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MAS maintains status quo with a milder 3Q20 growth contraction

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Highlights:

S'pore's 3Q20 GDP growth saw a contraction of 7.0% yoy (+7.9% qoq sa) according to advance estimates, while the 2Q20 growth estimates were revised to -13.3% yoy (-13.2% qoq sa). While 3Q20 GDP growth was slightly weaker than our forecast of -6.5% yoy and Bloomberg consensus forecast of -6.8% yoy, nevertheless the silver lining was manufacturing which reverted to positive growth +2.0% yoy as expected, led by semiconductor and precision engineering industries due to healthy global demand for semiconductors and semiconductor manufacturing equipment. Meanwhile, the services and construction sectors remain laggard at -8.0% yoy (+6.8% qoq sa) and -44.7% yoy (+38.7% qoq sa) respectively, albeit this marked a sequential improvement from their severe 2Q20 slump of -13.6% yoy and -59.9% yoy which coincided with the Circuit Breaker period. The construction sector has contracted on-year for the third straight quarter as the resumption of construction activities has been slow due to the need to implement safe management measures. Meanwhile, the aviation and tourism-related services industries continued to weigh down the services sector even though the finance & insurance and information & communications industries saw steady growth during the quarter. Notably, the combination of a weak labour market which impacted consumer confidence and spending, coupled with capacity constraints for retail and restaurants, meant that the retail and food services industries, while improving, were still lower than pre-Covid levels a year ago.

Looking ahead, we tip 4Q20 GDP growth to contract a milder -1.3% yoy, so no change to our full-year GDP growth forecast of around -5.5% yoy. If the Spore economy moves into Phase 3 in 4Q20, given the encouraging falling domestic Covid-19 infection numbers (especially in the foreign worker dormitories), this could mean further loosening of restriction/containment measures which should bode well for the laggard construction and services sectors, even though the road ahead for the aviation and hospitality-related industries remain challenging due to most international borders being shut. The external environment remains highly uncertain, with resurgence of infections leading to localised shutdowns in some key trading partners, heightened uncertainties pertaining to US-China relations and future fiscal support. One upcoming event risk is the US elections in early November where any prolonged uncertainty over the election outcome could potentially weigh on market risk sentiments and contribute to financial market volatility. MAS also tips sequential growth to slow in 4Q20 as the initial uptick in consumer-facing services is likely to fade due to the soft labour market conditions and lingering public health concerns.

This implies that any pent-up or "revenge" spending post-Circuit Breaker seen in 3Q20 could easily fade into 4Q20 due to the long tail nature of the Covid pandemic. This is especially since the domestic unemployment rate has likely not peaked yet and job redundancies are likely to creep higher from here.

MAS kept its S$NEER policy stance unchanged as widely expected, noting it was appropriate given the deterioration in economic conditions and weaker inflation outlook, and aimed to complement fiscal, liquidity and financial policies to support the Spore economy through the Covid-19 crisis. The key takeaways from the MPS was the emphasis on the weak recovery momentum amid a sluggish external backdrop, with persistent weakness in some domestic services and limited recovery in the travel-related sector, and while core inflation will turn positive in 2021, it will remain well below its long-term average. **Overall, the tone is basically status quo with a tinge of dovishness out into 2021** when a clearer assessment of the global and domestic economic recovery prospects and inflationary outlook may warrant a reconsideration of the currently accommodative monetary policy stance. Again, monetary policy accommodation is pitched as a "complement" to the fiscal policy efforts to mitigate the economic impact of Covid-19 and to ensure price stability over the medium term. **With MAS in wait-and-see mode, we expect short-term SGD interest rates to also tread water around current ranges, with the 3-month SIBOR and SOR anchored around 0.40% and 0.18% for the rest of this year.**

It is interesting that no 2021 GDP growth forecast range was provided even though MAS released its 2021 headline and core inflation expectations. MAS tips headline and core CPI to come in between -0.5% and 0% in 2020, and project headline CPI between -0.5% and 0.5% with core CPI at 0-1% in 2021. External inflationary pressures remain subdued given weak commodity markets and sluggish growth in our major trading partners, while domestic cost pressures are also likely muted due to the softening labour market conditions, albeit the disinflationary effects of government subsidies introduced this year will start to fade. As demand for some domestic services gradually pick up, core inflation is likely to turn mildly positive in 2021. In particular, private transport costs should rise modestly amid a continued reduction in the COE supply. With core inflation remaining low, there is no urgency to warrant an immediate reconsideration of the current S$NEER policy stance at this juncture, even though some reflation is anticipated next year. **Our 2021 GDP growth forecast is 4-6% yoy.**

Essentially an uneven recovery in 2021. The MAS view is that the record above-trend growth expected in 2021 is due to the effects of the low base in 2020 and the economic scarring inflected by the Covid pandemic will continue to weigh on external demand conditions in the next year or so. While the negative output gap will narrow only slowly in the year ahead - most sectors should recoup their pre-Covid levels by end-2021, with the exception being the travel-related services which will still likely fall well short of pre-Covid levels, whereas advanced manufacturing, ICT and digital financial services will lead the recovery. This largely dovetails with the latest IMF updates of its global growth forecasts which point to a milder 2020 recession of 4.4% (previously -5.2% in June) to reflect better-than-expected 2Q20 growth in developed economies, but shaded down its 2021 growth forecast by 0.2% points to 5.2% in anticipation of setbacks and a long ascent back to pre-pandemic levels of activities.

Gross Domestic Product in chained (2015) dollars

	3Q19	4Q19	2019	1Q20	2Q20	**3Q20***
Percentage change over corresponding period of previous year						
Overall GDP	0.7	1.0	0.7	-0.3	-13.3	**-7.0**
Goods Producing Industries						
Manufacturing	-0.7	-2.3	-1.4	7.9	-0.8	**2.0**
Construction	3.1	4.3	2.8	-1.2	-59.9	**-44.7**
Services Producing Industries	0.8	1.5	1.1	-2.3	-13.6	**-8.0**
Quarter-on-quarter growth rate, seasonally-adjusted						
Overall GDP	0.6	0.2	0.7	-0.8	-13.2	**7.9**
Goods Producing Industries						
Manufacturing	1.2	-1.5	-1.4	9.6	-9.1	**3.9**
Construction	0.9	1.3	2.8	-3.2	-59.4	**38.7**
Services Producing Industries	0.3	0.5	1.1	-3.4	-11.2	**6.8**

*Advance estimates
(Source: Singstat)

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