DBS Focus

Singapore: Heading for a recession

Economics/growth/fiscal/monetary

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- *The Singapore economy is likely to sink into a recession amid the impact of the Covid-19 outbreak*
- *The services sector, particularly the tourism, aviation, retail and trade related industries will bear the brunt, and key manufacturing sector will not be spared too*
- *We have lowered our full year forecast down to -0.5% to reflect the recession risk*
- *A second stimulus package of about SGD 14-16bn (approx. 2.9% of GDP) could be announced to cushion the economy from an impending recession*
- *The MAS may also announce a more aggressive monetary response to the crisis*

The Covid-19 outbreak has continued to stoke fear and panic around the world. Just when the situation in China appears to be stabilising, the healthcare systems in many countries around the world are put under tremendous pressure amid spikes in the number of cases of infection. The risk is now concentrated well beyond China.

As death toll continues to rise, consumer sentiments and investor confidence are taking huge beatings. The financial markets are being sent into tailspins. The recent dispute between the oil majors (US, Saudi Arabia and Russia), which sent global oil prices down on its sharpest one day fall since the Gulf War in 1991, has further exacerbated volatility in the financial markets.

Global outlook hasn't been grimmer than this since the Global Financial Crisis. Even as governments around the world scramble to contain the outbreak and roll out an array of both monetary and fiscal responses to buffer the impact on their economies, a massive negative growth shock on small and open economies such as Singapore will be inevitable. The latest being a self-imposed closure of borders by neighbouring country Malaysia, which is a key source of workers for Singapore.

Services sector to bear the brunt

We revised Singapore's GDP growth forecast down to 0.9% on 7th February [1]. Back then, the epidemic was still largely contained within China, with only pockets of infection (about 226 cases) outside of China. However, the situation has deteriorated sharply in the past few weeks. Even as China's Wuhan, the original epicentre of the outbreak, closed off all sixteen of its temporary hospitals due to the dwindling number of new cases within the city, the number of infections in other parts of the world has multiplied by more than 400 times since our previous report.

Tourism and aviation will be hit hard

As a result, more travel restrictions are imposed, which will hit the tourism related industries far harder than what was originally estimated. Besides China, the travel ban has now broadened to include countries such as Korea, Iran, France, Germany, Italy, Spain, Japan, Switzerland, UK and ASEAN countries. **In total, these markets account for about 69% of Singapore's total tourist arrivals in 2019**. The scale of the travel restrictions is unprecedented, and the impact will be extremely sharp. Tourism related industries such as hotels and restaurants, aviation, point-to-point transport services, retail and entertainments services will be severely impacted.

Singapore's tourist arrivals by country / region (2019)

Countries / region	Tourist arrivals	% Share
Overall	**19,111,343**	**100.0**
ASEAN	6,622,871	34.7
China	3,626,727	19.0
Japan	884,210	4.6
Korea	645,728	3.4
UK	607,736	3.2
Germany	380,678	2.0
France	212,768	1.1
Italy	102,701	0.5
Switzerland	97,933	0.5
Spain	65,386	0.3
Iran	7,963	0.0
Total affected	**13,254,701**	**69.4**

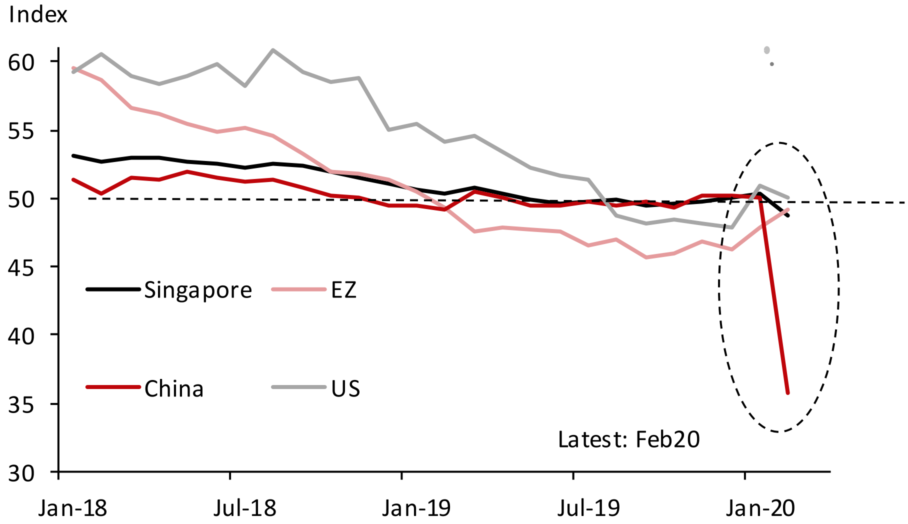
Source: CEIC, STB

Downside risk to exports and manufacturing

China imposed city lockdowns and extended closures of production plants across the country in Jan-Feb period in a bid to curb the spread of the Covid-19 virus. This resulted a drastic plunge in China's PMI to 35.7 in Feb20, from a reading of 50 the month before. Likewise, Singapore's manufacturing PMI fell to 48.7, the weakest in four years, and non-oil domestic exports (NODX) to China contracted by 35.8% YoY in the same month.

Weak global demand to weigh on exports

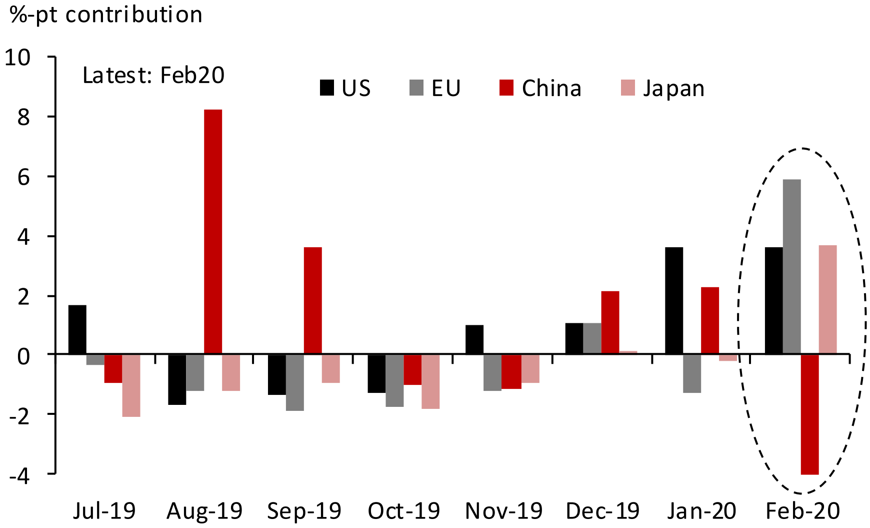
China's PMI has plunged



Sources: Bloomberg, DBS

Yet, overall NODX for February bucked the trend to post a mild expansion of 3.0%, thanks to strong surge in sales to the US (+23.5%), EU (+43%) and Japan (+61.7%). Cumulatively, the G3 markets have contributed a total of 13.2%-pts to Singapore's NODX in the month, versus a 4.5%-pts drag from China.

Fall in NODX to China offset by G3



Sources: CEIC, DOS, DBS

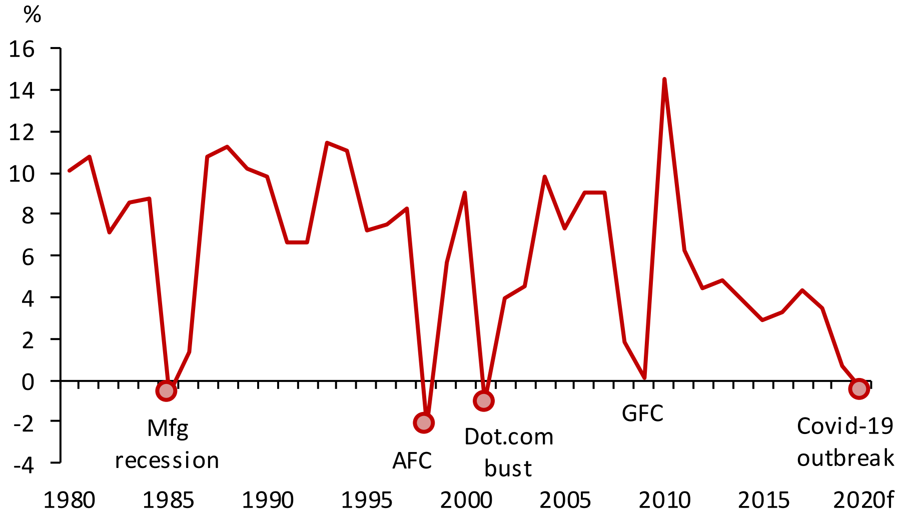
However, this could change drastically over the next few months. As governments around the world introduced city and country-wide lockdowns, border closures, and companies put in place their business continuity plans (BCP), economic activity would slow significantly. This would take a huge toll on global consumer sentiments and demand. The downswings in the financial markets with the associated negative wealth effect, would further dampen an already fragile global economy. No doubt there are emerging signs of a recovery in China's supply chains, but **sharp contraction in global demand would put a dent on the near-term prospects for exports and the manufacturing sector**.

An imminent recession

Recession appears inevitable

Considering the chaotic situation in many parts of the world and the economic costs of those restrictive measures on trade, investment, consumption and travel, this is evolving into a "self-induced" global recession. Being a small and open economy, Singapore will not be spared. **A recession in Singapore appears inevitable, and we have revised our full year GDP growth forecast for 2020 to -0.5% to reflect the recession scenario.** Note that this comes with significant downside risks should the outbreak worsen further.

Singapore's historical GDP growth and past recessions



Source: CEIC, DOS, DBS

Specifically, GDP growth figures for the first two quarters will be awful, with year-on-year contraction of up to 2%-pt expected. The negative headline (YoY) growth could sustain into the third quarter before an improvement at the end of the year. In addition, a technical recession – two consecutive quarters of sequential decline – in the first half of the year is almost a given, considering that the impact of the outbreak is no longer limited to just one quarter.

Putting into perspective, **this will be a lot deeper than SARS, and more painful than the Global Financial Crisis**. In these two downturns, Singapore still managed to post GDP growth of 4.5% and 0.1% respectively. In fact, the previous occasions when Singapore did register full year contraction were during the Dot.Com bust in 2001 (-1.1%), the Asian Financial Crisis in 1999 (-2.2%) and the manufacturing recession in 1985 (-0.6). However, it could have been worse if not for the robust policy response thus far and the forthcoming countercyclical measures in the pipeline.

Strong policy responses to buffer the impact

Amid an increasing challenging economic climate, the government announced a record fiscal deficit of SGD 10.95bn (2.1% of GDP) in Budget 2020 [2]. This came on the back of an accumulated surplus of SGD 17.4bn over the last four years. Beyond targeted countermeasures against the impact of the epidemic, broad-based growth strategies to prepare the economy for the future were also introduced. More importantly, the Stabilisation and Support Package worth SGD 4bn was rolled out to buffer the economy from the impact of the outbreak.

A massive second stimulus package

As the situation on the pandemic continued to deteriorate, official rhetoric is that a second stimulus package will be announced. **We expect the government to roll out a package of up to SGD 14-16bn (approx. 2.9% of GDP) to further buttress the economy**. This would entail utilising the remaining accumulated reserves of about SGD 7.7bn and drawing down an additional SGD 6-8bn from the reserves to fund the package. If not fully utilised, monies from the reserves could also serve as a contingency fund should a third package becomes necessary.

Plainly, **the focus has shifted from mitigating the impact of the Covid-19 outbreak to cushioning the economy from an imminent recession**. And policy responsiveness, in terms of getting the help to the companies immediately will be a crucial consideration.

Some of the policy measures may include:

- Broadening of the Temporary Bridging Loan scheme to include all industries, with the government shouldering 80% of the risk;

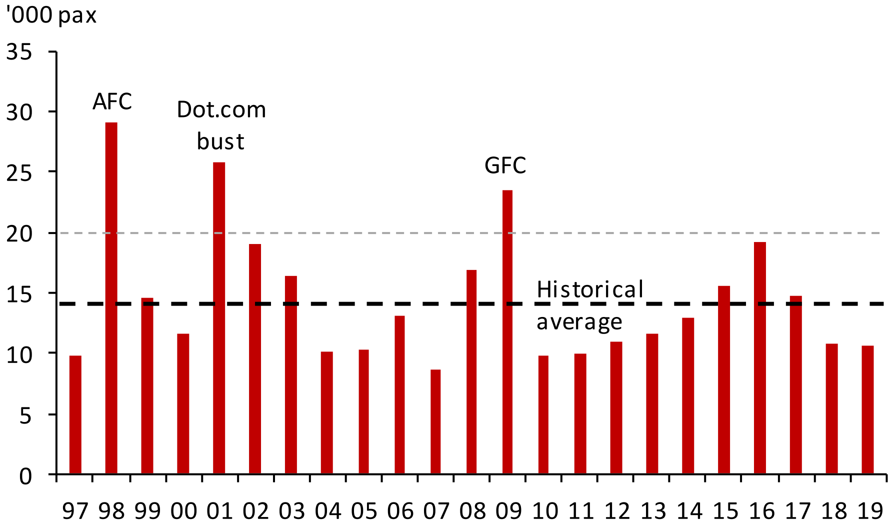
- Increase the quantum of the Temporary Bridging Loan and the Working Capital Loan schemes further for affected industries for up to SGD 2mn and SGD 1mn respectively;
- Enhancement to the Jobs Support scheme with the subsidy raised to 12% for all Singaporean workers with the duration extended to six months;
- A one-off SME Cash grant to be disbursed to micro and small enterprises immediately;
- Temporary one-month waiver of the Foreign Worker Levy (FWL for workers that are affected by the measures introduced (e.g., Malaysian workers).

Retrenchments will rise

Helping companies in order to safeguard jobs will remain a key thrust. Indeed, there will be knock-on impact from the downturn onto the labour market. **Retrenchments could rise in the coming months.** In the previous crisis (i.e., AFC, Dot.com bust and GFC), full year annual retrenchments typically exceeded 20,000. Similar phenomenon could occur in this downturn.

Total retrenchments for the year are **expected to reach about 24,500 persons, slightly above the threshold during the GFC period (23,430)**. Plainly, it could have been worse if not for the policy measures (e.g., Job Support scheme) to subsidize wages and mitigate the fallout on the labour market.

Annual retrenchment in Singapore



Source: CEIC, MOM

Nonetheless, more can be done to help Singaporeans and workers that are vulnerable to retrenchment. Some of the measures could include:

- Deferment of personal income tax payment for all retrenched workers [3];
- A one-off retrenchment benefit for displaced workers;
- Personal income tax rebates for all taxpayers (up till a certain cap) to lower the tax burden of the middle-income group, essentially the sandwiched class;
- Tax deductions for profitable companies to hire retrenched workers. The amount of tax deductions can be equivalent to, for example, six months' salary of the newly hired retrenched workers.

A "two-in-one" monetary easing by the MAS

Beyond fiscal policy, we also expect the Monetary Authority of Singapore (MAS) to ease the SGD policy in order to render more support for the economy. Inflation is no longer a risk with the recent plunge in oil prices, and measures that will lower domestic cost pressure. In fact, we reckon that full year inflation will ease to 0.4% for the year, down from 0.6% in 2019.

In contrast, recession risk is rising. **Falling inflation and the significant downside risk to growth essentially make for a more aggressive monetary response by the central bank.** Specifically, we expect MAS to 1) end the modest and gradual appreciation path of the SGD NEER policy band, and 2) introduce a downward re-centring of the band by up to 2%. In fact, an announcement before the next scheduled policy meeting around mid-April should not come as a surprise given the urgency of the matter.

Notes:

[1] Kindly refer to DBS report "Singapore: Pandemic, economics, markets" dated 7 Feb20

[2] Kindly refer to DBS report "Singapore: A robust fiscal response" dated 19 Feb20

[3] Singapore's personal income tax system is such that individual has to pay taxes for income earned the year before. Hence, a retrenched worker would still have to pay personal income taxes even when he is unemployed.

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Sources: Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations)