global financial crisis caused a full blown economic crisis which effects are felt to this day.

3. Singaporean economy during global economic crisis

The events of 2008 and 2009 leading to the global recession hit Singapore and its exceptionally open economy particularly hard.

GDP growth was just 1.4% in 2008, which meant a virtual stagnation in comparison to the period 2003-2007 during which the average annual growth was 7.3%. GDP reached its lowest level since 2001 when it was in negative figures following the impact of the global internet bubble burst. Displaying close relationship between the global business cycle and Singaporean economy, the GDP growth in 2008 slowed and reached –4.2% at the end of the year over 10 percentage points lower than at the beginning of the period when it was 6.7% (Figure 2).[4] In October 2008 Singapore became the first in Asia to declare a recession.

The beginning of 2009 saw a continuation of downward trend with economy sliding deeper into recession and GDP growth in the first quarter of –9.4%. Second quarter saw the recession to decelerate and GDP growth being –3.1%. Between the second quarter and the third quarter Singapore appeared to reach the through of the

[3] Different values shown as given by frequency domain (FD) filter and Hodrick-Prescott (HP) filter an discrepancy between them are of no consequences in this essay as the graph serves only to illustrate a general trend in Singapore's growth.

[4] *Asian Development Outlook 2009*, Asian Development Bank, March 2009.

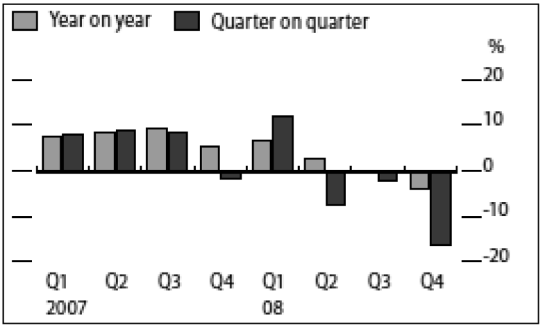

Figure 2. GDP growth

Source: *Asian Development Outlook 2009*, Asian Development Bank, Singapore Department of Statistics, March 2009.

economic cycle. GDP growth for the third quarter was positive and reached 0.6%. The end of 2009 saw the economy strengthening further with GDP reaching 4%. Over 8% higher than the year earlier. Most recent data show that overall Singapore economy contracted by 2% in 2009 with the value of gross domestic product of S$231.8 billion compared to S$236.6 billion in 2008.[5]

A big decrease in the value of Singapore's exports caused the growth of GDP to decelerate rapidly leaving it supported only by domestic consumption and investment of which the construction sector played the biggest role. Global slowdown was mostly felt in the international trade levels which fell by almost 12% in monetary term (US dollars) or almost 6% in volume terms by the end of 2008. Since Singapore is, and historically always was, the main trade centre in Asia, not only for the actual trade but also for all trade supporting services, contraction of international trade had very serious implication for the country.[6]

Another reason why Singapore suffered more than other countries is due to the character of its economy and its exports. As it was developing, Singapore's economy, and hence its exports, moved away from low-skill, low-value production, such as footwear, to high-skill, high-technology and high-value added production in manufacturing and information and communication sectors. This evolution helped to diversify the economy and allowed further growth but at the same time made Singapore more dependent on a smaller number of specific trade partners with the main ones being the United States and Western Europe, the countries at the centre of the global crisis.

End of 2007 is universally understood as the beginning of world economic slump but, overall, Singapore's exports suffered more in the first quarter of that year than in the fourth.

[5] Ministry of Trade and Industry, Press Release, 19 February 2010.

[6] *Ibid*.

Singapore's external trade rose by a slower pace of 4.5% in 2007 as compared to the 13% growth in 2006. Total trade increased to US$ 847 billion from S$ 810 billion in the previous year. The continued rise in external trade resulted in 4.4% growth in exports and 4.5% in imports. The expansion of Singapore's total trade in 2007 was due to increases in both oil and non-oil trade. Oil trade expansion was boosted primarily by the sharp rise in oil prices in the fourth quarter.

Non-oil domestic exports (NODX) grew by a slower 2.3% in 2007 compared to 8.5% growth in 2006 as higher non-electronic exports were offset by a contraction in electronic exports. Exports to all the top 10 markets, except for Taiwan, Indonesia, Hong Kong, the EU-27 and Japan, expanded in 2007. The three markets making the highest contributions to export growth were South Korea, the US and Malaysia.[7]

In 2008 Singapore's external trade rose by a faster pace of 9.6% as compared to the 4.5% growth in 2007. The level of total trade increased to a record high of US$928 billion from S$847 billion in the previous year. Expansion in external trade was attributed to a 5.8% rise in exports and 14% rise in imports.

The expansion in external trade was due to higher oil trade, which grew by 50%. This expansion was boosted primarily by the record high oil prices for the first three quarters of 2008. Non-oil domestic exports declined by 7.9% in 2008 compared to the 2.3% growth in 2007 due to lower electronic and non-electronic exports NODX to all the top 10 markets, except for Indonesia and Hong Kong, contracted in 2008. The three markets which made the highest contributions to the non-oil domestic exports decline were the US, the EU-27 and Malaysia.[8] Singapore's external trade declined by 19% in 2009 compared to the year before. The level trade reached S$747 billion in 2009. S$ 181 billion less compared to the year earlier. The contraction in external trade can be attributed to lower exports and imports, which decreased by 18 and 21%, respectively.

The decline was due to lower oil and non-oil trade. Oil trade contracted by 31% in 2009, after 50% expansion in the previous year. Non-oil trade decreased by 15% in 2009, following a flat growth in 2008. Non-oil domestic exports decreased by 11% in 2009 after a 7.9% contraction in the previous year. The decline was due to lower levels of electronic and non-electronic exports.

With the exception of Hong Kong and Taiwan, Singapore's top 10 markets contracted in 2009. The three markets which made the highest contributions to the decline of non-oil exports were the US, the EU-27 and Malaysia (Figure 3).[9]

This two-year period led to the worst economic record Singapore had for over 20 years. The values of total trade recorded for the year 2009 fell substantially lower

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[7] *Review of 2007 Trade Performance and Outlook for 2008*, International Enterprise Singapore, 2008.

[8] *Review of 2008 Trade Performance and Outlook for 2009*, International Enterprise Singapore, 2009.

[9] *Review of 2009 Trade Performance and Outlook for 2010*, International Enterprise Singapore, 2010.

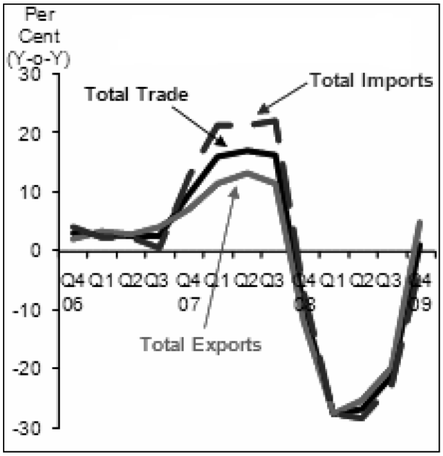

Figure 3. Singapore's external trade 2006-2008

Source: *Review of 2009 Trade Performance and Outlook for 2010*, International Enterprise Singapore, 2010.

than those recorded in 2006. Among exports affected the most in the two-year period described were consumer electronics, telecommunications equipment, personal computers, pharmaceuticals and chemicals. Biggest fall in demand came from the US and Europe.

As it was already mentioned, after virtual collapse of external demand Singapore's economy was supported wholly by domestic demand. But domestic demand had also been affected by worsening economic conditions and was largely made up of government spending and private investments, not private consumption. Consumption fell and reached 2.5% in 2008 (Figure 4). Worsening labour market conditions have caused negative expectations and fall of consumer spending.

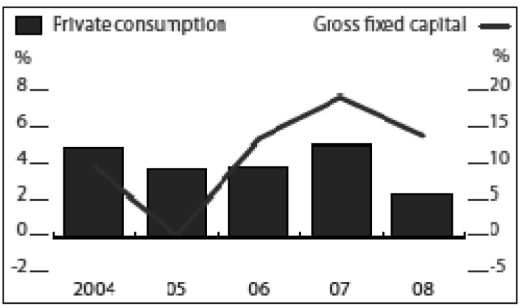

Figure 4. Consumption and investment growth

Source: *Asian Development Outlook...*

Sizeable government spending helped push the domestic demand growth to up to 3.6%. During the first three quarters both public and private investment experienced a strong growth reaching 13 and 14%, respectively. But by the fourth quarter of the year private investors' expectations became similar to those of consumers causing the size of investments to scale down. The remaining investments were largely the result of previous contracts or agreements and were generally of the construction type following a boom in that sector. Investment in equipment was small. Available preliminary data for 2009 suggest that overall consumption in that period fell in relation to 2008 and reached –0.5%

Recorded growth in 2008 was largely the result of activities in business, and financial and construction sectors with constructions recording the highest change in relation to 2007 by 20%. Business sector grew by 7.4% and financial sector by 5.5%. As expected, the fourth quarter of the year brought about some drastic changes in the growth pattern of the year. Unsurprisingly, Singapore's financial sector was the first one to suffer. Reflecting close connection to world's financial institutions it contracted by over 8% at the end of 2008. Nevertheless, growth in manufacturing saw the biggest contraction. Already weak in the first three quarters of the year it suffered further, contracting by over 10% in the fourth quarter alone. Growth record in this sector for the whole period was –4.1%.[10]

Singapore's trade and manufacturing supporting subsectors (e.g. transport and storage services) are also key elements of the economy. As the volume on international trade contracted, so did the activities in these sectors. Overall performance for 2009 was much weaker than in 2008. Services producing industries contracted by 2.2%. This was due to a contraction of all major services sectors, with the exception of the information & communications sector and business.

The manufacturing sector contracted by 4.1% compared to 2008. With the exception of the biomedical manufacturing sector, all manufacturing clusters (electronics, chemicals, transport engineering, precision engineering and general manufacturing) contracted. Unlike previous data suggested construction sector did not undergo a severe crash but, on the contrary, recorded positive growth for 2008 and 2009 with 20.8 and 16% respectively.[11]

Consumer price index rose dramatically causing inflation to surge to 6.5% in 2008. This had serious consequences to domestic expectations as consumers and investors are accustomed to low levels of inflation. Inflation in this period was the highest since 1981 when it reached ca. 8%. Since then, the average annual consumer price index has been 1.6%. When looking at inflation for the period since 1995 to 2006 and 2007 a spike can be seen in the latter period. But even then inflation reached only 2.1% giving no indication of a possible surge to over 6% the following year. Rise in inflation levels in 2008 was fuelled by high prices of oil and foodstuff recorded

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[10] *Asian Development Outlook...*

[11] Ministry of Trade and Industry, Press Release, 19 February 2010.

in the first three quarters of the year. As the recession across the world deepened and expectations worsened in 2009, oil prices fell. Suppressed by lower global oil prices and weaker domestic demand inflation in Singapore slowed sharply to just 0.6% in the first 7 months of the year. Later this level of inflation held and was the same for the whole of the year.

The problems described above paved way to serious concerns over employment with fears that economic downturn would result in large layoffs. Although the level of employment did increase in the last quarter, the number of employed (27,000) was almost half of that in the previous quarter (56,000). The total increase in employment during the 12 months reached 227,000. Unemployment levels were also worrying. The total number of redundant workers in 2008 was 16,880. In 2009 this number went up to 22,700. In both cases most workers lost their jobs in manufacturing sector. Smallest changes were recorded in the construction sector. Annual unemployment rates for 2008 and 2009 were 2.2 and 3%, respectively.[12]

4. External economic shocks and resulting Singapore's economic policies

Long-term development strategy, promoting open economy and targeting external demand as a source of growth has allowed this lacking in natural resources country to transform into a nation with a standard of living similar to that of rich countries of Western Europe and Northern America. But its biggest asset is also its biggest weakness. Unlike world's other big exporters it has almost no internal market to fall back on when external demand slackens. This "symbiotic" state with global demand causes Singapore to be more dependent on trade than any other Asian economy. This situation has always been the case for Singapore but in recent years it has strengthened further (Figure 5). As more developed nations' economies slow down, economic engine which has driven Singapore for almost 50 years grinds to a halt.

Because Singapore is so specialised in providing for trade, parts of its service sector are also dependent on it. As Asian trade hub, it developed not only infrastructure for transfer and storage of goods (harbour, etc.) but also trade related infrastructure and services (headquarters buildings, hotels and catering). Many international companies present in the country have scaled back their operations, further adding to Singapore's problems. According to company cessation data from May to October 2009 alone over 14,000 companies stopped operating. For the whole of 2008 this figure was 10,480.[13]

In January 2009 government announced a package of policies aiming to offset the effects of recession. The budget set out for the year included spending of

[12] Ministry of Manpower, Press Release, 29 January 2010.

[13] *Monthly Digest of Statistics Singapore*, Singapore Department of Statistics, January 2010.

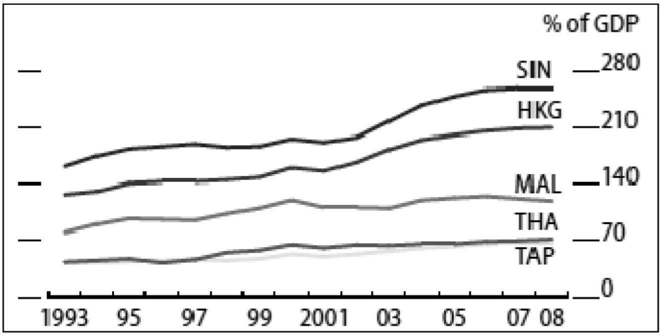

Figure 5. External trade as percentage of GDP

Source: *Asian Development Outlook...*

S$43.6 billion (US$29.3 billion) to boost the economy. Planned expenditure resulted in a budget deficit of ca. 10% of GDP. A stark contrast to estimated surplus of 1.6% in 2008.Two main packages aiming to help the economy included Special Risk--Sharing Initiative worth S$3.3billion and Jobs Credit Scheme worth S$3billion.

A number of smaller schemes were also introduced. These were: Building on Opportunities to Strengthen Tourism, a S$60 million plan to secure market demand in the tourism industry as numbers of tourists were predicted to fall to 9 million; Business Upgrading Initiatives for Long-term Development with a S$134 million fund to help small and medium-sized enterprises become more competitive through capability development; Preparing for the Upturn – collection of training schemes worth S$67 million which aimed to help companies develop personnel in science and technology through funding programs such as on-the-job training for new graduates; Young Entrepreneur Scheme to help young Singaporeans set up innovative start-ups by giving them cash from a $16 million Entrepreneurial Talent Development Fund.

One other measure including Skills Program for Upgrading and Resilience had been already launched in December previous year to help companies retrain workers, save jobs, and cut companies' retraining costs. The $400 million scheme was run by the Workforce Development Agency and the Ministry of Manpower. It received an additional $100 million in the January budget.[14]

Macroeconomic measures included lowering the level of company income tax from 18 to 17%; 20% rebate of personal income tax not exceeding S$2,000; child benefits and increased transfers for households in the low-income group. In order to limit the deficit and borrowing S$4.9 billion were used from fiscal reserves. Special

[14] G. Murdoch, *Singapore Fights Recession with Upbeat Acronyms*, Reuters, 9 March 2009, http://www.reuters.com/article/idUSTRE5190X520090210.

Risk-Sharing Initiative was a standard practice widely implemented in many economies in 2008. Its aim was to assure company liquidity by helping them get credit form financial institutions. Due to credit-crunch such loans were difficult to obtain, which threatened companies with cash-flow issues to become insolvent. The initiative aim was to help receive credit by giving a government guarantee for up to 80% of individual loans.

Jobs Credit Scheme aimed to prevent layoffs by subsidising employers. It targeted Singapore's citizens and permanent residents only. Parts of companies' labour costs were covered lowering their total costs and, hence, allowing them to retain their workforce. The scheme paid up to 12% of the first S$2,500 of the wages of each employee who contributes to the Central Provident Fund (CPF), the national savings plan. In theory, assuming wage rigidity, this was to encourage the demand for labour to shift to the right (wage subsidy effect) after it had shifted leftwards (fall in exports).

An empirical study suggests the scheme could have saved up to 30,000 jobs in 2009 and up to 50,000 in 2010 and 2011. On the other hand, the scheme runs the risk of transferring funds to companies which would have kept their workforce anyway, and misses those companies already facing problems or those which have already reduced their workforce.[15] Historically, the cost of adjustment during recessions was taken up by workers in the form of lower contributions made by employers to the national saving plan. Here, the costs are incurred by the Government.

There are economists who suggest that there were more efficient tools at government's disposal to soften the impact of recession on Singapore. For example, more effective could have been lowering of property taxes and costs of renting property instead of welfare handouts and tax brakes which effects might have been reduced by existing tax system. Another method could be to substantially increase child benefits. In the last 20 years financial help offered to families raising children have gone up from S$750 to S$2,000 annually. This is about S$167 a month. This is very little for a family with a child and does not, in practical terms, change its purchasing power.

Additionally, costs of utilities and transportation could be lowered. This, similarly to lower running costs of properties, would have an immediate effect on companies' expenditure lowering the risk of lying off workers.

The measures described above would have had tangible and local effect, unlike the reduction of CIT, which might have caused a capital drain since a large number of Singaporean companies are foreign.[16] But there is some good news. Inflation and

[15] T. Abeysinghe, J. Gu, Jobs credit scheme: Measuring its effectiveness, *The Straits Times*, 16 February 2009.

[16] T. Seng Huat, Govt should avoid handouts, *Asian One*, 22 January 2009, http://www.asiaone.com/Business/News/My%2BMoney/Story/A1Story20090122-116375.html.

growth indicators improved towards the end of 2009 suggesting that the worst may be over for Singapore. Exports in January 2010 were up by 37.1% compared to the same period in the previous year, whereas imports were up by 29.1%. The improvement came as a result of rising drugs production in Singapore's pharmaceutical sector and continuing growth in construction.

In the same period, official foreign reserves rose to US$189.6 billion. Their values in 2009 and 2008 were US$187.8 billion and US$174.1 billion, respectively.[17] In 2010 the policy to boost the economy was continued with the government announcing another range of fiscal packages in its budget. It included the S$20.5 billion Resilience Package that had three, already used, measures: Jobs Credit scheme to subsidies employers' wage bills, skills upgrading program for workers, and Special Risk-Sharing Initiative (SRI) to help businesses get credit. The Jobs Credit scheme will be scaled back and phased out in first half of 2010.[18]

On 19th February 2010 The Ministry of Trade and Industry announced it expected the Singapore economy to grow by 4.5-6.5% in 2010 raising their earlier estimate of between 3.0 and 5.0%.[19] However, there are fears that growth in construction sector and property market, which helped to speed up the economic recovery, may lead to a property bubble. To counter this the Government has eliminated housing loan schemes which defer principal payments to the future, imposed a seller stamp duty for residential properties sold within one year from the date of purchase and lowered mortgage borrowing limits. These measures are supposed to discourage short-term speculation and reduce the risk of the property market overheating.[20]

5. Conclusions

The nature of recession was such that it affected the very sectors Singapore has chosen as engines of its economy – manufacturing, and banking and finance. This "double hit" caused the slump to be very sudden and reductions in productivity drastic. Measures taken by Singaporean government to reduce the impact of global recession were, undeniably, quick and concrete. Unfortunately, effects of weakening of US, European and Japanese economies could not be avoided and the fiscal stimulus adopted only lessened the severity of recession. Even when putting the magnitude of the event aside any fiscal stimulus would have a limited effect because of the scale of openness of Singapore's economy. On the other hand, small physical size of the country may be of an advantage here, as time delays associated with implementation of macroeconomic policies could be much shorter than in other economies.

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[17] Monetary Authority of Singapore, *Official Foreign Reserves*, 8 March 2010.

[18] C. Haoxiang, Singapore's budget 2010 to aim longer term growth, *The Straits Times*, 20 October 2009.

[19] Ministry of Trade and Industry, Press Release, 19 February 2010.

[20] Singapore Budget Speech 2010, Singapore, 22 February 2010.

Although this essay was written at the end of the first quarter of 2010 there were very few concrete, official figures available to give a clear picture for the rest of that year and the next. Furthermore, there are serious fears that the problems over sovereign debt in Greece could be contagious and start a domino effect across Europe. Even though global economy has picked up and international trade has improved any financial crisis in Europe would have a profound effect on the global long term recovery. If such financial problems did happen they would, again, hit the very core of Singapore's economy. Because of this it is too early to say how well Singapore economy will cope in the aftermath of global recession. However, if Singapore continues to be as resilient and active as it has been in the past, it is possible it will regain its macroeconomic strength by the turn of this year.

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Special Feature A – Sectoral, Industry and Employment Business Cycles in Singapore, *Macroeconomic Review*, Monetary Authority of Singapore, April 2009.

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SINGAPUR A GLOBALNA RECESJA

Streszczenie: Autor rozważa problemy i decyzje, jakie stanęły przed Singapurem podczas światowej recesji, która była następstwem kryzysu finansowego rozpoczętego w 2007 r. Analizuje, jak pogarszał się stan singapurskiej gospodarki w miarę obniżania się poziomu globalnego popytu, a z nim poziomu międzynarodowego handlu. Omawia czynniki, które spowodowały, że ten szok ekonomiczny był najsilniejszy, jaki odczuł Singapur od ponad 20 lat, i wyjaśnia, dlaczego miały one tak olbrzymi wpływ na wszystkie sektory gospodarki Singapuru. Ocenia również mikro- i makroekonomiczną politykę rządu Singapuru mającą na celu ograniczenie negatywnego wpływu zewnętrznych szoków gospodarczych.