

Radio Singapore International, Will Singapore downturn in electronics sector in 2005?, 28 Jan 2005.

Will Singapore see downturn in electronics sector in 2005?

January 28, 2005

In Business Ideas this week, two economists offer their analysis on Singapore's economic outlook for 2005, and how the major global economies are expected to perform this year.

Welcome to the program, I'm Melanie Yip

MB: You know, if you look at the hundreds of factors that could affect Singapore's outlook over the few years, we can discern a few trends.

That was Manu Baskaran, an economist from the Centennial Group in Singapore. At a recent forum organized by Singapore's Institute of Policy Studies, Manu pointed to some trends that may affect Singapore's economic growth in 2005.

MB: That's first of all, the set of indicators that you know already exists, that there's stuff virtually in the pipeline that you know for certain is going to come down and hit us. And that tells us that there is going to be slower growth this year. But then, there is another set of factors, imbalances in the global economy, political stress points in the Middle East and you roughly know that it is impossible that all these are resolved in a nice and peaceful manner, and that tells you that you have a down turn coming through, with a risk of further down sides, as some of these risk factors play themselves out.

But Manu remains relatively positive about Singapore's abilities to handle external economic shocks.

MB: I'm relatively less dismal about how Singapore can respond to this dismal outlook in the global environment. And the reason that I'm saying that is there's been some very positive changes for Singapore. The region is going to be much of a source of positive impact. And I think domestically, some important changes have taken place that allow us to be more resilient to external shocks. However, in the long term, I still think that the challenges we face require responses in the economy and policy sphere that have not gone far enough.

And we should expect to have some continued weak sectors in Singapore, according to regional economist, Wong Keng Siong from the Bank of Toyko-Mitsubishi in Singapore.

WKS: I think there are two sectors that are not going to do particularly well this year. Firstly, construction. Competition in the construction industry is still depressed because there isn't a lot of projects coming up. Secondly, in the electronics sector, like it or not, the electronic is highly cyclical, and this year, we

are heading into a cyclical downturn for the industry. And so the prospects for electronics will not be so good in 2005.

Manu Baskaran from Centennial group also explains the downward trend.

MB: The best set of indicators is the one devised by the OECD, and the picture is constantly and consistently pointing down. So it has a good record of predicting US GDP. As far as what this means to Singapore is concerned, if you have a situation where economic growth is going to weaken, and that creates uncertainty in the minds of businesses, then the thing that is of most importance, is demand for the electronic components that dominate our manufacturing and export sectors. If you are a businessman thinking about making a big investment in some kind of new capital investment that is what drives demand for electronic components because a lot of these machinery, plants, and equipment today have a lot of electronics in it. Now, if businesses become uncertain for a variety of reasons, and they want to defer the investments for a year or two, then that will come through and translate into lower demand for IT in Singapore.

Despite that, Singapore can look forward to other industry up-swings in 2005, Wong Keng Siong from the Bank of Tokyo-Mitsubishi.

WKS: We have to look at industries in terms of relative attractiveness this year because generally, prospects will look generally less rosy compared to 2004. The industries which I think should do well should be those that can leverage on domestic demand and regional hub services, this would include financial services, not because we are in the industry. But the financial services sector this year should be able to see fairly decent loans performance because the domestic economy is showing signs of recovery and especially in the key property sectors. Domestic demand will see some improvement because job growth is fairly decent or has been fairly decent, and unemployment is coming off, which means that domestic confidence will continue to pick up. In terms of external demand, the financial services sector, I mean we are a hub in terms of regional financial services and there is a fair bit of demand in the region in financing needs, when their economies recover, when they need to put infrastructural projects back on line. This will require expertise in which Singapore is in a position to provide.

On the global economic scene, Manu Baskaran highlights the recent spate of geo-political risks and fears of uncertainty.

MB: The US twin deficits, the lackluster growth in the Euro-zone economies and in Japan, housing bubbles in many economies, particularly in the UK and Australia. Second, you have the geo-political risks in the Middle East. You know, the news about the tsunami has hogged the international news of late, but if you have been following the situation in Iraq, it is quite clear that there is a significant deterioration in the security situation there. Now, these highlight the potential risks politics can pose for the economy because the Middle East, Iraq, Iran and Saudi Arabia, really that's why the bulk of the world's oil is produced and transported.

Another global economy that is of great concern is China, which has been courting massive investments.

MB: I think if you look at the underlying factors, the risks are still too high, certainly too high for us to declare that China has succeeded in pulling off a soft landing. And the heart and guts of the problem is what has driven the Chinese economy over the last few years has been a massive investment binge that has brought the ratio of investment to GDP to above 45%. I know of no economy in recent history that has driven investments to those levels and not seen a recession or some kind of economic shock thereafter. The reason this happens is because, when you have so much investment it creates excess supply. And excess capacity means that businesses will look around and not want to invest when there are so many plants and capacity around. What will happen is as excess capacity build up, the guys who are producing stuff find that there's so much competition, their pricing power weakens, their operating margins weaken, and they start to lose money, and their cash flows are not strong enough to help repay their loans.

And how will China cope with uncertainties in its economy? Manu Baskaran.

MB: A lot of these investments have been funded by loans, in a credit culture that is still highly questionable. So the combination of a weak financial system, excess capacity and all the stresses and imbalances in the Chinese economy leads me to question if China can put it off easily. If China were to experience slower growth and a series of shocks, there will clearly be an impact on the Asian economies that have enjoyed rising exports to China. Now, as far as Singapore and South East Asia are concerned, I think about half of its exports are to feed the export orientated factories in China. So exports go to China, process again, goes out to meet final demand in Japan, Europe and the US. So that part of demand from China should be alright. But the other half will be affected and what affects Singapore more is the second round effects because our trading partners who benefited from China's growth will be hit and their demand for our stuff will also be hit.

Manu Baskaran, Head of Research at Centennial Group in Singapore ending this edition of Business Ideas. Join me at the same time, next week. I'm Melanie Yip for Radio Singapore International.