

Highlights from the 18th Singapore Economic Roundtable

21 November 2012

By IPS Economic and Business Cluster

Background on the Singapore Economic Roundtable

Started in 2003, the Singapore Economic Roundtable (SER) has successfully brought together a selected group of economists, academics, business leaders and policy-makers twice-yearly to discuss pertinent issues facing Singapore's position in the global economy. The SER assesses current monetary and fiscal policy in the light of changing economic conditions and also features a special topical session which looks at longer term structural challenges facing Singapore. Conducted along Chatham House rules of confidentiality, the SER provides a forum for experts to articulate their views and recommendations, and is intended to generate a frank and open exchange of ideas and concerns.

The 18th SER, which was held on 21 November 2012, focused on the macro-economic outlook in the medium term as well as the structural aspects of rising business costs in Singapore.

Proceedings from the 18th SER will be documented in an IPS publication released later this year. A brief summary of key issues of interest surfaced during the 18th SER are provided here:

Economic Outlook and Implications for Policy

1) There was not much anxiety about the immediate prospects for economic growth.

Participants recognised the risks to growth from a weaker global economy, falling construction contracts and weak productivity. But most participants appeared to agree with the Monetary Authority of Singapore (MAS) view that strong domestic demand (contributing some 70% to growth in the second half of 2012) driven by non-cyclical forces such as infrastructure and education spending will hold up and support overall growth.

2) The growth-inflation trade-off has worsened, many are concerned about competitiveness.

Nevertheless, with the global deleveraging process persisting and other threats to external demand, Singapore's growth outlook was likely to be subdued going forward. At home, the restructuring towards higher productivity will raise inflation to levels that will be higher than what Singapore is used to, as restrictions on foreign workers tighten labour markets and push up wages. Most participants agreed with MAS that a good part of this rise in inflation was transitional and that once the economy had

completed its restructuring, inflation would tone down. Still, other factors which fuel inflation would persist at the global level such as the zero-interest rate policy and large capital inflows.

Several business sector participants warned that Singapore's competitiveness was at risk as costs rose. They felt that the appreciating Singapore Dollar compounds the challenges they face. One participant from the logistics industry observed while infrastructure used to give Singapore a competitive edge in the past, it has become today a drag on growth, pointing to traffic congestion and heightened regulatory restrictions which affected his industry.

MAS agreed that some costs were higher in Singapore than in Hong Kong, which had similar land and labour constraints. It is undertaking a study to understand the deeper causes of this problem.

3) There continues to be concerns that our monetary policy tools are out-dated though no better alternatives were presented.

Many participants expressed concerns over the exchange rate appreciation needed to contain inflation. They saw monetary policy as having limitations in addressing issues which are better managed by supply side policies that have already been implemented (ie: building of more flats to house the larger population base).

MAS explained why an interest rate based policy would not do better. Domestic demand is currently being driven by cyclical components (such as strong retail sales and bank lending) and non-cyclical components such as education, private transport, healthcare and housing where supply constraints were raising costs. Were interest rates to be used to address, say housing costs, the levels of interest rates required would be so high as to cause extensive damage to the economy. MAS also explained that the exchange rate appreciation was calibrated so as to contain inflationary expectations but and was not excessively aggressive as it took into account the fact that rising costs were also part of a necessary adjustment of the economy.

4) Policy coordination and clearer Central Bank communication is essential

Several participants expressed concerns over two aspects of policy – an apparent lack of policy coordination and the need for clearer central bank communication.

Participants felt that monetary policy and housing policy were not coordinated well. Quantitative easing in the G-3 economies made for huge capital inflows into our asset markets leading to macro-prudential policy restrictions on the housing sector. But these have been negated by banks offering easy access to mortgages. Some participants also felt that there had been a lack of policy coordination in the transportation sector.

There is also a need for Central Bank to communicate effectively, with reference to the tipping point of growth whereby policy measures are introduced to curb inflation. The role of communication helps to shape expectation which will influence economic outcome.

Rising Cost of Doing Business– Current Status and Implications for Singapore

The discussion on business costs in Singapore raised more questions than answers:

- 1) There is still a lack of clarity on the key drivers of business cost escalation.

Business participants disputed some of the findings of the survey done as part of the presentation on business costs in Singapore. They felt, for instance, that rental cost escalation was far more serious a problem than the survey had identified. The sample size of 195 small and medium enterprises (SMEs) was small against an actual population of 150,000 (SMEs).

There was also some uncertainty as to why demand for labour remained so strong despite the rising wages and sharp slowdown in the economy. One participant postulated that there was insufficient “creative destruction” in Singapore because policy support for small businesses were helping inefficient businesses to survive, which meant that scarce labour resources were not being released to the rest of the economy. Wasteful subsidies and incentives that indirectly drove up demand for, and the prices of, scarce land and labour need to be reviewed.

Another issue was whether the lack of scale economies in Singapore meant that unit costs would inevitably tend to be high. There was no clear consensus on this issue among participants.

- 2) Singapore businesses are stepping up the pace of restructuring in response to rising costs.

SMEs are increasingly looking overseas for outsourcing options. The Iskandar region in South Johor, Malaysia is mentioned as a natural location due to proximity. Others mentioned include the Philippines and Indonesia. Participants were concerned with: a) the productivity and efficiency of operations overseas compared to Singapore, b) how to make the process more manageable through greater integration.

- 3) Competition related issues could be aggravating cost escalation.

One major concern that remains unaddressed is the extraction of surplus by upstream players such as suppliers and landlords who are able to squeeze SMEs due to a lack of competition.

The Competition Commission of Singapore (CCS) acknowledged that the problem could exist. CCS will continue to pursue investigations into possible anti-competitive conduct along the entire supply chain of some industries. However, CCS felt that a more detailed study of the market structure of rentals was required before conclusions could be drawn about anti-competitive behavior in industrial or commercial rentals. There was, however, some evidence to suggest there was an increasing dispersion of rentals, suggesting price discrimination between tenants based on their size or other attributes.

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