OCBC Bank

Singapore: Services Growth Deflated in 3Q16

Oct 14, 2016

Singapore

Treasury Advisory

Corporate FX & Structured Products

Tel: 6349-1888 / 1881

Fixed Income & Structured Products

Tel: 6349-1810

Interest Rate Derivatives

Tel: 6349-1899

Investments & Structured Products

Tel: 6349-1886

Selena Ling
+65 6530-4887
LingSSSelena@ocbc.com

Barnabas Gan
+65 6530-1778
BarnabasGan@ocbc.com

3Q16 GDP growth braked sharply to 0.6% yoy (-4.1% qoq saar).
The Singapore economy slumped 4.1% qoq saar in 3Q16, the biggest contraction since 3Q12 and underwhelming even the most bearish of the consensus forecasts. The key drags were manufacturing (-17.4% qoq saar which is the largest drop since 3Q12 as well), which was anticipated, but services momentum shrank for the third straight quarter by 1.9% qoq saar. This is akin to the second growth engine running into difficulties for the Singapore economy, and was attributable to the wholesale trade segment which was dragged down by lower prices for petroleum and chemical products.

In on-year terms, the 3Q16 growth print of +0.6% for headline GDP and -0.1% for services were both the slowest since 3Q09 (post-GFC). The flash estimates were revealing for the following reasons:

- **The 1.4% yoy manufacturing expansion we saw in 2Q16 was a blip**. The stabilisation in the Jul and Aug industrial production data and the return of the latest manufacturing PMI data to >50 (expansion territory) were also likely illusionary. Looking ahead, the manufacturing growth will likely continue to be weighed down by transport engineering and precision engineering (due to O&G weakness globally), biomedical and general manufacturing clusters. The WTO's recent downgrade of both 2016 and 2017 global trade growth forecasts and China's latest export data reinforces the grim picture.

- **The drag from the external demand weakness has now permeated into the core of the Singapore economy**, **namely the services sector**. Although there are still growth opportunities within selected services industries like infocomms, education, health and social services segments, domestic business and consumer sentiments have clearly softened in line with the labour market conditions. With more muted wage growth amid a pullback in hiring intentions, consumption will likely be more restrained.

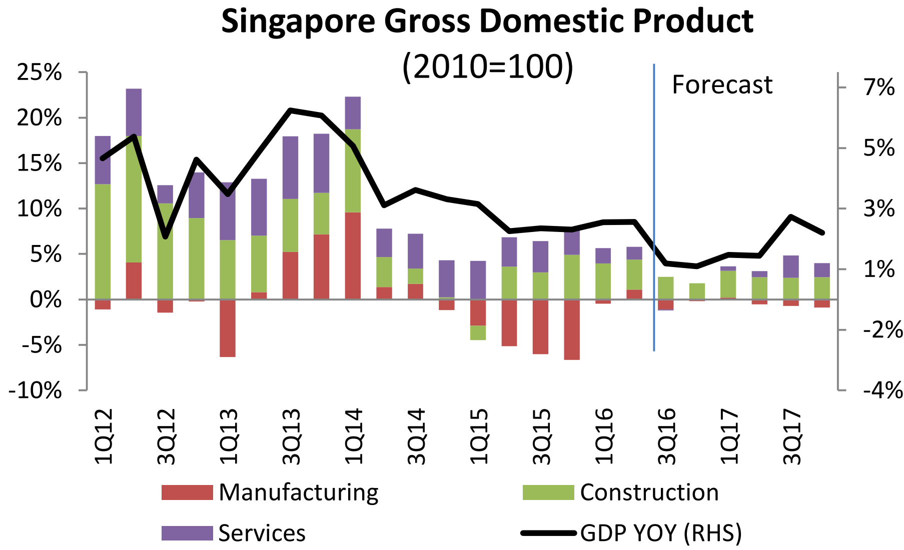
- **Construction remains the only bright spot**, expanding by 2.5% yoy (+0.5% qoq saar), lifted by public construction activities notwithstanding the sharper decline in private sector construction activities. As such, there is room for stimulative fiscal measures in the FY17 Budget (due in 1Q17), with government spending to underpin the healthcare and education project pipeline.

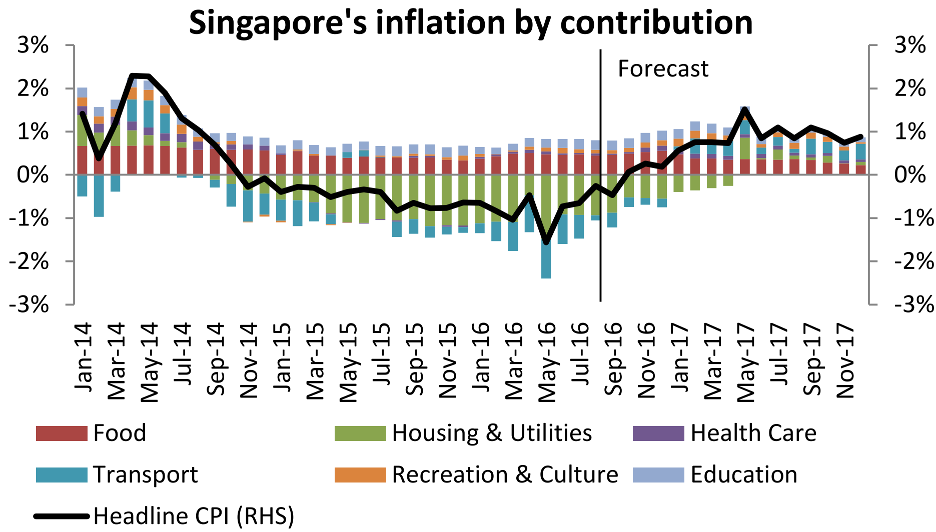
- **A downgrade for full-year growth forecast is inevitable due to 3Q disappointment and the downward revision of 1H GDP growth estimates.** Given the flat-lining of services growth momentum, we revise our full-year GDP growth forecast for 2016 to 1.3% yoy and 2017 to 1.5%, down from 1.9% and 2.0% previously. The official growth forecast is at the lower end of the 1-2% range for 2016 and only slightly higher for 2017.

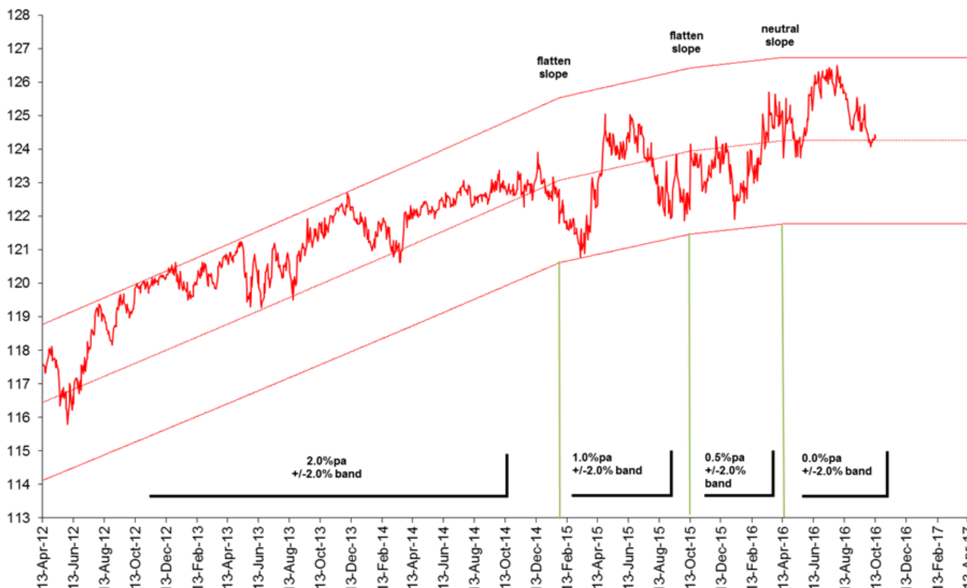
- **MAS kept monetary policy static as we anticipated.** MAS kept monetary policy settings unchanged, maintaining the rate of appreciation at zero percent, and keeping the width of the policy band and the level at which it is centered also unchanged. MAS' viewpoint is that the current policy band provides some flexibility to accommodate the near-term weakness in inflation and growth. We read it as saving the policy ammunition (potentially a re-centering lower) to be deployed if necessary, possibly at the next policy meeting in April 2017, given that there are significant headline event risks ahead on the horizon such as the US presidential elections and a potential FOMC rate hike in December.

- **Headline and core inflation expectations have softened but are anticipated to rise benignly in 2017.** MAS tips 2017 headline inflation to rise from around -0.5% this year to 0.5-1.5% next year, and core inflation to similarly creep higher from around 1% this year to 1-2% next year, predicated on global oil prices having troughed in 2016, muted wage growth, and moderate price increases for healthcare and education services, and higher private road transport costs (amid carpark fee hikes, higher petrol costs, and expected tapering of COE supply). In the interim, the domestic short-term interest rate outlook remains benign and a function of the currency gyrations and broader USD story. **We tip 3-month SIBOR and SOR at 0.9% and 0.7% respectively by end-2016 and to rise modestly to 1.08% and 0.88% by mid-2017.**

- **The 2H16 growth weakness sets the stage for a more stimulative FY17 Budget.** If a conservative official 2017 GDP growth forecast of 0-2% is announced at a later date, this could pave the way for a more aggressive fiscal stance. Sustained public construction projects could provide a stabilising growth force amid the twin drags from manufacturing and services. Logical questions that will likely arise are if the property cooling measures and the foreign worker levies will be unwound should the Singapore economy enters into a technical recession. The official rhetoric remains that it is still pre-mature to unwind some of the temporary property cooling measures like the ABSD and the SSD, but this option will be on the table going into 2017. Similarly, any major strategic policy shifts may be unveiled with the FutureEconomy Committee towards the end of this year. Nevertheless, with the modest uptick in the unemployment rate amid the softening domestic labour market conditions, one area of continued policy focus going forward will be the upgrading and upskilling of workers, especially the professionals, managers, executives & technicians (PMETs).







Source: CEIC, OCBC Bank

This publication is solely for information purposes only and may not be published, circulated, reproduced or distributed in whole or in part to any other person without our prior written consent. This publication should not be construed as an offer or solicitation for the subscription, purchase or sale of the securities/instruments mentioned herein. Any forecast on the economy, stock market, bond market and economic trends of the markets provided is not necessarily indicative of the future or likely performance of the securities/instruments. Whilst the information contained herein has been compiled from sources believed to be reliable and we have taken all reasonable care to ensure that the information contained in this publication is not untrue or misleading at the time of publication, we cannot guarantee and we make no representation as to its accuracy or completeness, and you should not act on it without first independently verifying its contents. The securities/instruments mentioned in this publication may not be suitable for investment by all investors. Any opinion or estimate contained in this report is subject to change without notice. We have not given any consideration to and we have not made any investigation of the investment objectives, financial situation or particular needs of the recipient or any class of persons, and accordingly, no warranty whatsoever is given and no liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of the recipient or any class of persons acting on such information or opinion or estimate. This publication may cover a wide range of topics and is not intended to be a comprehensive study or to provide any recommendation or advice on personal investing or financial planning. Accordingly, they should not be relied on or treated as a substitute for specific advice concerning individual situations. Please seek advice from a financial adviser regarding the suitability of any investment product taking into account your specific investment objectives, financial situation or particular needs before you make a commitment to purchase the investment product. OCBC and/or its related and affiliated corporations may at any time make markets in the securities/instruments mentioned in this publication and together with their respective directors and officers, may have or take positions in the securities/instruments mentioned in this publication and may be engaged in purchasing or selling the same for themselves or their clients, and may also perform or seek to perform broking and other investment or securities-related services for the corporations whose securities are mentioned in this publication as well as other parties generally.

Co.Reg.no.:193200032W