OCBC Bank

Singapore Outlook

# S'pore 2019 pre-Budget thoughts: Well-positioned for future challenges

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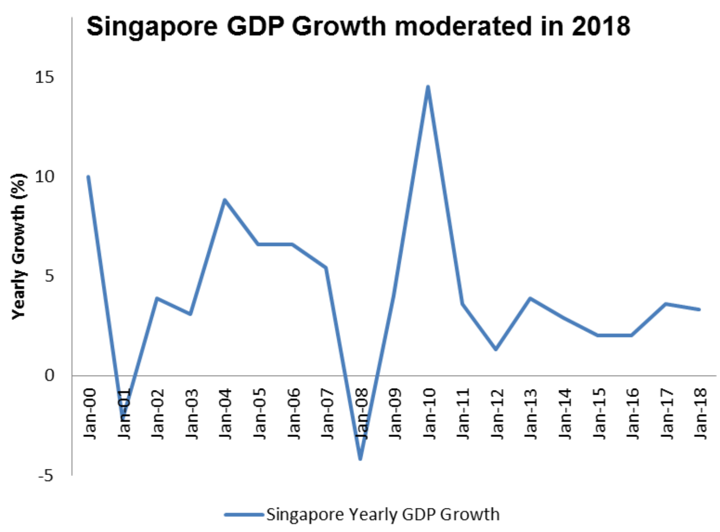
**The Singapore economy ended 2018 on a relatively healthy note.**

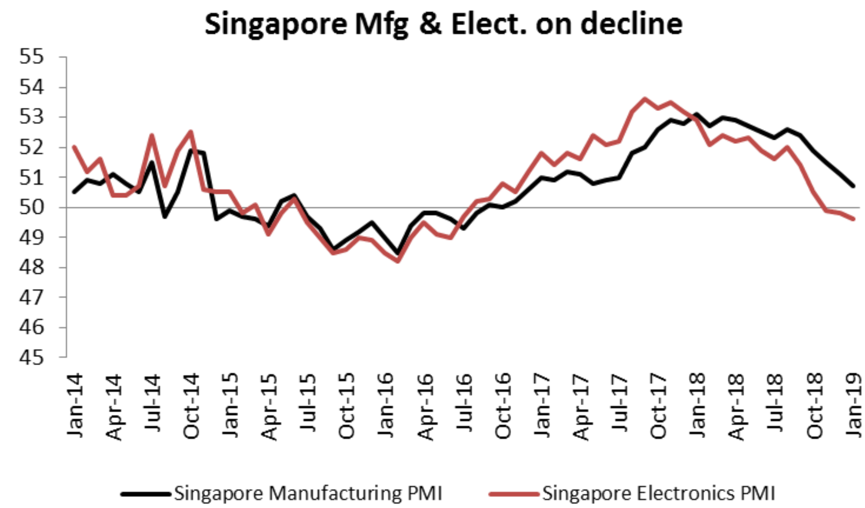
**The Singapore economy grew 3.3% on-year for the full-year 2018**, notwithstanding the US-China trade tensions, a further cooling in China's economy and eroding momentum in the manufacturing, especially electronics cycle. This is a moderation from the 3.6% seen in 2017. From a policy perspective, the Monetary Authority of Singapore (MAS) tightened its monetary policy stance by steepening the gradient of the S$NEER slope twice in April and October 2018, but cost competitiveness was not significantly impacted. The manpower challenge appeared to be at the top of the list for challenges cited by businesses in 2018, with 50% identifying rising labour cost. According to a Singapore Business Federation (SBF) National Business Survey, the top concern for large companies (65%) and SMEs (60%) is hiring people with the right skills and attitude. For fiscal policy, the 2018 Budget focused mainly on building a vibrant and innovative economy, enabling a smart, green and liveable city, and safeguarding a fiscally sustainable and secure future, as well as ensuring a caring and cohesive society.



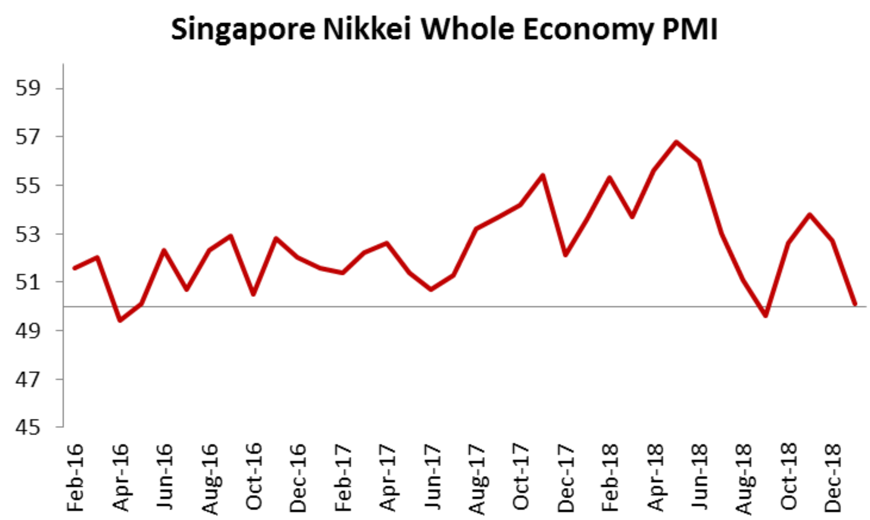

Source: Bloomberg

**The Singapore economy is at crossroads.**

2019 GDP growth prospects look slightly softer again, notwithstanding that US-China trade tensions, and the global and regional growth moderation, coupled with a decelerating Chinese economy and Brexit risks, are not unfamiliar headwinds. The IMF has downgraded its global growth forecast again to 3.5% for 2019, while the Economist magazine has warned of an era of slowbalisation. Moreover, recent regional manufacturing Purchasing Manager Index (PMI) prints look soggy and point to services and consumption needing to step up as the main growth driver this year, which is true for Singapore as well. In fact, approaching the year-end in 2018, financial market gyrations suggest some trepidation over a potential US recession. Short-term risks include the 15 February deadline for another potential US government shutdown if president Trump does not get his wall funding, 1 March deadline for US-China's 90-day tariff truce, Brexit deadline etc, and how these event risks unfold could have a significant impact on how the global growth prospects pan out.



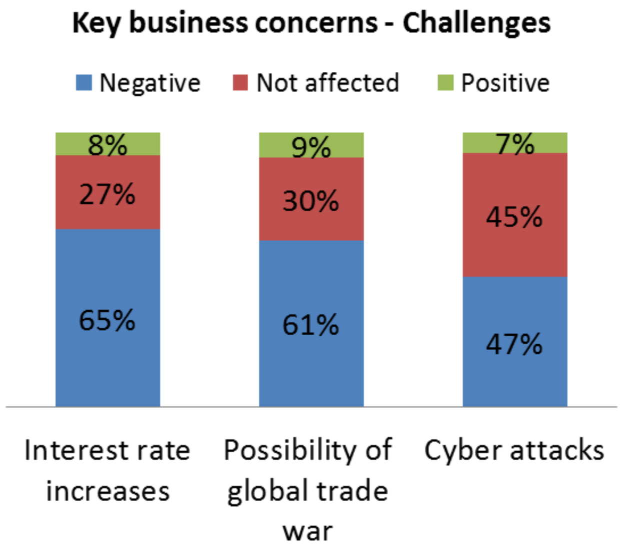

Source: Bloomberg




Source: Bloomberg

**Rising domestic business caution amid the external economic and geopolitical headwinds.**

Understandably, the business expectations survey for both manufacturers and services firms had turned south, with a net 14% and 4% of companies respectively anticipating less favourable business conditions for 1H19. The SBF survey also showed businesses were negatively impacted by challenges such as interest rate increases (65%), possible global trade war (61%) and cyber-attacks (47%) in 2018. The implications of widespread caution among the domestic business sentiments, if sustained, suggest that it may translate to fewer hiring and lower capital expenditure, which may in turn prompt workers to tighten their belts and spend less as well.




Source: SBF

**However, it is not all doom and gloom as Singapore's fiscal health is actually very strong**.

Although the government had budgeted for a small deficit of $0.6 billion (equivalent to 0.1% of GDP) for FY2018, we estimate that the budget out-turn could be a modest surplus of $0.7 billion (equivalent to 0.2% of GDP) due to slightly better than expected revenue collections for the fiscal year-to-date, namely from corporate and personal income taxes and the stamp duty (mainly before the latest cooling measures). However, a sizeable budget surplus overshoot is not anticipated for FY2018 given that GDP growth was not spectacular per se.

**More generous Budget is likely, but no urgent need to overreact to growth deceleration.**

The 2016 and 2017 fiscal surpluses were sizeable at $5.8b (1.3% of GDP) and $10.6b (2.4% of GDP) respectively. Therefore, there is ample fiscal ammunition to offer more assistance to the local economy if need be. If the 2019 Budget is a pre-election Budget, then there may be ample fiscal latitude to be more generous and further boost expenditure, especially in key areas like infrastructure, healthcare and education. Looking back at the previous three election years, both 2006 and 2015 saw an overall fiscal deficit even though real GDP growth was still positive at 8.9% yoy and 2.2% yoy respectively, whereas 2011 saw a fiscal surplus of $4 billion when GDP growth reached 6.4% yoy. Our forecast for 2019 GDP growth is 2.7% yoy, which is a further deceleration from the 3.3% last year. While financial markets are volatile, the global economy and S'pore economy does not appear to be facing an imminent financial crisis and/or recession. As such, we do not see an immediate need for a major recalibration of priorities yet. Given 2020 may be a more challenging year, it may be prudent not to over-react for now. However, given there may be a significant outlay for the Merdeka Generation package (possibly $4-7 billion, so we simplistically assume $5 billion parked under Special Transfers), the overall budget deficit for 2019 may balloon up to $6.9 billion or 1.5% of GDP.

**Singapore's overall fiscal position (SGD bn)**

| | FY16 Actual | FY17 Actual | FY18 Budget | FY18 OCBC Forecast | FY19 OCBC Forecast |
|---|---|---|---|---|---|
| Total operating revenue | 69.0 | 75.8 | 72.7 | 74.0 | 73.6 |
| Total expenditure | 71.0 | 73.6 | 80.0 | 80.0 | 83.3 |
| Primary fiscal balance | -2.1 | 2.3 | -7.3 | -6.0 | -9.7 |
| Special transfers | 6.5 | 6.2 | 9.1 | 9.1 | 13.6 |
| NIRC | 14.4 | 14.6 | 15.9 | 15.9 | 16.4 |
| Overall fiscal surplus/deficit | 5.8 | 10.6 | -0.6 | 0.7 | -6.9 |
| % of Nominal GDP | 1.3 | 2.4 | -0.1 | 0.2 | -1.5 |

Source: Bloomberg, CEIC, OCBC Bank

**What to expect for the 2019 Budget to be released on 18 February?**

Finance Minister Heng Swee Keat has said it will focus on keeping Singapore safe and secure and ensuring its industries can continue to transform and create good jobs for workers. He anticipated a comprehensive agenda including enabling workers to learn new skills to upgrade, enabling companies to build deep capabilities, looking after the environment and quality of life in Singapore, as well as details of the Merdeka Generation package. Here we break down to what the 2019 Budget may hold for an average Singaporean (whether a youth, a working professional with family commitments or an elderly/retiree) or a company (whether a large corporate or a small and medium size company).

**Budget highlights for election years**

| Budget Year | Budget highlights |
|---|---|
| 2006 | 1. Grow and Share Package<br>a. First time growth dividends were given out in cash<br>b. Citizens receive payouts of $200-$800 |
| 2011 | 1. Grow and Share Package<br>a. Singaporeans receive payouts of $100-$800 in growth dividends<br>2. Personal Income Tax rebate<br>a. 20% rebate, capped at $2000 |

| | |
|---|---|
| 2015 | 1. Personal Income Tax rebate<br>a. 50% rebate, capped at $1000<br>2. Silver Support Scheme<br>a. 150,000 elderly receive quarterly payouts of $300-$750. Estimated to cost $350m in 2016<br>3. The Pioneer Generation Package (Announced in Budget 2014, implemented in 2015)<br>a. $8 billion in total to help 450,000 senior citizens with healthcare<br>4. HDB Service and Conservancy charges<br>a. Cost the government $80 million in total<br>5. SkillsFuture credit<br>a. Over 2 million Singaporeans, aged 25 and above, receive an initial credit of $500 from 2016<br>6. Maid levies<br>a. Extend reduction to households with children aged 16 and below, up from 12 and below<br>b. 144,500 households benefited from it and it costs the government $125 million per year<br>7. Jubilee bonus<br>82,000 civil servants received $500 each |

Source: CNA, The Straits Times

**For the Singaporean man in the street:**

**For working professionals, the threat from global competition and digital disruption is real. It is timely to top up the SkillsFuture Credit from the initial $500 quantum**. The SkillsFuture Credit was introduced in 2015 Budget where every Singaporean aged 25 and above will receive an initial $500 to be used on a range of Government-supported courses. Approximately 146,000 Singaporeans started using their SkillsFuture Credit in 2018, bringing the total number of those who tapped the subsidy to around 465,000 in 2018. The cost estimate was over $1 billion a year for 2016-2020. Given that the technological and digital challenges enveloping the Singapore economy, the average Singaporean worker needs to continuously upgrade one's skillsets to stay relevant. The SkillsFuture Credit was touted to be topped up at regular intervals, so 2019 Budget appears to be a timely opportunity to top up the initial $500, possibly to the tune of another $500 for each eligible Singaporean. Beyond an absolute quantum top-up from the government to the SkillsFuture Credit, other options could be to allow an individual to top-up his/her account and receive additional 1-for-1 funding from the government capped at $X, or receive one-off tax relief for retrenched professionals who leverage on SkillsFuture to retrain for new job opportunities. This may encourage individuals to relook at the urgency and importance of re-skilling and up-skilling.

**Rising healthcare costs due to an ageing population have been a major theme in recent years. The Merdeka Generation Package** is meant to defray healthcare costs for 500,000 Singaporeans born between 1950-59, and will definitely be welcomed. Citizens aged 65 and above are tipped to double to 900,000 by 2030 (or 1 in 4) with an increase in life expectancy and the ageing of baby boomers. Beyond cost increases, capacity for aged homes may still fall short despite increases in homes and centres, according to Lien Foundation-NUS. Attracting workers to the long-term care sector is also a challenge. Making elderly care more affordable and comprehensive will become increasingly important over time. The Ministry of Health has said it is on track to meeting its targets of 6,200 daycare places, 10,000 home care places and 17,000 nursing home beds by 2020. Still, the elderly healthcare costs in Singapore are projected to rise to more than US$49 billion annually by 2030, according to a recent Marsh & McLennan Companies report. Hence, more policy attention to these areas, especially for preventive care, beyond the Merdeka Generation Package (MGP) will be timely as well.

**How much will the MGP cost?**

If you recall, the Pioneer Generation Package (PGP) was introduced in 2014 to honour and thank pioneers for their hard work and dedication, and benefited about 450,000 Singaporeans who were born on or before 31 December 1949 and obtained citizenship before 31 December 1986. The PGP will help pioneers with their healthcare costs for life (including additional 50% off subsidised services and medications at polyclinics and Specialist Outpatient Clinics), support for MediShield Life premiums through subsidies and MediSave top-ups, MediSave top-ups of $200-800 annually for life, and assistance through the Pioneer Generation Disability Assistance Scheme. The PGP alone had cost $8 billion. While the full details of the MGP is not announced, it will apply to Singaporeans born between 1950-1959. PM Lee had opined that the MGP benefits "will not be as large as for the Pioneer Generation, who had much less advantage in life. But (it) will go some way to relieve their healthcare worries, and more importantly, show our appreciation for the Merdeka Generation's contributions". Assuming that about 500,000 Singaporeans were born between 1950-1959 and qualify for MGP, albeit with less generous benefits compared to PGP, the MGP could cost anywhere between $4-7 billion. Note that Trade and Industry Minister Chan Chun Sing had also given the assurance that the funds will be set aside by this term of government “because the rule in the Singapore system is that no government can make - or should make - empty promises on behalf of a future government” and it will not come from a future hike in the GST. Hence, it is likely that the 2019 Budget will fund the MGP at one go.

**Pioneer Generation Package vs Merdeka Generation Package**

| Package | Differences | Similarities |
|---|---|---|
| Pioneer Generation (Announced in 2014, implemented in 2015) | 1. Singaporeans born in 1949 or earlier + obtained citizenship by 1986<br>2. $8 billion package<br>3. Benefits 450,000 senior citizens<br>4. Amount of Pioneer Generation MediSave top-up for each pioneer ranges from $200 to $800 annually<br>a. In 2018, pioneers born between 1945 and 1949 will receive $200, while those born between 1940 and 1944 will receive $400. Pioneers born between 1935 and 1939 will get $600, and those born in 1934 or earlier will get $800<br>b. 2017 and 2018 both saw $180 million payout in top-ups<br>c. This is in addition to the Medisave top-ups for Singaporeans aged 65 and above in 2018, which come under the GST Voucher Scheme | Both include outpatient care subsidies, MediSave top-ups, MediShield Life premium subsidies and payouts for long-term care |
| Merdeka Generation (Announced in 2018, implemented in 2019) | 1. Singaporeans born between 1950 and 1959, approximately 500,000 of them<br>2. Also available to those born in 1949 and earlier + obtained citizenship by 1996 but missed out on the previous Pioneer Generation Package<br>3. Benefits will not be "as large as for the Pioneer Generation" | |

Source: CNA, The Straits Times

**To encourage a more active lifestyle and combat chronic diseases like diabetes, a sugar tax is likely to be implemented**. Singapore has the highest prevalence of diabetes among developed nations, and almost 1 in 9 persons have diabetes. MOH tips that the number of Singapore residents with diabetes could hit one million by 2050 if nothing is done to curb the rising trend. The sugar tax could either be a single rate or tiered according to sugar content, but the main purpose is not to bolster tax revenue but to achieve higher awareness and push beverage companies to offer healthier alternatives. Some of the other proposed measures include mandatory front-of-pack nutrition labels, restrictions or bans on advertising for less healthy, pre-packaged sugar-sweetened beverages (SSB), and/or bans on higher sugar SSBs. Some 45 jurisdictions, including UK, some US cities, Mexico, Brunei and Thailand, have already imposed taxes on SSBs, so Singapore will be in good company to do so. A public consultation exercise to garner feedback to the Health Promotion Board was underway in December-January. If we look at the UK example, where a two-tier sugar tax, comprising of £0.04 (or S$0.07) per 250ml for SSBs with 2.5 teaspoons of sugar or more and £0.06 per 250ml for SSBs with four teaspoons of sugar or more, was introduced in the 2016 Budget, the measure is estimated to generate an additional £1 billion a year in tax revenue which will be spent on funding for sport in UK schools. Similarly, any sugar tax revenue could be allocated to encouraging community-based sports or health-related activities.

**In previous election year budgets, individuals did receive significant fiscal largesse**. These took the form of the Grow and Share package (comprising of $200-$800 cash payouts) in both 2006 and 2011, personal income tax rebates of 20% capped at $2,000 in 2011 and 50% capped at $1,000 in 2015, Silver Support Scheme for the elderly (where 150,000 elderly received quarterly payouts of $300-$750 amounting to $350m in 2016), and Jubilee bonus of $500 for 82,000 civil servants in 2015.

**In particular, the 2018 Budget gave a one-off SG bonus to all adult Singaporeans of between $100-300 depending on their assessable income for YA2017, so it's not inconceivable to see another one-off bonus to share in the economic growth upside in 2018.** Otherwise, the usual enhancements to the GST vouchers, U-Save vouchers and MediSave top-ups may apply. More targeted help for the low-income households could take the form of enhancements to the Workfare Income Supplements. Additional help for the needy, vulnerable or special needs segments are also both feasible and definitely welcome.

**On the personal tax front, also look for any potential tax relief for individuals** who pay the Medishield Life premiums for their elderly parents and dependent children subject to an absolute cap, and/or separate relief for premium paid for medical or health insurance whether for themselves or their family members also subject to a cap. There could also be additional tax deductions for caregiver expenses for aged or special needs persons. To encourage taking greater ownership of personal health responsibilities, there could be tax relief given for regular health screening exercises and or subsidies for community-based sport activities.

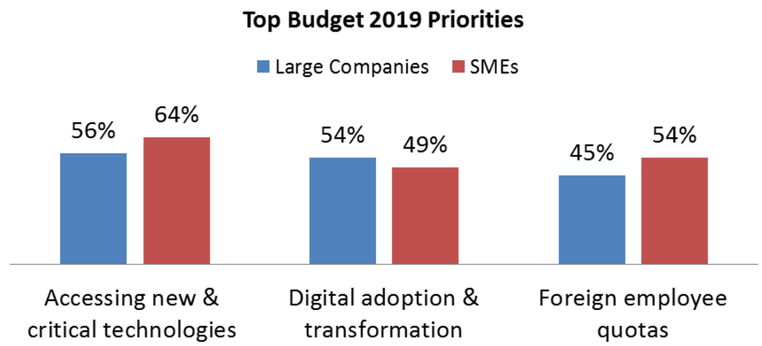
**However, with the recent property cooling, there is also less urgency to help first-time home buyers**. That said, more clarity on the details for the new Voluntary Redevelopment Scheme (VERS) for ageing Housing Development Board (HDB) flats aged 70 years or older which is application to around 5% of HDB flats, and the "less generous" compensation than the Selective En bloc Redevelopment Scheme (SERS) may be forthcoming given the recent concerns over the 99-year leases of HDB flat prices.

**Pay more for your foreign domestic worker (FDW) levy with effect from April 2019.** This was announced in the 2018 Budget to be hiked from $265 to $300 for the first maid hired and to $450 for the second maid onwards, and the qualifying age for the concessionary FDW levy of $60 under the aged person scheme will also increase from 65 to 67 years. Other potential revenue sources could include hiking the excise duties or sin taxes for products like tobacco and/or alcohol. This would be in addition to the GST on imported services that will kick in from 1 January 2020. However, the revenue contributions from each of these individual segments are not expected to be very significant per se. Hence the overarching argument for a future 2% point hike in the GST from 2021 onwards still applies for medium-term fiscal sustainability.

**For corporates:**

**More support for the digitalisation for corporates.** Much has been said about digital disruption, with often cited examples of how AirBnB, Grab, Uber, Amazon Prime, Redmart, Lazada, FoodPanda and the likes have transformed the hospitality, transport, online shopping, food delivery and other economic landscapes. Singapore already has clear ambitions as a Smart Nation, so e-commerce, digitalisation and implementing digital solutions are nothing new. However, there is a need to broaden and provide end-to-end support for SMEs in their digital transformation journey. This could comprise transforming their business models, providing data analytics, artificial intelligence (AI), customer experience design and digital marketing resources, sharing Asian consumer analytics and market insights, and manpower training as well. This is especially true for the retail sector. Only 33% of SMEs currently prioritise the development of digital business capabilities compared to large companies (60%) according to SBF. This is even though the 2018 Budget did talk about ramping up the SMEs Go Digital programme to develop targeted industry digital plans, and the TechSkills Accelerator efforts to equip people with relevant skills.

**Singapore has dropped from 1st (which went to the US) to 2nd place in the top 10 digital-competitive countries.** While ranked first in the knowledge and technology factors, Singapore came in 15th place (previously 6th) in future readiness. More tellingly, despite the existence of high levels of training and education, and an environment conducive to digitalization, society's attitudes towards the adoption of technologies and the agility of business to take advantage of the digital transformation are rather limited at 20th and 18th place respectively, according to the IMD World Digital Competitiveness Ranking 2018. Interestingly, both large and SMEs hope that the 2019 Budget will provide more support for accessing new and critical technologies, as well as help with digital adoption and transformation.

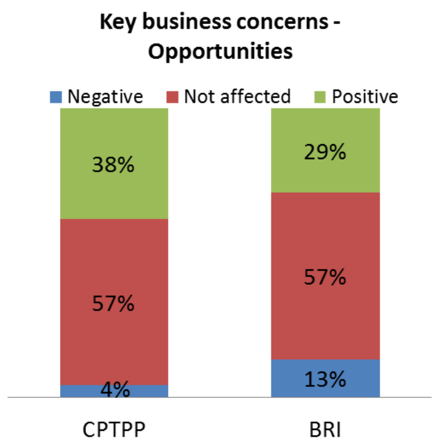



Source: SBF

**Tie to ramp up the ITMs and put more resources to up the ante?**
For businesses, the Industry Transformation Maps (ITMs) was launched with much fanfare in 2016. A total of 23 ITMs covering 80% of the Singapore economy were touted as an integrated approach for trade associations and chambers, companies and the Government to work together to prepare for the challenges of the future economy and stay abreast of global competition. With the ITM implementation well underway, there remain questions of how to benchmark the progress of ITMs and if more resources need to be allocated to the trade associations and business chambers to play a bigger role of business facilitation, especially in the areas of encouraging “hunting in packs” and joint ventures to crack new and existing overseas markets. This is especially since the SBF survey which showed that 8 in 10 businesses believe collaboration with other businesses is important to expedite the market entry proves, with relevant contacts in the target overseas market (52%) rated as most helpful.

**Smaller companies still lag in the innovation and internationalisation drive.** Often cited constraints include management bandwidth, busyness with daily survival, lack of know-how etc. These are not new challenges per se, but given the amount of policy attention that has been focused on bringing the SMEs up the value curve, it begs the question of why it remains such an uphill task. In terms of the differentiation between medium and small enterprises, it may be timely to consider greater enhancement of financial schemes to aid the small enterprises overcome the myriad of difficulties they face. Ironically, there was a decline in overseas expansion activities among SMEs from 81% in 2017 to 68% in 2018.

**With multi-national companies now relooking at their China strategy amid the ongoing US-China trade war, and considering diversifying their manufacturing and production value chains to Southeast Asia, Singapore is naturally well-positioned** to capitalise on this trend given our financial and transport hub status, robust legal framework, educated manpower and strong network of free trade agreements. Given the shift in global value chains, companies need to reassess their operational strategies and potentially adopt a global-local approach. Note that the SBF survey highlighted that domestic businesses are optimistic that the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Belt and Road Initiative (BRI) will bring new opportunities. To build on this, local capabilities need to continue to be sharpened to attract, support and anchor manufacturing and other ancillary services, especially the higher value-adding activities, to be based here. The Enterprise Development Grant, Capability Transfer Programme and the Tech Skills Accelerator (TeSA) are already in place, but time is of the essence, so fast-track approval is necessary.




Source: SBF

**The government can take the lead in incorporating new technologies into our daily lives and businesses practices, but building cyber resilience is also critical.** Cyber-attacks are increasingly frequent, sophisticated and impactful, and collective action by the Government, businesses, individuals and the community are necessary for a safer cyberspace, according to PM Lee. Recent incidents have reflected the growing importance of cyber-security in order to safeguard Singapore's Smart Nation vision and protect the integrity of Singapore's national databases. At the micro level, targeted initiatives to fight the war on cyber-related crime could include digital tax incentives or grants to SMEs to invest in cybersecurity products, services and solutions, and enhance cyber resilience. Additional protective measures, whether in terms of public education programs and collaborative platforms to facilitate information and knowledge sharing, can also form part of the integral cyber defence for Singapore. This will add meat to Singapore's cybersecurity strategy based on four pillars, namely strengthening the resilience of our Critical Information Infrastructure. Mobilise businesses and the community to make cyberspace safer, by countering cyber threats, combating cybercrime and protecting personal data, developing a vibrant cybersecurity ecosystem comprising a skilled workforce, technologically-advanced companies and strong research collaborations, so that it can support Singapore's cybersecurity needs and be a source of new economic growth, and stepping up efforts to forge strong international partnerships, given that cyber threats do not respect sovereign boundaries.

**Manpower issues remain important for companies seeking to grow in the coming years**. There is unlikely to have any be any broad-based loosening of the foreign worker policies given the need to continue to push for more productivity-driven growth. Moreover, the earlier planned foreign worker levy (FWL) hikes for the marine shipyard and process sectors were deferred again for the third year in 2018 until 2019, and we think a further deferral is highly unlikely. However, some companies have argued for a more fine-tuned and targeted approach to allow faster-growing industries or segments to be able to source for the skilled talent they need. There is some merit for consideration, but the latest business expectations surveys also suggest a relatively lacklustre employment picture ahead. Notably, a net 2% of manufacturers anticipate lower employment intentions ahead, which matches the employment outlook back in 3Q18, while services firms in the accommodation, real estate and financial & insurance industries also expect to reduce hiring activity in 1Q19. In 2018, the improvements in local employment (28,400) were led by the services industries like community, social & personal services, transportation & storage, financial & insurance services, information & communications, and professional services. The 2018 labour market report revealed that while total employment grew by 15,600 and retrenchments held relatively steady at 2,800 in 4Q18, nevertheless the overall unemployment rate still edged up to 2.2% (3.0% for residents and 3.1% for citizens). As such, the overall unemployment rate may continue to tick higher in 1H19 before stabilizing.

**Changes to Foreign Worker Levies in Budget 2017***

| Sector | Tier | Sector Dependency Ratio (DR) | Levy Rates ($) (R1/R2) Current | Levy Rates ($) (R1/R2) 1 July 2017 | Levy Rates ($) (R1/R2) 1 July 2018 |
|---|---|---|---|---|---|
| **Construction** | Basic tier | ≤ 87.5% | 300 / 650 | 300 / 700 | 300 / 700 |
| | MYE-Wavier | | 600 / 950 | 600 / 950 | 600 / 950 |
| **Services** | Basic tier | ≤ 10% | 300 / 450 | 300 / 450 | |
| | Tier 2 | 10-25% | 400 / 600 | 400 / 600 | |
| | Tier 3 | 25-40% | 600 / 800 | 600 / 800 | |
| **Marine** | Basic tier | ≤ 83.3% | 300 / 400 | ~~350 / 500~~ *300 / 400*^ | |
| **Process** | Basic tier | ≤ 87.5% | 300 / 450 | ~~300 / 500~~ *300 / 450*^ | |
| | MYE-Wavier | | 600 / 750 | ~~600 / 800~~ *600 / 750*^ | |
| **Manufacturing** | Basic tier | ≤ 25% | 250 / 370 | 250 / 370 | |
| | Tier 2 | 25-50% | 350 / 470 | 350 / 470 | |
| | Tier 3 | 50-60% | 550 / 650 | 550 / 650 | |

Source: Budget 2017

*In Budget 2018, foreign worker levy rates remain unchanged for all sectors. The earlier-announced (Budget 2015) planned foreign worker levy increases for marine shipyard and process sectors were once again deferred.

**Pushing ahead towards a green and zero-waste nation**. 2019 is Singapore's Year Towards Zero Waste campaign with a year-long campaign aimed at raising awareness of waste issues in Singapore and the need to conserve resources, as well as relooking the waste management cycle for three major streams of trash: Food waste, packing waste and e-waste, under its first Zero Waste Masterplan. The Ministry of the Environment and Water Resources and the National Environment Agency will publish their inaugural Zero Waste Masterplan in the second half of 2019, so more policy resources will likely to focus on efforts to encourage recycling right, supporting relevant ground-up projects and reusing and resources in a circular economy approach.