INTERNATIONAL MONETARY FUND

Staff Country Reports

April 2005
Corrected: May 2005
IMF Country Report No. 05/141

Singapore: 2004 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Singapore Authorities

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2004 Article IV consultation with Singapore, the following documents have been released and are included in this package:

- the staff report for the 2004 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on November 8, 2004, with the officials of Singapore on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on January 21, 2005. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its February 7, 2005 discussion of the staff report that concluded the Article IV consultation.

- a statement by the Singapore Authorities.

The document listed below has been or will be separately released.

Selected Issues Paper

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

To assist the IMF in evaluating the publication policy, reader comments are invited and may be sent by e-mail to publicationpolicy@imf.org.

Copies of this report are available to the public from

International Monetary Fund • Publication Services
700 19th Street, N.W. • Washington, D.C. 20431
Telephone: (202) 623-7430 • Telefax: (202) 623-7201
E-mail: publications@imf.org • Internet: http://www.imf.org

Price: $15.00 a copy

International Monetary Fund
Washington, D.C.

This page intentionally left blank

INTERNATIONAL MONETARY FUND

SINGAPORE

Staff Report for the 2004 Article IV Consultation

Prepared by Staff Representatives for the 2004 Consultation with Singapore

Approved by Masahiko Takeda and Juha Kähkönen

January 21, 2005

- The 2004 Article IV consultation discussions were held in Singapore during October 26–November 8. The team comprised Messrs. Aziz (head), Nakabayashi, Dell'Ariccia, and Jang (all APD), and Ms. Amiti (RES). Mr. Takeda (APD) participated in discussions with senior officials during November 5–8.

- The mission met with Senior Minister Goh Chok Tong, who also serves as the Chairman of the Monetary Authority of Singapore (MAS), Second Finance Minister Raymond Lim, other senior officials, and representatives of the private sector.

- At the conclusion of the 2003 Article IV consultation in March 2004, Directors commended the authorities for their pragmatic use of countercyclical policies in response to the SARS outbreak in 2003. Directors noted the need to advance structural reforms to enhance the economy's competitiveness and growth prospects, and supported the authorities' ongoing reform efforts. Directors encouraged the authorities to enhance fiscal transparency and implement the Financial System Stability Assessment (FSSA) recommendations.

- Singapore provides data to the Fund generally on a timely basis, and is in observance of the Special Data Dissemination Standard (SDDS).

- Singapore has accepted the obligations of Article VIII, Sections 2, 3, and 4. It maintains an exchange system free of restrictions on payments and transfers for current international transactions.

- Last year, Singapore published for the first time the Article IV staff report. The authorities informed the mission that they will make a decision on whether to publish this year's staff report closer to the Board meeting.

Contents

EXECUTIVE SUMMARY

State of the Economy

Singapore's economy has recovered rapidly since mid-2003, having weathered a series of adverse shocks since the Asian crisis. Lately, job creation has gathered strength. This turnaround owes much to a favorable external environment, supportive macroeconomic policies, and continued structural reforms. Inflation has crept up, but remains contained. With the softening in global demand, particularly the cresting of the world electronic cycle, growth could slow to about 4 percent in 2005, close to potential. There are risks to this outlook, especially on the external front.

Policy Stance

With the improvement in economic conditions, both monetary and fiscal policies have focused on orderly and gradual withdrawal of the stimulus provided in the recent past.

Discussions

Against this background, policy discussions centered on the appropriate stance in the uncertain environment to support growth while keeping inflationary pressures under check. On the structural front, the discussion focused on assessing progress on planned reforms and the direction of new initiatives to enhance Singapore's competitiveness.

- The current tightening of monetary policy is appropriate as there is little slack in the economy. The labor market has tightened and real wages are set to rise. This, along with high energy prices, could push up inflationary pressures moderately. However, if the slowdown appears to be more severe, then monetary policy may need to become supportive. This year's higher-than-expected growth has provided room to cut the personal income tax rate and further strengthen the existing social safety net in next year's budget.

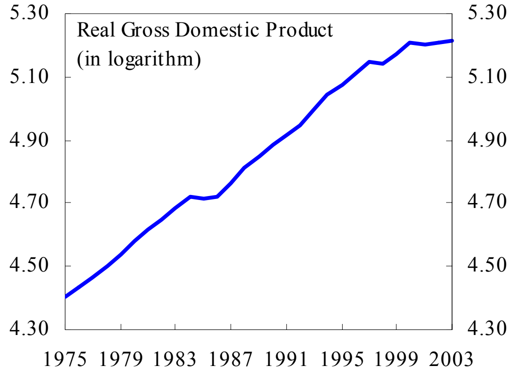
- Medium-term prospects depend on the strength of new engines of growth in the face of competition from regional economies. A wide range of structural reforms is being implemented to enable new sources of growth to take hold. The government is negotiating bilateral free-trade agreements with neighboring countries. Several schemes have been put in place to retrain and upgrade skills of the unemployed in response to the rise in long-term unemployment.

- The financial sector remains robust. Bank profitability and capitalization are strong. Progress has been made in implementing many of the FSSA recommendations.

I. Introduction

1. **In last few years, Singapore's economy has been hard hit by a series of external shocks**. These shocks—the Asian crisis, the bursting of the technology bubble, and the SARS outbreak in 2003—have disrupted an economic expansion largely uninterrupted since the 1970s. In the latest downturn, output contracted at an average (annualized) quarterly rate of 3¾ percent between Q3 2002–Q2 2003. Over the next four quarters, the economy recovered rapidly, buoyed by strong global demand, supportive monetary and fiscal policies, and structural reforms.

A series of external shocks has slowed growth in recent years.



2. **Ongoing structural changes have complicated adjustment to these shocks**. Competitive pressures from regional low-cost economies have pushed Singapore's manufacturing sector to restructure and diversify. The services industry is also undergoing changes. Partly reflecting this restructuring, the unemployment rate has remained above its historical average, despite the recovery.

3. **To facilitate an orderly adjustment to these changes, a wide range of structural reforms has been undertaken in the past few years**. These reforms include changing the tax system to reduce business costs; increasing wage and labor market flexibility; liberalizing the banking, telecom, and utility sectors; enhancing the financial regulatory and supervisory framework; and negotiating free-trade agreements with major trading partners.

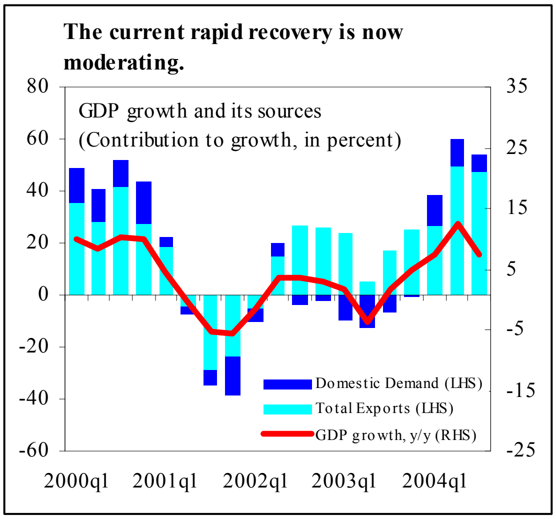
4. **Amidst these economic changes, last August the country witnessed its second leadership transition since independence**. Lee Hsien Loong, son of independence leader Lee Kuan Yew, became the new Prime Minister. He retained the finance portfolio, but was replaced by former Prime Minister Goh Chok Tong as the head of the Monetary Authority of Singapore (MAS). The new cabinet contains few changes, signaling policy continuity. The ruling People's Action Party, in power since independence, remains firmly in control with an overwhelming majority in Parliament.

5. **In recent years, the Executive Board has broadly endorsed the government's macroeconomic policies and structural reforms**. The authorities' pragmatic use of countercyclical policies over the past few years has been supported by the Board. The MAS has implemented many of the recommendations of the FSSA that was concluded last April, and has taken steps to enhance the transparency of the monetary policy framework. While endorsing the government's structural reform agenda, the Board noted that the divestment of the government-linked companies (GLCs) has been somewhat gradual. On certain other issues, the authorities' views have diverged from those of the staff and the Board. For example, on fiscal policy, the authorities have proceeded more cautiously to expand the

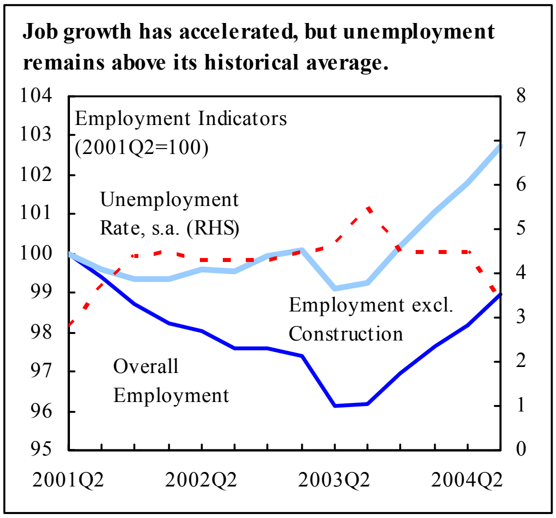
social safety net despite large reserves. This partly reflects their concerns over the vulnerability of the economy to a dilution of investor confidence, if such measures were viewed as large liabilities constraining the government's ability to strengthen Singapore's competitiveness in the future.

II. Recent Developments

6. **The frenetic pace of the recent recovery has now begun to slow**. The recovery—mainly driven by exports, reflecting strong global electronics demand, and since early 2004 supported by domestic investment—delivered an unprecedented four straight quarters of double-digit growth from Q3 2003 to Q2 2004. In Q3 and Q4 2004, the pace slackened markedly as electronics exports and consumption slowed. For the year, growth is expected to reach around 8 percent in 2004, recovering from 1.1 percent in 2003.

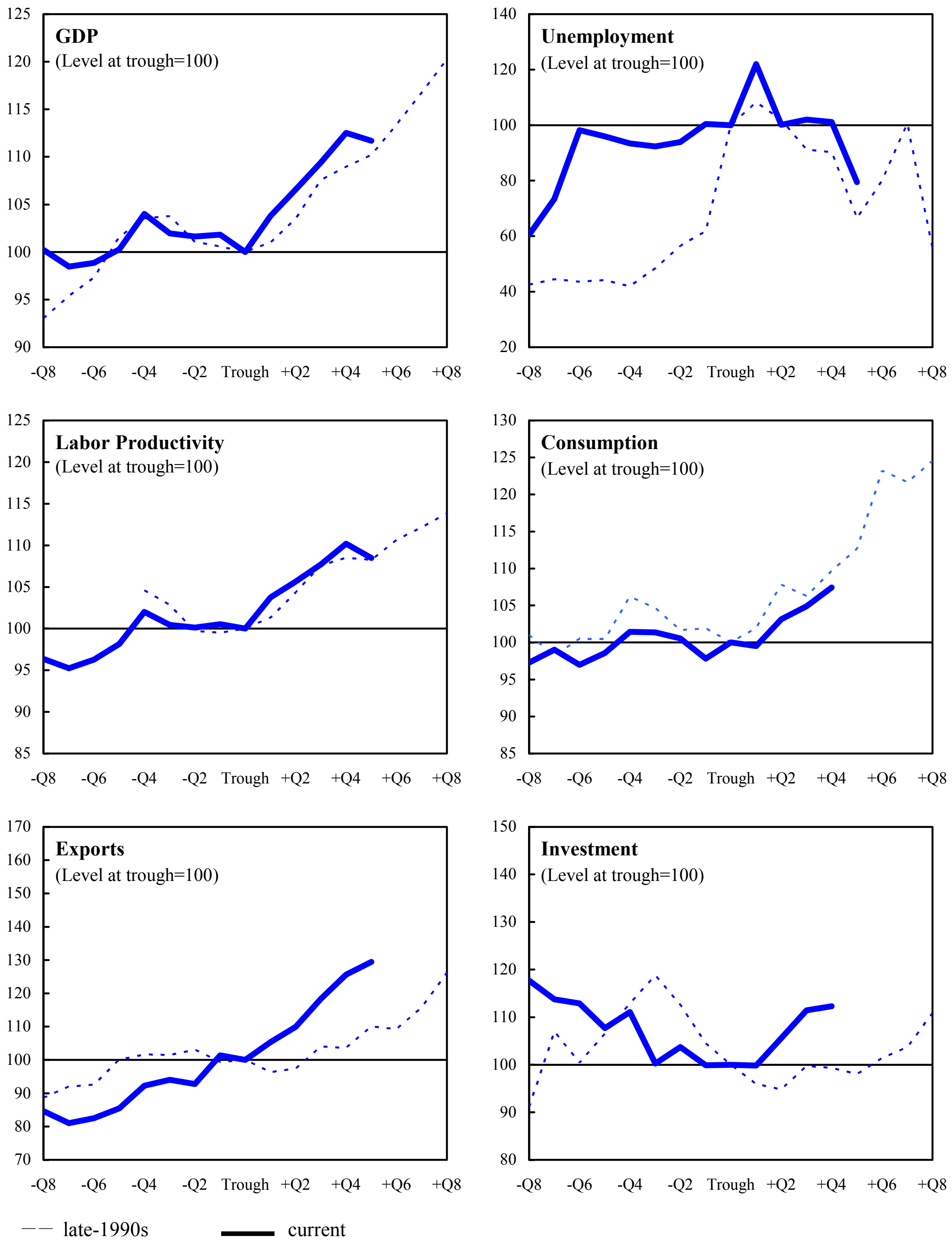


7. **Over the recovery, employment growth increasingly gathered strength**. The unemployment rate has fallen from its 17-year high of 5½ percent in Q3 2003 to 3½ percent in Q3 2004, but still remains above its historical average of around 2 percent. Construction job losses have continued as the sector has remained on a declining trend that began in 1999. Long-term unemployment among the unskilled has also emerged. Rapid productivity growth has so far outstripped real wage increases, resulting in a substantial decline in labor cost. The National Wages Council, made up of representatives from employers, the unions, and the government, has recommended moderate wage increases for 2004/05, the first proposed rise in three years.



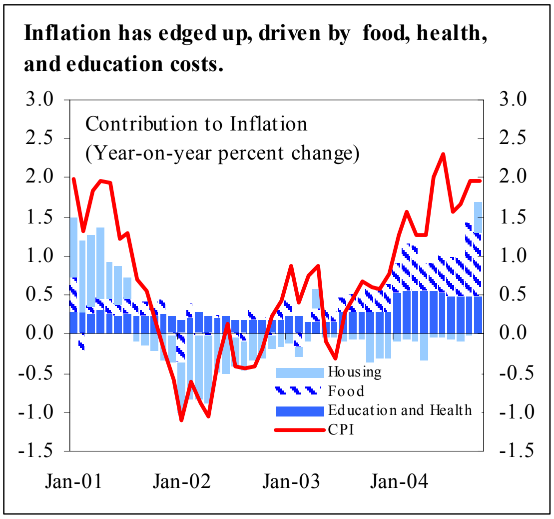
8. **Inflation has crept up, but remains low**. The CPI rose by 1.7 percent in the first ten months of 2004, led by rising education, health, and food costs. The rise in global oil prices has had only a modest effect as retailers cut back on profit margins and because of the

The current recovery has been stronger, with higher export and investment demand, than in the post-Asian crisis period.



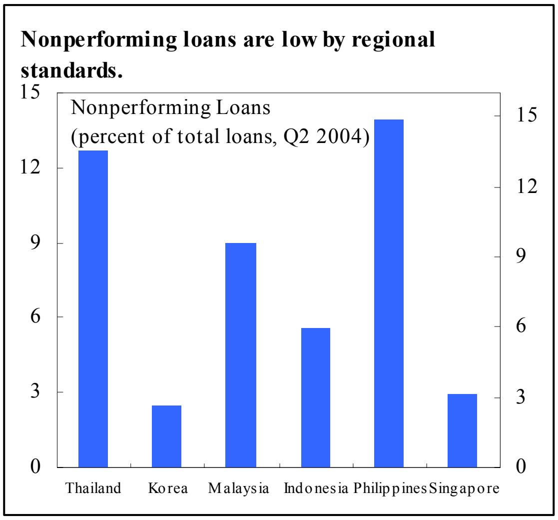
Source: CEIC, Singaporean authorities, and Fund staff estimates.

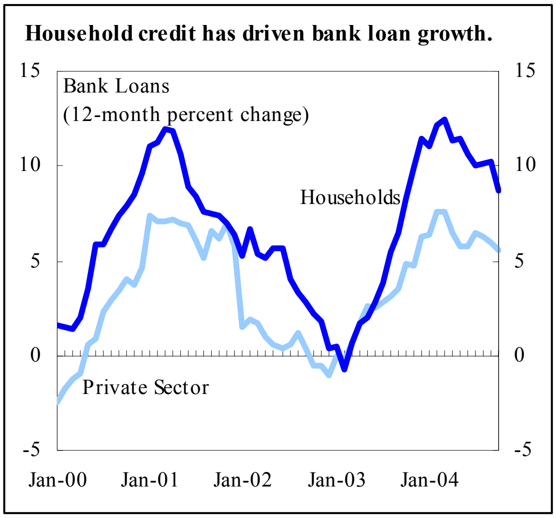
relatively low weight of oil-dependent goods and services in the consumption basket. An increase in the goods and services tax (GST) rate from 4 percent to 5 percent in 2004 was an added one-off factor, contributing an estimated 0.4 percentage points to the CPI.



9. **Despite strong exports, the current account surplus narrowed in the first three quarters of 2004, reflecting higher imports as investment picked up**. Although outward investment remained strong, official reserves rose by US$14 billion (US$110 billion at end-November covering 6 months of imports).

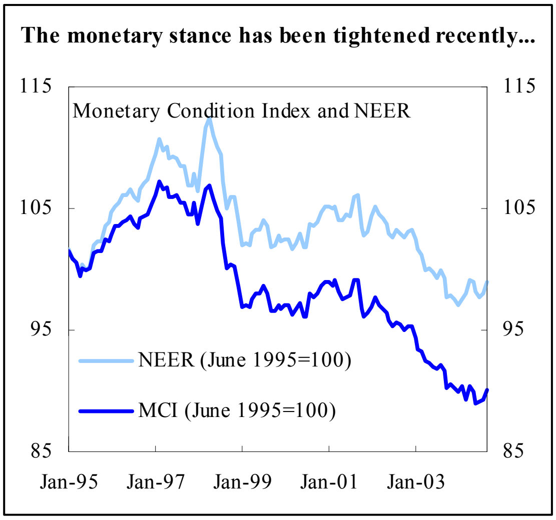
10. **The corporate and financial sectors remain strong**. The corporate sector is profitable with low debt-to-equity ratios. Domestic banks are well capitalized with rising non-interest earnings and low nonperforming loans. With ample liquidity, bank lending has risen since mid-2003 mainly due to growing household credit. However, growth in corporate credit has been anemic, with firms relying on internal savings and bond issues to finance investments. Stock prices have risen in line with regional trends and new issuance of equity has increased. The property price deflation appears to be bottoming out.

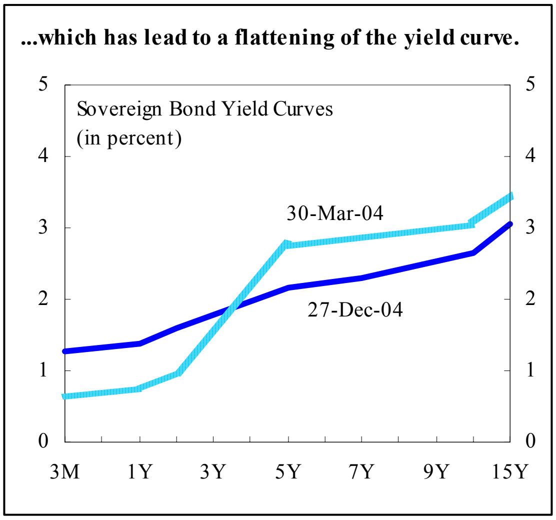




11. **On the policy front, the MAS announced a modest and gradual tightening of its monetary stance in April, and maintained this position in last October's policy review**. Operationally, the MAS shifted the "zero appreciation" path of the nominal effective

exchange rate (NEER) adopted in mid-2001 to a modest and gradual appreciation, citing a firming up of inflationary pressures.[1] After having depreciated by 6½ percent since 2001, the NEER (as calculated by IMF) appreciated modestly in Q3 2004, but reverted to its pre-April announcement level toward end-2004. The yield curve has flattened and the SGD-USD SIBOR discount has widened.





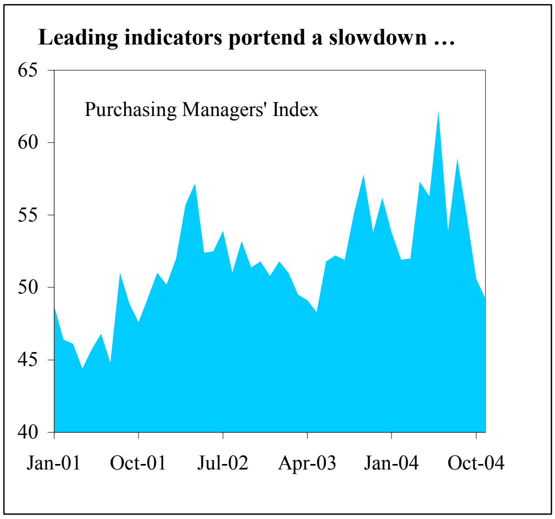
12. **The current fiscal stance is broadly neutral.**[2] Last year, the fiscal surplus was over 6 percent of GDP, higher than expected due to lower-than-budgeted capital spending. This year's budget also plans on large capital spending, which combined with an increase in the GST rate, aims at keeping the fiscal stance neutral.

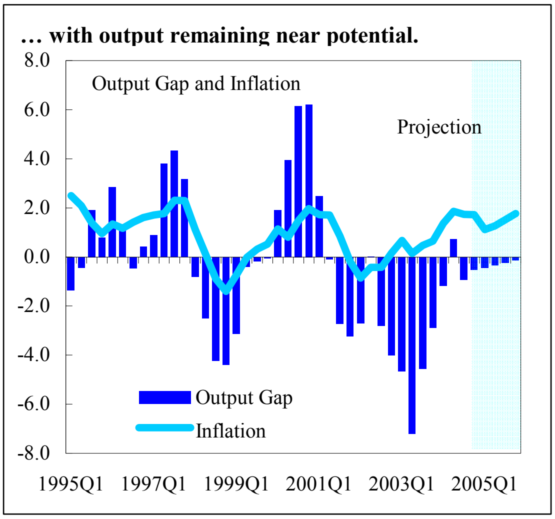
III. Economic Prospects and Risks

13. **Looking ahead, staff expects activity to moderate to more sustainable levels in the near term**. The softening in global demand, particularly the cresting of the world electronic cycle, could slow GDP growth to about 4 percent in 2005. Leading indicators such as purchasing managers' index (PMI) also point in this direction. Domestic demand will play a larger contributory role, including through a restocking of inventories, which were depleted in the recovery. Despite the moderation in activity, there is likely to be very little slack in the economy going forward, reflecting the recent rapid growth. With the labor market tightening, real wages are also set to rise to catch up with the productivity gains. These factors, along with high energy prices, will raise inflationary pressures. Under the present monetary stance, however, inflation should remain within 2 percent. As export growth slows and investment increases, the current account surplus should narrow.

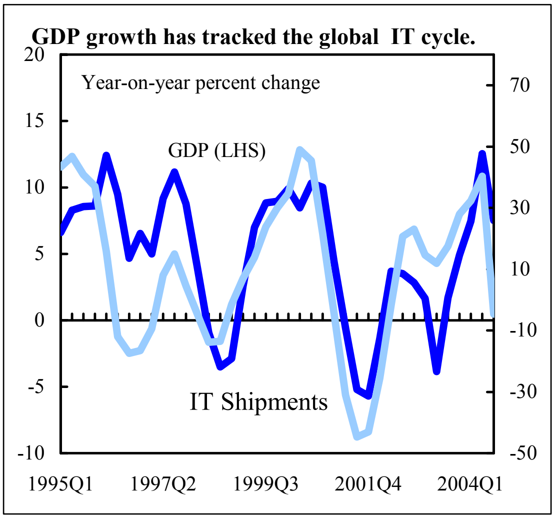
[1] Singapore's monetary policy is based on the management of a trade-weighted exchange rate within an undisclosed band, with the primary objective of maintaining price stability.

[2] This is based on staff calculation of the fiscal impulse. Singapore's fiscal year runs from April–March.





14. **This outlook is subject to some uncertainty, especially on the external front**. Much will depend on how world demand reacts to the volatility in oil prices, on the extent of the downturn in the global electronics cycle, and on the level of activity in China.[3] Geopolitical tensions and security threats also pose risks. If these risk factors materialize, growth could be lower. Nevertheless, given Singapore's strong external and fiscal positions and resilient financial system the risk of a crisis is low (Table 5).[4] On the domestic front, recent employment gains and sizeable cyclical increases in corporate profits could portend stronger consumption and investment growth.

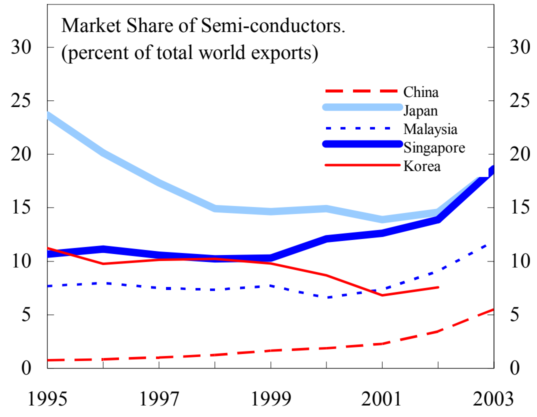


[3] On current forecast, global semiconductor sales are expected to remain flat in 2005 after growing by nearly 30 percent in 2004. GDP growth in US, the Euro area, and China are also expected to fall. Estimates suggest that a 10 percent decline in the semi-conductor sales growth can reduce GDP growth by 1 percentage point. Exposure to U.S. demand is large. Direct exposure to China has grown in recent years, but is still relatively modest. However, the combined exposure to Indonesia, Malaysia, and Hong Kong SAR—economies that are in turn affected by activity in China—is significant.

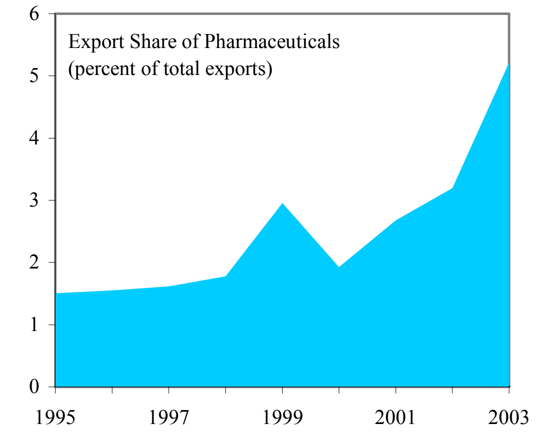
[4] Public finances have been in surplus for the last two decades, and the government has accumulated a substantial net asset position, estimated at about 120 percent of GDP at end-March 2004. Singapore does not have any external public debt. The outlook for the fiscal and external current account position remains favorable.

15. **The medium-term outlook hinges on how effective recent reforms will be in establishing new areas of growth**. In response to increasing competition from low-cost regional economies, the authorities have undertaken a wide range of reforms to diversify the economy and make it more competitive. The manufacturing sector is moving up the quality ladder, market share of electronics exports has increased, and new industries, such as pharmaceuticals, are expanding rapidly (Box 1). Singapore's role as an international hub for goods and services is also expanding, with both financial and trading sectors diversifying into new businesses. Competition with Hong Kong SAR remains strong, but Singapore has continued to strengthen traditional business ties with countries in its neighborhood (Indonesia and Malaysia), while venturing into new markets like Australia, China, and India, and specializing in niche financial fields, such as Asian dollar transactions. Accordingly, the staff expects growth over the medium term to average 4–5 percent, while the current account surplus should narrow as investment recovers from its recent low levels.

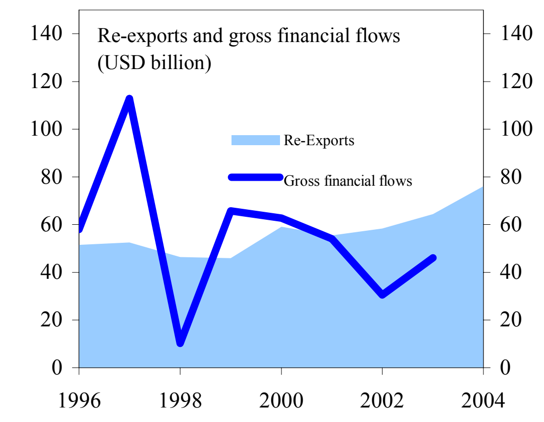
Singapore's market share of semi-conductors has increased.



Pharmaceuticals are expanding.



International hub business is also increasing.



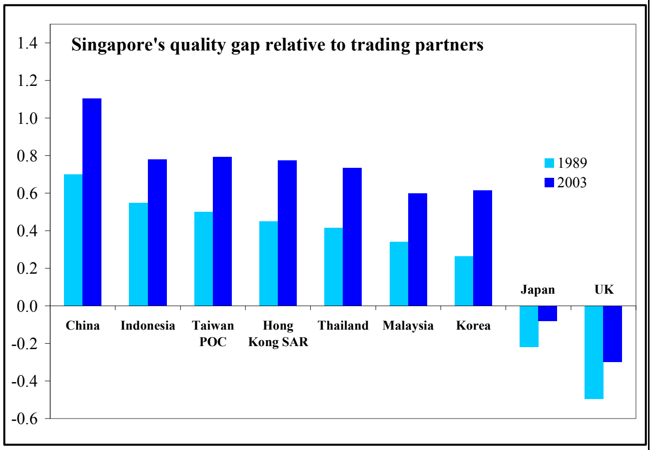
IV. Policy Discussions

16. **Policy discussions took place against the backdrop of improved economic conditions and substantial progress on structural reforms**. The authorities agreed with the staff's assessment of near-term uncertainties, and added disorderly adjustment to the global current-account imbalance to the list of risk factors. Discussions, thus, centered on the appropriate policy stance in this uncertain environment to support growth while keeping inflationary pressures under check. On the structural front, the discussions focused on assessing progress on planned reforms and their early impact, and the direction of new initiatives to further enhance Singapore's competitiveness.

BOX 1. IS SINGAPORE MOVING UP THE QUALITY LADDER?[1]

With increased competition from low wage countries in the region, Singapore is searching for different ways to stay competitive. It is more difficult for advanced economies like Singapore to compete on wages, and since they are probably already close to the technology frontier in many products, large productivity improvements are likely to be infrequent. One avenue, which Singapore has successfully followed, is to diversify its production into technologically advanced industries, like bio-chemicals and pharmaceuticals. Another way, which is a little harder to identify, is to upgrade the quality of products in existing industries. Although less attention has been directed at quality upgrading, it remains an important means of maintaining competitive edge.

Measuring quality differences in products is generally difficult. One approach is to use differences in prices as an indicator of quality differences. This approach is feasible provided data is sufficiently disaggregated such that one is comparing like with like. If this is the case, then price differences indeed pick up quality differences rather than simply compositional differences. The U.S. provides highly disaggregated bilateral trade data, which for some countries includes more than 10,000 products for any given year. We assume that given its competitive product markets the U.S. would not be willing to pay a higher price for a product from Singapore than the same product from, say, China unless it was of higher quality. Using data between 1989 and 2003 a number of interesting results emerge from the exercise:



- Singapore produces higher quality manufacturing goods, on average, compared to its low-wage competitors. However, Singapore's average quality is lower than more technologically advanced countries like Japan and the U.K.

- The quality gap has increased relative to its low-wage competitors. Relative to China, this has increased from 70 percent in 1989 to 110 percent in 2003.

- Although the average quality of Singapore's products is still lower than that of Japan and the U.K., the size of the quality gap has narrowed.

Thus, these results suggest that Singapore is successfully moving up the quality ladder. This is a very encouraging sign for its future growth prospect. By differentiating its products from its low-wage competitors, exports can continue to be a key driver of high growth rates in the period ahead.

---

[1] For details see Chapter I of the accompanying *Selected Issues* paper, prepared by Mary Amiti.

A. Near-Term Policies: Treading a Cautious Path

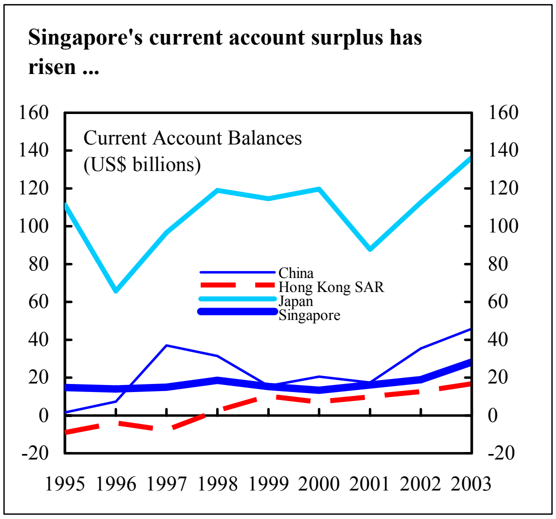
17. **With little slack in the economy going forward, the staff supported MAS's announced monetary policy tightening**. Although inflationary pressures were likely to be moderate, the announced tightening would pave the way for an orderly and gradual withdrawal of the stimulus provided in recent years to support growth. That said, in the staff's view, monetary policy needed to become more supportive, perhaps even ahead of the scheduled policy review in April 2005, if the downside risks to the outlook became ominous. The authorities responded that if the need arose they would change policy between the bi-annual reviews, as was done after September 11, 2001. They also noted that the band around the target NEER path provided some room to accommodate unexpected developments in the economy.[5] The authorities did not consider a possible increase in exchange rate flexibility in regional currencies, particularly in the renminbi, as complicating their monetary policy given that they already use a trade-weighted exchange rate as an intermediate target.

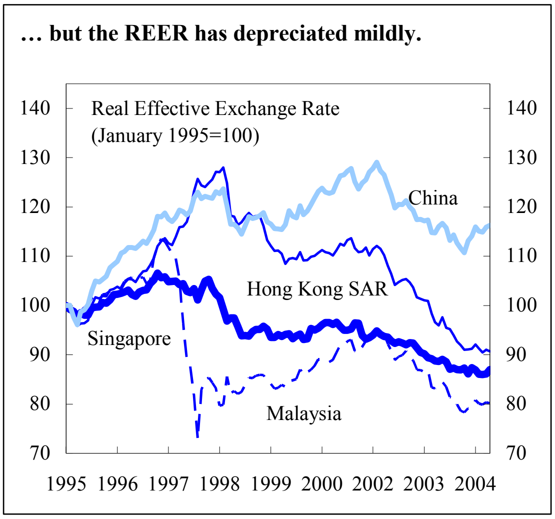
18. **The mission welcomed MAS's ongoing efforts to increase the transparency of its monetary policy framework**. These efforts have been well received by market participants and have helped strengthen policy credibility. In recent years, MAS has published its Monetary Policy Statement, and disseminated operational information and data on money market transactions. Nevertheless, the trade-weighted exchange rate index and the policy band, together with its central rate, are not published. The MAS has contended that this deliberate "translucence" prevents the market from testing the trading band and allows them to correct policy mistakes without severely disrupting the economy. This practice does not appear to have impaired credibility, as evidenced by the low and stable inflation rate over almost ten years, despite several large shocks to the economy during the period.

19. **The authorities and the mission discussed factors behind the surge in current account surpluses in recent years, including the possibility of real exchange rate misalignment**. The current account surplus has more than doubled from around 14 percent of GDP in 2000 to nearly 31 percent of GDP in 2003, although it is expected to moderate somewhat this year. Despite the relatively small size of the Singapore economy, the absolute level of these surpluses is significant. Over this period, the real exchange rate depreciated by about 8 percent.

---

[5] The MAS does not make explicit either its inflation or NEER targets, but past behavior suggests that monetary policy is well approximated by a Taylor rule that puts 80 percent weight on the deviation of the 9–12 month ahead expected inflation from a "target" inflation rate of 2 percent, and 20 percent weight on the output gap. The appropriate level of the NEER is then set based on estimates of direct and indirect pass-through effects of changes in the NEER on inflation and growth. Based on this analysis and the current outlook, staff estimates that another 1–1½ percent appreciation of the NEER is needed to keep the 9–12 month ahead inflation under 2 percent. This appreciation will likely be spread over the next 3–6 months.





20. **The MAS considered both the surge in the current account surplus and the current level of the real exchange rate to be in line with fundamentals**. They noted that the spike in the current account surplus reflected households' and the corporate sector's market-based response to the increased uncertainty in recent years. In response to adverse external shocks to the Singapore economy, investment had been reduced domestically (by over 18 percentage points of GDP) and increased abroad to take advantage of the relatively better opportunities and higher returns overseas.[6] Going forward, the authorities and the mission agreed that the current account surplus was likely to decline as economic prospects stabilized, but would remain fairly high given Singapore's demographics.[7] On the issue of real exchange rate misalignment, the authorities pointed to the study published in its most recent Macroeconomic Review, which found the REER to be broadly in line with its equilibrium level.[8]

21. **The staff cautioned that the large current account surpluses was not fully explained by private sector behavior**. The government and GLCs are major contributors to domestic savings, and how they allocate resources between domestic and foreign investment is an important factor in the determination of the exchange rate. Their active investment abroad may have alleviated upward pressures on the real exchange rate despite the high current account surpluses. However, the staff noted that there were no perceptible signs of a

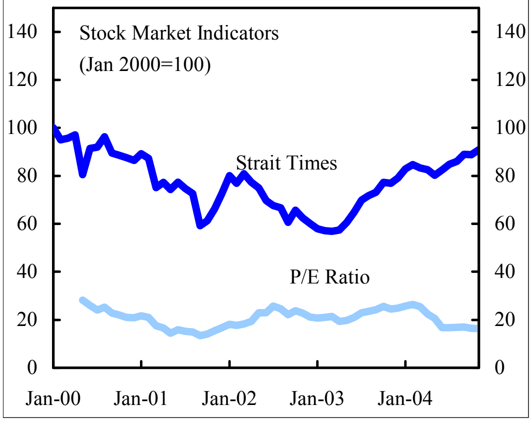
[6] Much of Singapore's high saving is undertaken by corporations (including those by GLCs) at around 25–30 percent of GDP, partly reflecting the large share of profits in national income Central government saving has averaged around 9 percent of GDP during this period. Household saving rate is comparable to international levels at around 8–10 percent of GDP, of which net saving through the mandatory saving program (CPF) accounts for only around 2½ percent of GDP.

[7] See Chapter V, Singapore: Selected Issues, IMF Staff Country Report No. 00/83 on the close relation between Singapore's saving rate and population dynamics.

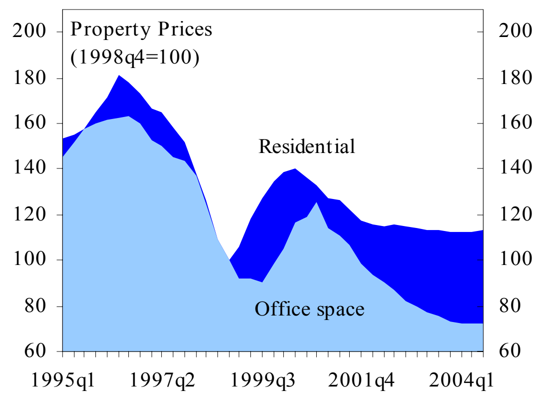
[8] According to this study, the 10–12 percent lower REER compared to its pre-1998 level largely reflects the decline in real estate prices and worsening terms-of-trade, partially offset by the rise in net foreign assets.

major real exchange rate misalignment in commodity or asset prices at present—inflation was stable and low, while neither the equity nor the real estate market showed signs of overheating. In addition, the present intended tightening of monetary policy would keep the NEER on an appreciating path, helping to reduce Singapore's current account surplus and contribute to the orderly adjustment of the global current account imbalance.

Equity prices have risen, but the P/E ratio has been stable.

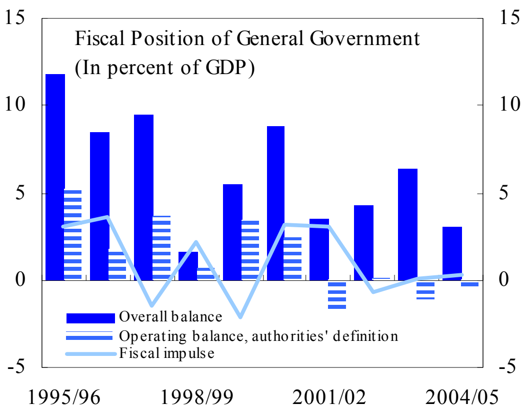


Property prices have declined.



22. **The mission commended the authorities for the judicious use of fiscal policy to support the economy**. After providing substantial support in the early 2000s, fiscal policy has remained broadly neutral. This year's budget also contained several measures to support private enterprise and to attract investment, particularly in the wealth management industry.

The fiscal position has been in surplus over the years.



23. **The FY2005/06 budget process is still in its early stages**. Staff projections indicate that this year's fiscal outturn could be better-than-budgeted by ⅓ percent of GDP due to the cyclical improvement in revenue. This would provide room to cut the top personal income tax rate to 20 percent from 22 percent to restore parity with the corporate tax rate and further strengthen the existing social safety net (such as by increasing medical benefits to the elderly) in the FY2005/06 budget, without straining the medium-term balanced budget objective. The authorities noted that several measures, including strengthening social assistance, were under consideration.

24. **The authorities are seeking ways to fortify the automatic stabilizers to reduce reliance on discretionary measures as a countercyclical tool**. To this end, they are considering changing the basis of tax assessment to current-year income from the existing practice of previous-year income. The mission supported this change, but the authorities noted that the reaction from corporates had not been positive in view of the perceived

increase in compliance costs. The authorities are also considering treating *ex ante* spending limits on certain categories of spending and transfers more flexibly to improve their response to cyclical changes.

25. **The government considers its high level of fiscal reserves to be a crucial factor underlying the strong investor confidence in Singapore**. If faced with competitive pressures in the future, these reserves assure investors that the government has sufficient funds to finance tax cuts and infrastructure spending. The reserves also provide a buffer against rising health costs as the population ages. The mission observed that without compromising this insurance need, the government could leverage its fiscal strength to provide some additional assistance to the long-term unemployed and retirement benefits targeted to low-income earners. The authorities, however, were unwilling to introduce any entitlement program at this juncture and considered retraining and job-matching schemes that improved employment opportunities to be better suited to provide social insurance. For the medium term, the authorities intended to continue formulating policy within the existing budgetary framework.[9] The staff noted the merits of this rules-based system and suggested that the present 50-percent limit on the use of yearly investment income, which appeared somewhat arbitrary, could be reviewed against Singapore's future revenue and spending profiles. The authorities responded that while they were always seeking ways to improve the fiscal framework, this limit was important to safeguard the reserves.

26. **The staff welcomed the first public review of Temasek's operations—the government holding company in charge of all SOEs** (Box 2). The review indicates that Temasek's portfolio is well diversified across sectors and countries. Following Temasek's example, the staff suggested that the government could also consider publishing, without disclosing sensitive details, the aggregate assets of Government of Singapore Investment Corporation (GIC), the broad elements of its portfolio, and its overall returns. The authorities, however, argued that GIC operations remained strategic and there was sufficient internal oversight to ensure its proper functioning. They did not see any benefit of disclosing the market value of GIC's assets, since they were not burdened with debt and thus did not need to build investor confidence on this front. They were also reluctant to compile consolidated public sector accounts on the grounds that individual entities were audited under Singapore law and their accounts were available publicly. The authorities agreed, in principle, to participate in the fiscal ROSC exercise, but needed to better understand the resource costs before committing to a timetable.

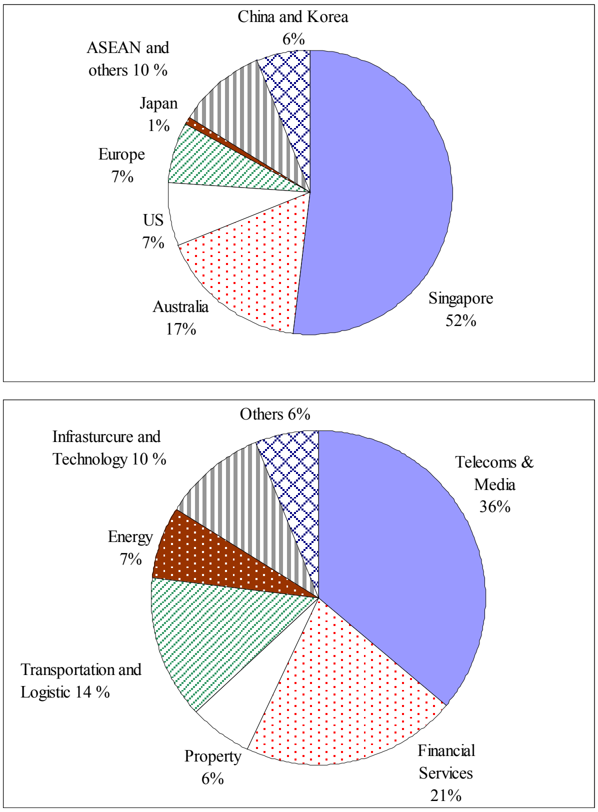
[9] This framework (made up of both formal rules and established practice) calls for the government to maintain a balanced budget over the election cycle. Any surplus over the cycle is transferred to the reserves, while deficits can be financed by the reserves only with the consent of the President, who is elected independently of the government. Within each year, the government can use only up to 50 percent of the investment income.

Box 2. Temasek

The government of Singapore owns interests in various enterprises, both locally and abroad. These investments have been managed by the government's holding company Temasek, incorporated in 1974. It manages a portfolio of about US$53 billion (55 percent of GDP) roughly equally divided between domestic and foreign investments and spread across a wide range of industries, including holdings in local industry leaders such as Singapore Airlines, Singtel, and DBS. Temasek companies (TCs) account for some 13 percent of Singapore's GDP. The holding company's performance has been respectable with a total shareholder's return of 18 percent per annum over the past 30 years, although, partly due to the Asian crisis, returns have been lower, 3 percent to 6 percent, in the last 5–10 years.

Temasek's success stands out in contrast to the generally held view that state-controlled enterprises are unprofitable and inefficient. Temasek attributes this success to its corporate governance framework which allows its management and board of directors to run the company without extensive interference from the government. Temasek's board is directly accountable to the President of the Republic, who is elected separately from the Prime Minister, the head of the government. The President approves the appointment and removal of board members and the CEO.

Temasek's holdings cut across sectors and countries.



Source: Temasek Review 2004

Notwithstanding this success, concerns have been raised that the presence of TCs in certain sectors may be hindering private participation. This is recognized in the recently published Temasek's charter which directs it to divest its non-strategic holdings without, however, setting a time frame. Several Temasek's holdings are also a legacy of state-led development policies of the past. Nevertheless, a stronger commitment to exit from sectors where the private sector can be an effective alternative will help to dissipate concerns that TCs crowd-out private entrepreneurship.[1]

While listed TCs are subject to the rules of disclosure imposed by the Singapore Exchange, Temasek itself is not listed and is not required to publish or disclose its financial accounts. Thus, the recent publication of the company's charter and review represents a welcome move toward greater transparency. In the coming years, transparency will assume even greater importance as Temasek expands its operations overseas.

[1] For example, there is evidence that TCs are rewarded in financial markets with a positive premium relative to private companies (see C. Ramirez and L. Tan, *Singapore Inc. versus the Private Sector: Are Government-linked Companies Different? IMF Staff Papers Vol. 51 No. 3, 2004*).

B. Medium-Term Issues: Searching for New Engines of Growth

27. **The authorities underscored that economic prospects over the medium term depended on the strength of new engines of growth**. Regional economies, particularly China and India, had been eroding Singapore's traditional advantages by their increased openness and low-cost structure. Thus, to "remake Singapore" in response to these challenges, the government adopted the recommendations of the Economic Review Committee (ERC) in 2003. The ERC recommended measures to enhance competitiveness, promote private entrepreneurship, and facilitate economic diversification (Table 7). The authorities explained that significant progress had been made to increase wage flexibility, reduce business costs, and promote the outward expansion of domestic firms and Singapore as a business hub.[10] The mission noted that it would be important to evaluate the impact of these reforms and review the need for new ones.

28. **The mission encouraged the authorities to accelerate their planned divestment of GLCs**. The government has been a major player in Singapore's development, delivering a remarkable economic transformation since the mid-1960s. Nevertheless, looking ahead, the ERC envisioned a greater economic role for the private sector and recommended divesting GLCs to provide room for entrepreneurship. In this regard, the authorities felt comfortable with the present measured pace of divesting GLCs on a case-by-case basis. On a related issue, some private sector observers expressed concern that competition may be stifled by the extensive presence of GLCs in certain sectors of the economy. The authorities acknowledged the presence of such an impression in some quarters, but stressed that effective firewalls separated the legislative, regulatory, and participatory roles of the government. The staff hoped that the newly legislated Competition Law would help allay to some of these concerns, but urged the government to review sector-specific competitive conditions.

29. **Singapore has sought out new markets through bilateral free trade agreements (FTAs) in recent years**.[11] The authorities explained that their bilateral FTAs (which they considered to be consistent with WTO principles) were accelerating the momentum of trade and investment liberalization, thereby strengthening the multilateral trade system. They also ensured that their bilateral FTAs were not in conflict with multilateral and ASEAN-based agreements.

30. **The authorities are refocusing the mandatory savings scheme (CPF) as a core retirement scheme, rather than use it as a discretionary countercyclical instrument**. They noted that the increasing use of flexible wage contracts had reduced the need for discretionary changes in employer contribution rates for countercyclical purposes. The

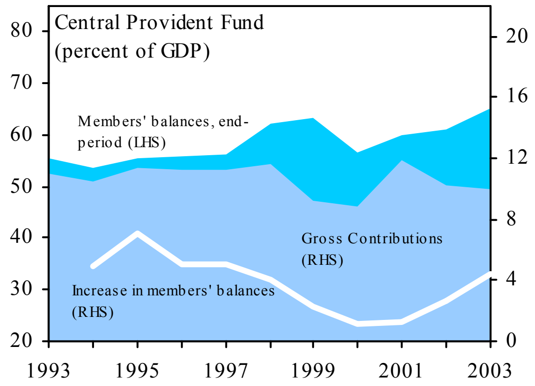
---

[10] A recent survey indicates that over 60 percent of the private sector has introduced wage flexibility by linking 30 percent of monthly salaries to performance and profit indicators.

[11] Singapore already has FTAs with several countries, including Japan and the United States. Negotiations are completed with Korea and near completion with India, while those with Canada, China, and Mexico are at advanced stages.

authorities also added that recent measures had raised the minimum savings for retirement, and that CPF members with insufficient resources were being aided through budgetary transfers. Retirees were also encouraged to monetize their residential properties by downgrading, subletting or using reverse mortgages to benefit from capital gains from their housing investments.[12] The mission agreed that with the last round of cuts in contribution rates there was little room for further reductions without compromising wage replacement rates. CPF officials also agreed with the staff that the CPF Investment Scheme, which was aimed at infusing greater investment flexibility, would be more extensively used if its high transaction costs were reduced by pooling funds under a small number of asset managers with simpler choices of risk-return portfolios. The government plans to align CPF rates of return with long-term government security yields, which should improve the returns on members' balances over time.

Net CPF contribution has grown recently.



31. **The authorities are concerned about the emergence of structural unemployment**. They noted that continued loss of low-end manufacturing jobs and the ongoing restructuring toward capital intensive industries have increased long-term unemployment.[13] With the economy moving toward more knowledge-based activities, there is a growing danger that the less-educated and less-skilled workers may find themselves permanently unemployed. The authorities were addressing this problem through a wide range of retraining and skills upgrading programs. A new government statutory board, the Workforce Development Agency, was formed in 2003 to coordinate and strengthen these programs.

32. **The mission held extensive discussions on the regulatory challenges arising from banks' overseas expansion and the increase in asset management firms in Singapore**. The authorities noted that bank profitability and capitalization remained strong and that local banks have responded to increased domestic competition with the expansion of foreign banks by consolidating at home and expanding abroad (Box 3). The mission observed that the expansion abroad could pose new risks and regulatory challenges. The authorities said that

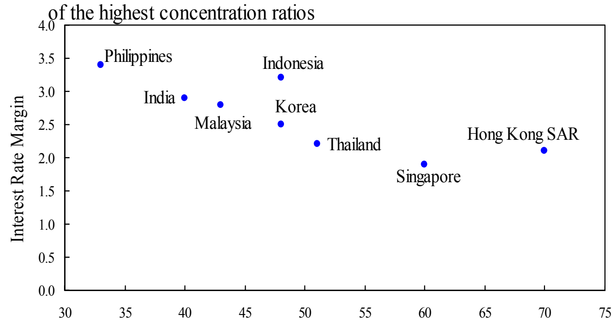
[12] Given the large share of wealth held in residential properties (over 90 percent of households are homeowners with a total net wealth of over 150 percent of GDP), retirees in Singapore often face the dilemma of being "asset rich, but cash poor." Net household wealth held as equity in pension funds (including CPF) is around 65 percent of GDP. Overall, net wealth of households is around 350 percent of GDP, comparable to that in the U.S. but less than that in Japan or in the U.K.

[13] According to the authorities' estimates, the natural rate of unemployment has been creeping up to around 3–3½ percent in recent years from around 2 percent before the Asian crisis.

BOX 3. SINGAPORE: OVERSEAS EXPANSION OF DOMESTIC BANKS[1]

In recent years, bank activities in many emerging market economies have been progressively liberalized. Financial reforms have eased legal barriers to entry, liberalized deposit and loan rates, relaxed restrictions on bank portfolios and ownership, and reduced reserve requirements.

In Singapore, there has been a continuous process of financial reform and liberalization since the 1970s, and a major five-year program was launched in 1999 to liberalize access by foreign banks to Singapore's domestic market. This liberalization, together with the less benign post-Asian-crisis macroeconomic environment, has challenged the traditionally highly profitable Singaporean banks. Foreign banks have played an important role in compressing intermediation margins, especially in certain segments, for example, mortgage lending. However, the banking sector remains concentrated. The three local Singapore banks control about 60 percent of deposits, and their net interest rate margin is the lowest in the region. The concentrated market structure may have contributed to the low interest margin by reducing costs through scale effects.



Sources: Fitch Research, Capital Intelligence

These competitive pressures have led domestic banks to consolidate and expand abroad to maintain profitability. Market concentration and scale have contributed to the relative efficiency of Singapore's banks, which have the second lowest cost-to-income ratio in the region. Other advantages for the Singapore's banks in their expansion abroad have been a sound regulatory environment, high capitalization, and low NPLs. Since 1999, Singapore banks have acquired interest in Malaysia, Hong Kong SAR, Thailand, the Philippines and Indonesia. (Temasek, which is a major shareholder of Singapore's largest domestic bank, DBS, has separately also acquired shares in Indian, Malaysian, and Indonesian banks.) The performance of the overseas acquisitions so far has been mixed: with successes in Hong Kong and Malaysia, and problems in Thailand and the Philippines. This pattern has largely reflected local conditions rather than the efficiency of Singaporean banks.

The opening of Singapore's domestic market to foreign competition and the expansion of Singapore's banks abroad pose new challenges for bank regulators. The growing presence of foreign banks raises new supervisory issues—the objectives of the parent bank and the local institution may differ and local regulators may lack important information about the parent bank's financial stability. The expansion of local banks into foreign countries with different market, legal, and regulatory infrastructures also brings new risks—problems in their foreign ventures may threaten the stability of the parent banks.

MAS is well aware of these risks and has been actively seeking cooperation with bank regulators in countries hosting Singapore's banks subsidiaries and in the home countries of the major foreign banks active in Singapore.

---

[1]For details see Chapter II of the accompanying *Selected Issues* paper, prepared by Giovanni Dell'Ariccia.

they monitored risks arising from these developments and maintained regular contact with regulators in host countries. While client accountability was stressed in regulating asset managers and hedge funds, financial exposure of banks to these firms was closely monitored.

Local banks' balance sheets remain healthy.

Key Financial Indicators for Local Banks
(In percent)

	1998	1999	2000	2001	2002	2003	2004 1st half
Capital adequacy							
Regulatory capital to risk-weighted assets	18.1	20.6	19.6	18.1	16.9	17.9	15.5
Asset quality							
Nonperforming loans to total loans	…	5.3	3.4	3.6	3.4	3.2	2.9
Classified loans to total loans	7.8	8.5	5.6	5.7	5.5	5.1	4.3
Profitability							
After-tax return on assets	0.4	1.2	1.3	0.8	0.8	0.9	1.4
After-tax return on equity	4.2	10.7	12.6	7.7	7.6	8.3	12.8

33. **The MAS has set up a unit to coordinate implementation of the FSSA recommendations**. Progress has been made, including in lowering the minimum capital requirement for local banks from 12 percent to 10 percent, a step endorsed by the FSSA (Table 8). The mission welcomed the advances and encouraged the authorities to clarify the roles of the monetary authority and its accountability in the planned amendments to the MAS Act. It also supported the introduction of a deposit insurance scheme, scheduled for 2005, and encouraged the authorities to regularly update and publish financial soundness indicators.[14] Earlier this year, the MAS published the Financial Stability Review, a new bi-annual publication, which reiterated the overall soundness of Singapore's financial sector. The authorities intend to implement the Basel II standards in tandem with the G10 countries, by end-2007. The FSSA had concluded that regulatory and supervisory practices were close to international standards and codes, including in accounting standards, and that the authorities had taken initiatives to improve corporate governance and strengthen the framework of disclosure practices. Despite these efforts, the recent incident related to speculative oil trading by a Singapore-listed subsidiary of an overseas company indicates that there is room for further improvement in these areas.[15]

34. **The mission welcomed the authorities' continued efforts to enhance data quality and its timeliness**. The authorities have published net international investment position (IIP) data for 2001–2003. The mission welcomed this data release, but noted that the levels appeared understated in light of Singapore's large current account surpluses since the 1990s. Officials remarked that this could reflect different market values of the portfolios of foreign and resident investors. Singapore remains a destination, since the 1970s, of large foreign investment, and only in the 1990s has outward foreign investment become substantial. In addition, as the IIP surveys had been started recently, the sample may not be fully representative. As the coverage of the surveys was widened the quality of the data would also

[14] The proposed scheme would cover up to S$20,000 per depositor and per institution, while banks would pay a risk-weighted insurance premium.

[15] After the return of the mission from Singapore, in late November, a Singapore-listed Chinese state-owned company sought bankruptcy protection after losing $550 million in speculative oil trading. With the loss more than the company's market value, trading of its shares was suspended on the stock exchange (SGX). An SGX inquiry is underway.

improve. Indeed, the IIP positions have been revised upward recently. The officials responded positively to staff suggestion of conducting a comprehensive review of the statistical bases by participating in a data ROSC. The authorities are reviewing the modalities and resource cost of the ROSC, before making a final decision.

V. Staff Appraisal

35. **Singapore's economy has recovered rapidly since mid-2003, having weathered a series of adverse shocks since the Asian crisis**. Lately, job creation has also gathered strength following large productivity gains in the earlier part of the recovery. This turnaround owes much to a favorable external environment, including strong global electronics demand. It was also helped by supportive macroeconomic policies as well as continued structural reforms to improve competitiveness.

36. **Looking ahead, economic activity is expected to moderate to more sustainable levels in the near term**. Taking into account the softening in global demand, particularly the cresting of the global electronic cycle, output growth could slow to about 4 percent in 2005. The outlook is shrouded in considerable uncertainty, especially on the external front. Despite the expected moderation in activity, however, there is likely to be little slack in the economy, reflecting the recent rapid growth. The tightening in the labor market and high energy prices could raise inflationary pressures.

37. **In this environment, the current tightening stance of monetary policy is appropriate**. This will also pave the way for an orderly and gradual withdrawal of the stimulus provided in recent years to support the economy. However, if the slowdown appears to be more than expected, monetary policy may need to become more supportive. MAS's monetary policy framework centered on the management of the trade-weighted exchange rate has worked well to keep inflation low and stable. MAS's ongoing efforts to increase the transparency of the framework are commendable.

38. **There are no apparent signs of a real exchange rate misalignment, but the rise in recent current account surpluses is not fully explained by private sector behavior**. Foreign investment by the government and GLCs could have played a part in warding off upward pressures on the real exchange rate despite the rise in current account surpluses. However, with the expected increase in domestic investment and the authorities' intended appreciation of the nominal effective exchange rate, current account surpluses should narrow in the near term. This will also aid in the orderly adjustment of the global current account imbalances.

39. **Fiscal policy has been judiciously used in recent years to support the economy**. With the higher-than-expected growth, the fiscal position this year is likely to be better than budgeted. Such an outturn would provide room for the authorities to cut the top personal income tax rate in the next budget, and strengthen the existing social safety net. Singapore's fiscal-policy framework of maintaining a balanced budget over the medium term remains appropriate, although the framework could be improved further by setting the limit on the use of the annual investment income within the context of Singapore's future revenue potential and spending needs.

40. **The recent public review of Temasek's operations is a significant milestone in increasing fiscal transparency**. Following Temasek's example, the government could also consider publishing, without disclosing strategic and sensitive details, GIC's aggregate assets, broad elements of its portfolio, and its overall returns. Such a move could further enhance investor confidence by testifying to the strength of the government's financial position. More generally, publishing the consolidated public sector accounts, in line with international accounting standards, would greatly help in this regard. The staff welcomes the authorities' interest in undertaking a fiscal ROSC in the near future.

41. **In response to rising competition from low-cost regional economies, the authorities have implemented an array of reforms to enhance competitiveness**. As a result, significant progress has been made in increasing labor market and wage flexibility, reducing business taxes and costs, and promoting the outward expansion of Singapore firms. Moreover, quality upgrading and diversification in the manufacturing sector and Singapore's expansion into a hub for regional asset management, health, and education services are also taking place. These developments will provide a new basis for sustained growth over the medium term. Nevertheless, to promote entrepreneurship and increase the role of the private sector, the staff encourages the authorities to step up the GLC divestment process. The newly legislated Competition Law should help to strengthen the separation of the roles of the government as a referee and a player in the economy.

42. **The authorities have rightly focused attention on the regulatory challenges arising from banks' overseas expansion**. The financial system remains robust and benefits from an efficient legal system, good accounting standards, and ongoing initiatives to promote corporate governance, as noted in the FSSA. The authorities are encouraged to implement the remaining FSSA recommendations, including clarifying the roles of the monetary authority and its accountability in the planned amendments to the MAS Act. Recent events, related to speculative trading by a listed company, suggest the need for increased regulatory vigilance of companies trading in the Singapore exchange.

43. **Given the aging population, a key challenge is to ensure that the retired are adequately provided for**. Thus, the measures taken to refocus the CPF as a core retirement scheme are welcome. Moreover, the increasing use of flexible wage contracts has reduced the need for discretionary changes in contribution rates for countercyclical purposes. The CPF investment scheme's high transaction costs could be reduced by pooling funds under a single or a small number of asset managers with simpler choices of risk-return portfolios, which could allow a more extensive use of this scheme.

44. **Singapore is in observance of the SDDS and generally publishes economic and financial data on a timely basis**. The authorities' continued efforts to improve data quality are welcome. The staff encourages the authorities to consider a comprehensive review of the statistical base by participating in a data ROSC.

45. **The staff recommends that the next Article IV consultation with Singapore be held on the standard 12-month cycle**.

Table 1. Singapore: Selected Economic and Financial Indicators, 1999–2005

Nominal GDP (2003): US$91.3 billion — GDP per capita (2003): US$21,825
Population (2003): 4.19 million — Quota: SDR 862.5 million

	1999	2000	2001	2002	2003	2004 Proj.	2005 Proj.
Growth (percentage change)							
Real GDP	6.9	9.7	-1.9	2.2	1.1	8.1	4.0
Total domestic demand	7.0	16.2	-6.3	-1.7	-9.6	11.5	4.6
Final domestic demand	2.5	12.7	0.4	-2.1	-1.6	6.7	2.9
Consumption	8.2	15.4	3.5	2.5	-0.4	6.3	3.4
Gross fixed investment	-4.9	8.7	-4.5	-9.9	-3.8	7.5	1.9
Change in inventories (contribution to GDP growth)	3.5	2.6	-5.7	0.4	-6.2	2.6	1.0
Net exports (contribution to GDP growth)	1.5	-2.8	3.6	3.6	8.7	-0.1	-0.7
Exports of goods and services	7.9	14.7	-6.4	3.6	9.5	18.5	6.1
Imports of goods and services	8.0	18.3	-9.0	1.9	5.6	20.3	8.6
Saving and investment (percent of GDP)							
Gross national savings	50.6	46.3	43.6	42.5	44.2	45.1	40.3
Gross capital formation	32.0	32.0	24.9	21.2	13.4	16.3	17.0
Inflation and unemployment (period average, percent)							
CPI inflation	0.0	1.3	1.0	-0.4	0.5	1.7	1.6
Unemployment rate	3.5	3.1	3.3	4.4	4.7	3.9	3.5
Central government budget (percent of GDP) 1/							
Revenue	29.5	29.2	27.2	23.0	20.8	20.7	20.5
Expenditure	24.0	20.4	23.7	18.7	14.4	17.6	17.5
Overall balance	5.5	8.8	3.5	4.2	6.3	3.1	3.0
Primary operating balance 2/	3.4	1.1	-3.5	-2.7	-3.0	-2.9	-3.1
Money and credit (end of period, percentage change)							
Broad money (M3) 3/	7.3	-1.8	4.0	-0.8	5.9	4.6 7/	...
Credit to private sector	-3.0	5.9	16.3	-8.6	5.4	5.1 7/	...
Interest rate (three-month interbank, in percent)	2.8	2.8	1.3	0.8	0.8	1.4 7/	…
Merchandise trade (percentage change)							
Export volume	5.4	16.8	-8.6	4.4	12.2	19.3	5.9
Import volume	9.5	14.8	-12.4	1.2	7.3	21.7	8.6
Terms of trade	-0.8	-2.5	-1.8	-0.8	0.3	-1.0	-1.2
Balance of payments (US$ billion)							
Current account balance	15.3	13.2	16.1	18.9	28.2	29.8	26.2
(Percent of GDP)	(18.6)	(14.3)	(18.7)	(21.4)	(30.9)	(28.8)	(23.3)
Balance on goods	12.4	12.7	15.7	19.9	29.3	31.6	26.9
Exports, f.o.b.	124.4	149.3	133.7	137.3	157.8	195.5	207.1
Imports, f.o.b.	-111.9	-136.6	-118.0	-117.4	-128.5	-163.9	-180.2
Overall balance	4.3	6.9	-0.9	1.3	6.8	15.7	1.7
International reserves and external debt							
Gross official reserves (US$ billion)	77.2	80.4	75.8	82.3	96.3	110.1 8/	...
(Months of imports) 4/	(5.6)	(6.6)	(6.2)	(6.1)	(5.8)	(6.0)	...
Gross external debt (US$ billion) 5/	34.2	32.2	33.9	33.6	36.3	38.8 9/	...
(Percent of GDP)	(41.5)	(34.8)	(39.4)	(38.1)	(39.7)	(37.5)	...
Exchange rate							
S$/US$ (end of period)	1.666	1.732	1.851	1.737	1.701	1.642 8/	...
Nominal effective exchange rate 6/	119.2	119.5	121.2	120.2	115.7	114.0 10/	...
Real effective exchange rate 6/	107.2	107.4	108.2	105.7	101.0	98.4 10/	...

Sources: Data provided by the Singapore authorities; and Fund staff estimates and projections.

1/ Fiscal year beginning on April 1.
2/ Overall balance excluding capital revenue, investment income, net lending, debt service, and fund transfers.
3/ Adjusted for the acquisition of POSBank by the Development Bank of Singapore in November 1998.
4/ In months of following year's imports of goods and services.
5/ Based on BIS data; corporate bonds outstanding and the external bank claims by the BIS reporting countries.
6/ IMF Information Notice System monthly index (1990 = 100); period average.
7/ As of end-October 2004.
8/ As of end-November 2004.
9/ As of end-March 2004.
10/ As of end-September 2004.

Table 2. Singapore: Balance of Payments, 1999–2005 1/

(In billions of U.S. dollars)

	1999	2000	2001	2002	2003	2004 Proj.	2005 Proj.
Current account balance	15.3	13.2	16.1	18.9	28.2	29.8	26.2
Trade balance	12.4	12.7	15.7	19.9	29.3	31.6	26.9
Exports, f.o.b.	124.4	149.3	133.7	137.3	157.8	195.5	207.1
Of which : electronics exports	62.9	77.0	64.1	65.1	71.6	64.9 3/	…
Imports, f.o.b.	-111.9	-136.6	-118.0	-117.4	-128.5	-163.9	-180.2
Services balance	2.1	2.0	0.7	0.2	1.1	1.0	0.1
Income balance	1.8	-0.3	0.8	-0.1	-1.1	-1.7	0.5
Transfer payments (net)	-1.0	-1.1	-1.1	-1.1	-1.1	-1.1	-1.3
Net capital flows 2/	-11.0	-6.4	-17.0	-17.6	-21.4	-14.2	-24.5
Capital and financial account balance	-14.4	-5.9	-14.4	-13.6	-25.3	-14.2	-24.5
Capital account (net)	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Financial account (net)	-14.2	-5.8	-14.3	-13.5	-25.1	-14.0	-24.3
Direct investment (net)	8.6	11.9	-2.0	2.0	5.9	6.3	6.7
Portfolio investment (net)	-8.9	-15.0	-10.0	-11.1	-10.9	-7.0	-13.6
Other investment (net)	-13.9	-2.7	-2.3	-4.4	-20.1	-13.3	-17.5
Net errors and omissions	3.4	-0.5	-2.6	-4.0	3.8	0.0	0.0
Overall balance	4.3	6.9	-0.9	1.3	6.8	15.7	1.7
Memorandum item :							
Current account as percent of GDP	18.6	14.3	18.7	21.4	30.9	28.8	23.3
Trade balance as percent of GDP	15.1	13.7	18.3	22.5	32.1	30.5	23.9
Net international investment postion							
(In billions of U.S. dollars)	...	...	54.6	67.9	76.0	...	...
(In percent of GDP)	...	...	63.5	76.9	83.2	...	...

Sources: Monetary Authority of Singapore, Economic Survey of Singapore; and staff estimates and projections.

1/ Data for the current account balance, the capital and financial account balance, and net errors and omissions are converted to U.S. dollars from the official presentation in Singapore dollars using period-average exchange rate.

2/ Including net errors and omissions.

3/ For the first three quarters.

Table 3. Singapore: Monetary Survey, 1999–2004

	1999	2000	2001	2002	2003	2004 March	2004 June	2004 Sept.
	(In billions of Singapore dollars at end-period)							
Net foreign assets	131.0	126.3	132.9	133.2	150.0	153.6	164.0	163.9
Monetary authorities	127.1	137.8	138.6	141.5	161.9	170.7	173.7	171.4
Deposit money banks 1/	3.8	-11.5	-5.7	-8.3	-11.9	-17.1	-9.7	-7.5
Domestic credit (net)	121.8	126.6	144.6	121.3	134.0	145.4	142.8	137.2
Claims on private sector	150.2	159.1	185.1	169.1	178.3	181.0	183.8	184.5
Claims on government (net)	-28.4	-32.5	-40.4	-47.7	-44.3	-35.6	-41.0	-47.3
Other items (net)	-78.3	-82.1	-96.6	-74.2	-89.2	-97.3	-102.4	-100.4
M2	174.5	170.9	180.9	180.3	194.8	201.7	204.4	200.7
M1	31.1	33.3	36.1	35.8	38.7	41.4	41.1	41.9
Quasi-money	143.4	137.6	144.8	144.5	156.1	160.2	163.3	158.9
	(Annual percentage change)							
Domestic credit	-0.3	4.0	14.2	-16.1	10.5	16.2	12.2	6.6
Claims on private sector	-3.0	5.9	16.3	-8.6	5.4	7.7	6.4	5.7
M2	8.5	-2.0	5.9	-0.3	8.1	9.9	10.7	8.4
M3	7.3	-1.8	4.0	-0.8	5.9	7.9	9.3	7.3

Source: IMF, *International Financial Statistics* .

1/ Commercial banks.

Table 4. Singapore: Summary of Government Operations, 1998/99–2004/05

(In percent of GDP)

	1998/99	1999/00	2000/01	2001/02	2002/03	2003/04		2004/05	
						Budget 1/	Act	Budget 1/	Proj. 2/
Total revenue	30.7	29.5	29.2	27.2	23.0	22.0	20.8	20.5	20.7
Current revenue	24.3	25.8	25.1	24.0	21.2	20.8	19.2	19.6	19.8
Tax revenue	16.0	15.7	15.8	15.7	13.6	13.5	13.1	13.6	13.8
Investment income 3/	3.6	4.5	5.7	5.5	5.2	4.5	3.8	3.9	3.8
Other nontax revenue	4.7	5.6	3.6	2.8	2.5	2.8	2.3	2.1	2.2
Capital revenue 4/	6.4	3.8	4.1	3.1	1.7	1.2	1.5	0.9	0.9
Total expenditure	29.0	24.0	20.4	23.7	18.7	20.5	14.4	17.7	17.6
Current expenditure	11.8	11.3	12.7	15.5	13.6	13.6	13.1	12.9	12.8
Operating expenditure	10.9	10.3	11.3	12.1	12.2	12.5	12.2	11.7	11.7
Debt servicing	0.7	0.6	0.3	0.3	0.3	0.2	0.2	0.2	0.2
Agency fees on land sales	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Investment expenses	0.2	0.2	0.4	0.4	0.3	0.6	0.3	0.5	0.5
Transfer payments	0.0	0.3	0.6	2.7	0.8	0.4	0.4	0.5	0.5
Development expenditure and net lending	17.2	12.5	7.2	7.4	4.7	6.9	1.3	4.7	4.6
Development expenditure 5/	9.1	7.1	5.8	6.8	5.5	6.8	5.6	6.2	6.2
Net lending	8.1	5.4	1.4	0.6	-0.7	0.1	-4.3	-1.5	-1.5
Fund transfers 6/	0.0	0.2	0.5	0.7	0.4	0.0	0.0	0.1	0.1
Overall balance	1.7	5.5	8.8	3.5	4.2	1.5	6.3	2.8	3.1
Primary operating balance 7/	0.5	3.4	1.1	-3.5	-2.7	-3.9	-3.0	-3.3	-2.9
Memorandum items:									
Budget balance (the government's definition)	0.7	3.4	2.5	-1.8	0.1	-0.5	-1.2	-0.8	…
Government saving	12.4	14.2	11.9	7.8	7.3	7.2	6.1	6.6	6.9
Structural primary operating balance 8/	1.2	3.3	0.1	-3.0	-2.3	-3.5	-2.4	-2.7	-2.7
Fiscal impulse based on operating balance 9/	2.2	-2.1	3.2	3.1	-0.7	1.2	0.1	0.3	0.3
Gross government domestic debt 10/	84.0	90.1	84.2	96.7	99.2	...	106.4	…	…
of which: Central Provident Fund	43.5	44.9	38.0	58.0	59.8	...	63.3	…	…

Sources: Data provided by the Singapore authorities; and staff estimates and projections.

1/ Original budget, excluding supplementary budgets. Fiscal year runs from April 1 through March 31.
2/ Includes the effect of automatic stabilizers.
3/ Includes all investment income from government assets and interest earnings on development loans from 2000/01.
4/ Sale of government property.
5/ Includes the land reclamation expenditure.
6/ Includes transfers to the Edusave Endowment Fund, the Medical Endowment Fund, the Lifelong Learning Endowment Fund and the ElderCare Fund.
7/ Overall balance excluding investment income, capital revenue, debt service, net lending, and fund transfers.
8/ Calculated with the elasticity of revenue with respect to output equal to 1.1, and a zero elasticity of expenditure with respect to output.
9/ Calculated as an increase in the structural primary operating deficit.
10/ Data for end of calendar year.

Table 5. Singapore: Indicators of Vulnerability, 1999–2004

	1999	2000	2001	2002	2003	2004	Month for 2004 data
Financial sector indicators							
Broad money (M3, percent change, y/y)	7.3	-1.8	4.0	-0.8	5.9	4.6	Oct.
Private sector credit (percent change, y/y)	-3.0	5.9	16.3	-8.6	5.4	5.1	Oct.
Credit to the property sector (percent change, y/y)	2.1	9.6	6.4	0.4	11.4	8.7	Oct.
Share of property-sector credit in total non-bank credit (percent)	39.8	41.7	41.9	42.3	44.6	45.6	Oct.
Credit rating of local banks (S&P) 1/	A	A+/A	A+/A	A+/A	A+/A	A+	Sep.
Three-month Interbank rate (percent, end-year)	2.8	2.8	1.3	0.8	0.8	1.4	Nov.
NPL ratio (local banks, percent) 2/	5.3	3.4	3.6	3.4	3.2	2.9	June
Capital adequacy ratio of local banks (percent)	20.6	19.6	18.1	16.9	17.9	15.5	June
Asset market indicators							
Stock prices (percent change, y/y)	78.0	-22.3	-15.7	-17.4	31.6	18.3	Nov.
P/E ratio	99.2	20.9	16.8	21.2	24.9	16.4	Oct.
Stock prices of the finance sector (percent change, y/y)	120.6	-23.2	-1.9	-13.5	23.8	10.3	Nov.
Real estate prices (1998Q4=100, 4-quarter moving average) 3/							
Residential	121.3	137.1	123.4	115.4	113.3	112.7	Q3
Office space	93.3	116.6	107.8	88.3	76.5	72.5	Q3
External Indicators							
Current account balance (US$ billion)	15.3	13.2	16.1	18.9	28.2	22.1	Q1-Q3
(In percent of GDP)	18.6	14.3	18.7	21.4	30.9	28.6	Q1-Q3
Gross official reserves (US$ billion)	77.2	80.4	75.8	82.3	96.3	110.1	Nov.
(In month of next year's imports of goods and services)	5.6	6.6	6.2	6.1	5.8	6.0	Nov.
Real exchange rate (end of period, 1990=100)	106.4	109.6	106.1	104.9	98.8	98.8	Sep.
Sovereign yield spread (in percent) 4/	…	2.1	2.1	1.5	0.9	1.2	Sep.
External debt (US$ billion) 5/	34.2	32.2	33.9	33.6	36.3	38.8	Mar.
(In percent of GDP)	41.5	34.8	39.4	38.1	39.7	37.5	Mar.
(In percent of exports of goods and services)	22.7	18.0	20.8	20.1	19.3	16.7	Mar.
Of which: Public sector external debt	0.0	0.0	0.0	0.0	0.0	0.0	Mar.

Source: Data provided by the Singapore authorities and IMF, Information Notice System.

1/ Ratings of the three major local banks.
2/ In percent of total loans.
3/ The price indices are computed based on the Laspeyres method before 1998Q4 and based on the moving average method from 1998Q4.
4/ Spread of 10-year US$-denominated bond issued by DBS over the U.S. government bond.
5/ Based on BIS data; corporate bonds outstanding and the external bank claims by the BIS reporting countries.

Table 6. Singapore: Illustrative Medium-Term Scenario, 2000–2009

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
							proj.			
Real growth (percent change)										
GDP	9.7	-1.9	2.2	1.1	8.1	4.0	4.5	4.5	4.5	4.5
Total domestic demand	16.2	-6.3	-1.7	-9.6	11.5	4.6	5.9	5.3	4.6	4.7
Final domestic demand	12.7	0.4	-2.1	-1.6	6.7	2.9	4.2	4.3	4.4	4.4
Consumption	15.4	3.5	2.5	-0.4	6.3	3.4	4.0	4.3	4.3	4.4
Gross fixed investment	8.7	-4.5	-9.9	-3.8	7.5	1.9	4.5	4.5	4.5	4.5
Change in inventories 1/	2.6	-5.7	0.4	-6.2	2.6	1.0	1.0	0.5	0.0	0.0
Exports of goods and services	14.7	-6.4	3.6	9.5	18.5	6.1	7.1	7.5	7.7	7.7
Imports of goods and services	18.3	-9.0	1.9	5.6	20.3	8.6	8.2	8.2	8.2	8.2
Saving and investment (percent of GDP)										
Gross national savings	46.3	43.6	42.5	44.2	45.1	40.3	40.6	40.8	41.1	41.4
Central government	12.5	8.8	7.4	6.4	6.7	6.8	6.8	6.8	6.8	6.8
Private and other	33.9	34.8	35.1	37.8	38.4	33.5	33.8	34.0	34.3	34.6
Gross capital formation	32.0	24.9	21.2	13.4	16.3	17.0	18.2	18.9	19.3	19.6
Gross fixed capital formation	29.8	29.6	25.8	24.9	24.7	24.2	24.2	24.2	24.2	24.2
Inflation and unemployment (period average, percent)										
CPI inflation	1.3	1.0	-0.4	0.5	1.7	1.6	1.5	1.5	1.5	1.5
Unemployment rate	3.1	3.3	4.4	4.7	3.9	3.5	3.4	3.3	3.3	3.3
Central government (percent of GDP) 2/										
Revenue	29.3	27.7	24.0	21.3	20.7	20.6	20.3	20.3	20.3	20.3
Expenditure	21.3	22.9	20.0	15.5	16.8	17.5	17.3	17.2	17.2	17.2
Overall balance	8.0	4.8	4.0	5.8	3.9	3.1	3.1	3.1	3.1	3.1
Budget balance (the government's definition)	2.7	-0.7	-0.3	-0.8	-0.6	-0.1	0.5	0.6	0.1	0.0
Merchandise trade (percent change)										
Export volume	16.8	-8.6	4.4	12.2	19.3	5.9	7.1	7.6	7.8	7.8
Import volume	14.8	-12.4	1.2	7.3	21.7	8.6	8.3	8.4	8.4	8.3
Terms of trade 3/	-2.5	-1.8	-0.8	0.3	-1.0	-1.2	0.1	0.1	0.1	0.1
Balance of payments (in percent of GDP)										
Current account balance	14.3	18.7	21.4	30.9	28.8	23.3	22.5	21.9	21.8	21.8
Balance on goods and services	15.9	19.1	22.8	33.3	31.4	24.0	22.3	21.7	21.5	21.3
Balance on income and transfers	-1.6	-0.4	-1.4	-2.5	-2.7	-0.7	0.2	0.2	0.3	0.5
Overall balance	7.4	-1.0	1.4	7.4	15.1	1.5	9.6	10.2	9.9	6.1
Gross official reserves (US$ billions)	80.4	75.8	82.3	96.3	112.0	113.6	125.3	138.6	152.5	161.8
(In months of imports) 4/	(6.6)	(6.2)	(6.1)	(5.8)	(6.1)	(5.7)	(5.7)	(5.7)	(5.7)	(5.7)

Sources: Data provided by the Singapore authorities; and staff estimates and projections.

1/ Contribution to GDP growth.
2/ On a calendar year basis.
3/ Based on changes in export and import unit values.
4/ In months of next year's imports of goods and services.

Table 7. Key Recommendations of the Economic Review Committee

Recommendations	Status
Taxation	
• Reduce corporate and personal income tax rates to 20 percent by year of assessment (YA) 2005.	• The government cut corporate and top personal tax rates from 24.5 percent and 26 percent respectively to 22 percent in YA2003. The corporate tax rate will be lowered to 20 percent from YA2005.
• Raise GST from 3 percent to 5 percent.	• The GST rate was raised from 3 percent to 4 percent on January 1, 2003, and to 5 percent on January 1, 2004.
• Create GST offset package to help Singaporeans adjust to GST increase.	• Implemented in 2003-04 offset packages that include income transfers (Economic Restructuring Shares (ERS)); additional ERS will be distributed in 2005.
Central Provident Fund (CPF)	
• Refocus CPF on providing basic retirement savings, home ownership and medical needs, and on addressing labor market flexibility. • Defer returning CPF contribution rate to 40 percent from 36 percent (20 percent employee; 16 percent employer) for two years.	• In August 2003, the government made further changes to earlier ERC recommendations. • A lower long-term variable contribution rate of 30 percent to 36 percent (with employer rate between 10 percent and 16 percent) was set to maintain competitiveness. For older workers, CPF rate will be reduced to 27 percent by 2006. • From October 1, 2003, cut employer contribution rate from 16 percent to 13 percent. Employees continue to contribute 20 percent. • Increased CPF and Medisave Minimum Sums; revised Special and Medisave Accounts contribution rates; tightened withdrawal rules at age 55; and further reduced CPF salary ceiling. • The tax relief ceiling for voluntary top-up of individuals' contributions will be raised by 17 percent from 2005.

Recommendations	Status
Land	
• Pursue policies that ensure the adequate supply of land at competitive, stable prices.	• Lowered rentals and prices for industrial properties. • Extended rental rebates for industrial tenants and lessees until June 2004. • Expanded eligibility for tax deductions for upfront land premium payments for industrial land to 60-year leases from 30 years previously.
Labor Market	
• Enhance labor market flexibility by raising variable wage component and drop seniority-based wage system.	• Made several changes to CPF to address labor market flexibility (see above). • FY2003/04 budget introduced portable medical benefits. • In January 2004, Tripartite Taskforce on Wage Restructuring encouraged companies to adopt a more flexible wage model that would increase the variable component of wages, linked to the performance of the employee and company. As of end-June 2004 more than 60 percent of the private sector workforce were under some form of flexible wages. • A new category of work pass introduced from July 2004 to help businesses recruit skilled workers.
Entrepreneurship and Internationalization	
• GLCs should be commercially run and operate globally. They should be reviewed for divestiture. • To create pro-enterprise environment, have sunset rule on all licenses, outsource licensing and other government functions, allow enterprises to retain intellectual property from government projects, and enact generic competition law. • Improve availability of capital for entrepreneurs.	• Review of GLCs for possible divestment every three years. Companies to be divested are Ascendas, PSB Corp, HDBay, and Cleantech Services. • Review of administrative rules and licensing procedures on a rolling five-year cycle. • Allow companies to defer income taxes for two years if their overseas investment incurs operating losses. • Tax exemptions for start-up companies for up to 3 years. The withholding tax on royalty payments will also be reduced from 15% to 10% from January 2005. • Provision of financing for start-up companies. • Competition law will come into force in 2005.

Recommendations	Status
Manufacturing and Services Sectors • Continue to attract multinational companies in electronics, chemicals, biomedical sciences and engineering sectors. Develop new engines of growth such as industrial IT, micro-electromechanical systems, nanotechnology and photonics. • Continue to develop areas with strong expertise, like trading and logistics, ICT, financial services and tourism. In addition, launch into new sectors such as healthcare, education and creative industries.	• Promote private wealth management. All foreign-sourced income remitted by resident individuals will be exempt from tax from YA2005. Singapore-sourced investment income derived by individuals from financial instruments will also be exempt from tax from YA 2005. • Extend overseas trade linkages and develop target markets through the active pursuit of FTAs. • Promote Singapore as a business hub. The maximum duration for the pioneer incentive was extended from 10 to 15 years in 2004. The regional HQ incentive was also extended from 3 to 5 years. • Allow approved companies to claim capital allowances on equipment used by subsidiaries outside Singapore from FY2003. • A Ministerial Committee on Services has been set up to oversee the development of the service industries and to resolve trade-offs between economic goals and social objectives.
Human Capital • Develop the full potential of individuals through a more flexible school curriculum. • Assist unemployed through comprehensive re-employment approach with job counseling, training, job search assistance and subsidized job attachments.	• A new statutory board (the Singapore Workforce Development Agency) was established in September 2003 to promote continuing education and training. • To encourage Singaporeans to upgrade their skills in preparation for career switches, tax relief for course fees is increased from S$2,500 to S$3,500 and extended to courses that eventually result in a career switch. • The salary ceiling for the Skills Development Levy was raised by 20 percent from July 2004.

Table 8. Singapore: FSSA Recommendations

Key Policy Recommendations	**Status**
Macro-prudential monitoring: Further strengthen MAS' monitoring of: (i) risks arising from new financial products; (ii) cross-border financial flows (including flows in the ADM and particularly transactions between branches and head offices) to detect potential strains in the offshore banking market; (iii) household and corporate sector balance sheets to assess the resilience of the private sector; and (iv) market and counter-party risks of derivatives activities by financial institutions.	**Some progress:** In January 2005, MAS published a new bi-annual publication—Financial Stability Review—which assesses the overall stability of the financial system.
Regulatory systems and supervisory practices: Further enhance the MAS' legal and regulatory framework through the completion of the review of the regulatory minimum capital requirements for local banks and the implementation of its new risk-based capital framework for the insurance industry, planned for introduction in late 2004; and complete the ongoing review of the MAS Act.	**Implemented**: Review of capital requirements completed. Insurers to comply with the new risk-based capital framework from January 1, 2005.
The MAS' accountability, independence, and oversight capabilities: Reduce the potential for conflicts of interest arising from the multiple official responsibilities of the Chairman of the MAS.	**In progress**: A working group will propose amendments to the MAS act addressing i) specification of MAS' objectives, and ii) MAS accountability framework (targeted for 2005)
Monetary and financial policy transparency: Provide more information on how supervisory actions are taken in line with the risk-based supervisory framework and disclose more information to improve the public's ability to assess supervisory performance.	**Under review:** 2 monographs published on: "Objectives and Principles of Financial Supervision in Singapore," April 2004. "MAS' Roles and Responsibilities in Relation to the Securities Clearing and Settlement Systems in Singapore," May 2004.
Anti-money laundering and combating the financing of terrorism: Improve the effectiveness Of cross-border mutual legal assistance.	**In progress:** Singapore has a continuing program of Mutual Legal Assistance Treaty (MLAT) negotiations with several countries. A few are near completion. In November 2004, Singapore also signed a regional MLAT with seven ASEAN countries.
Capital market development: Review and address factors that may constrain the further development of the corporate bond market, including the limited use of credit ratings, guaranteed interest rates of the central Provident Fund (CPF), and the CPF investment policy.	**Under review**

SINGAPORE—FUND RELATIONS

(As of November 30, 2004)

I. Membership Status: Joined August 3, 1966; Article VIII

II. General Resources Account:

	SDR million	Quota (In percent)
Quota	862.50	100.00
Fund holdings of currency	572.98	66.43
Reserve position in Fund	289.56	33.57

III. SDR Department:

	SDR million	Allocation (In percent)
Net cumulative allocation	16.48	100.00
Holdings	188.86	1,146.30

IV. Outstanding Purchases and Loans: None

V. Financial Arrangements: None

VI. Projected Payments to Fund: None

VII. Exchange Arrangement:

Singapore's exchange rate regime is a managed floating system. The Monetary Authority of Singapore (MAS) monitors its value against an undisclosed basket of currencies and intervenes in the market to maintain this value within an undisclosed target band. The U.S. dollar is the intervention currency. As of November 30, 2004, US$1=S$1.6417.

Singapore has accepted the obligations of Article VIII, Sections 2, 3, and 4 and maintains an exchange rate system that is free of restrictions on the making of payments and transfers for current international transactions.

Singapore maintains restrictions on Singapore-dollar credit facilities, and bond and equity issuance. Singapore-dollar proceeds obtained by nonresident financial entities (such as banks, merchant banks, finance companies, and hedge funds) from loans, equity listings or bond issuance to finance activities outside Singapore have to be swapped or converted into foreign currency upon draw-down. Financial institutions are prohibited from extending Singapore-dollar credit facilities in excess of S$5 million to nonresident financial entities if there is reason to believe that the Singapore-dollar proceeds may be used for Singapore-dollar currency speculation.

VIII. Last Article IV Consultation:

The 2003 Article IV consultation discussions were held in Singapore during December 3-15, 2003, and the consultation was concluded by the Executive Board on March 15, 2004.

IX. FSAP Participation:

The FSAP was undertaken in conjunction with the 2003 Article IV consultation. FSAP missions took place in November 2002, July-August 2003, and September 2003.

X. Technical Assistance: None

XI. Resident Representative: None

SINGAPORE—STATISTICAL ISSUES

Singapore provides data to the Fund generally on a timely basis and meets the SDDS specifications for the coverage, periodicity, and timeliness of the data, and for the dissemination of advance release calendars. The authorities have continued to improve the quality of data, including publishing more disaggregated data, but there are a number of deficiencies in statistical practice, particularly in the external and fiscal areas.

- In early 2003, the Singapore Department of Statistics (DOS) completed a rebasing of the Singapore System of National Accounts to reference year 1995 from 1990. The DOS also made improvements in data sources and methodology. One issue addressed in this exercise was the treatment of a value-added tax, namely the Goods and Services Tax (GST), introduced in April 1994. Also, a reconciliation of various national accounts estimates was conducted, resulting in lower statistical discrepancies, and work on further improvements, particularly with respect to changes in inventories, is ongoing.

- Merchandise trade statistics do not fully include trade with Indonesia, although trade transactions with Indonesia are captured elsewhere in the current account of the balance of payments. In January 2004, the authorities released some trade data with Indonesia covering 2003. The authorities plan to publish additional information on trade with Indonesia as part of their plans to accede to the Harmonized System Convention of the World Customs Organization (WCO).

- In December 2003, the DOS introduced a new reporting format for the BOP's services account that includes the standard services components (except communication services), in line with the fifth edition of the *Balance of Payments Manual (BPM5)*. Other goods and services receipts and payments, which are substantial, used to be not disaggregated. The DOS used data from the Survey on International Trade in Services (launched in 1996) as an additional source for the compilation of more detailed services statistics.

- Information on government assets held abroad is not published nor provided to the Fund. Interest on these assets and debt service payments on domestic debt made from the extrabudgetary Government Securities Fund are published on an annual basis, but are not fully reflected in the fiscal position. More generally, data on the financial position of the consolidated public sector are not published. Singapore has nevertheless complied with the expanded SDDS requirements to include data on the international investment position.

Annual balance of payments data are reported to STA each year. Since September 2004, data on quarterly gross direct and portfolio investment inflows have been provided to STA following the dissemination of such data from the Q1 2004 issue of the *Quarterly Economic Survey of Singapore*.

Singapore—Core Statistical Indicators
(As of December 13, 2004)

	Exchange Rates	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account	Central Government Operations	GDP	External Debt/Debt Service 1/
Date of latest observation	12/13/04	11/04	10/04	10/04	10/04	12/13/04	10/04	10/04	Q3/04	10/04	Q3/04	...
Date received	12/13/04	12/04	11/04	11/04	11/04	12/13/04	11/04	11/04	11/04	11/04	11/04	...
Frequency of data 2/	D	M	M	M	M	D	M	M	Q	M	Q	...
Frequency of Reporting 2/	D	M	M	M	M	D	M	M	Q	M	Q	...
Source of data 3/	N	N	N	N	N	N	N	N	N	N	N	...
Mode of reporting 4/	E	E	E	E	E	E	E	E	E	E	E	...
Confidentiality	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public	...
Frequency of publication 2/	D	M	M	M	M	D	M	M	Q	M	Q	...

1/ Official external debt is zero; data from official sources on private external debt are not available, although a survey to improve reporting in this area has recently been launched.
2/ D-daily; M-monthly; Q-quarterly.
3/ A-direct reporting by authorities; N-official publications and websites.
4/ E-electronic data transfer.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 05/56
FOR IMMEDIATE RELEASE
April 28, 2005
Revised: 5/31/2005

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2004 Article IV Consultation with Singapore

On February 7, 2005, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with Singapore.[1]

Background

In recent years, Singapore's economy has been hard hit by a series of external shocks. These shocks—the Asian crisis, the bursting of the technology bubble, and the SARS outbreak in 2003—disrupted an economic expansion largely uninterrupted since the 1970s. The shocks have come at a time when Singapore is also facing increasing competition from regional low-cost economies. To facilitate an orderly adjustment to these changes, a wide range of structural reforms has been undertaken in the past few years.

Aided by supportive macroeconomic policies and improved external conditions, Singapore's economy has recovered rapidly since mid-2003. Lately, job creation has also gathered strength. The turnaround—mainly driven by exports, reflecting strong global electronics demand, and since early 2004 supported by domestic investment—delivered an unprecedented four straight quarters of double-digit growth from third-quarter 2003 through the second quarter of 2004. Since then, the pace has slackened as electronics exports and domestic consumption slowed. Despite this slowdown, GDP growth is expected to reach around 8 percent in 2004, recovering

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

from 1.1 percent in 2003. Inflation has crept up, but remains low. The current account surplus has narrowed, reflecting higher imports as investment picked up.

With emerging inflationary pressures, the Monetary Authority of Singapore (MAS) announced a modest and gradual tightening of its monetary stance in April 2004, and maintained this position in last October's policy review. After having depreciated by 6½ percent since 2001, the trade-weighted exchange rate index (as calculated by the IMF) appreciated by 1¼ percent in 2004, although it moderated in the latter part of the year.

The current fiscal stance is broadly neutral. The fiscal surplus was over 6 percent of GDP in FY2003, much higher than expected due to lower-than-budgeted capital spending. This year's budget also contains a large planned capital outlay, which, combined with an increase in the goods and services tax rate, aims at keeping the fiscal stance broadly neutral. The budget also includes several measures to support private enterprise and to attract investment, particularly in the wealth management industry.

The financial sector remains robust. Bank profitability and capitalization are strong, and nonperforming loans are low. Local banks have responded to increased domestic competition with the entry of foreign players by consolidating at home and expanding abroad. In June 2004, the minimum capital requirement for local banks was lowered from 12 percent to 10 percent.

An array of structural reforms has been undertaken in the past few years. In response to increasing competition from low-cost regional economies, the government adopted the recommendations of the Economic Review Committee (ERC) in 2003. The ERC recommended measures to enhance competitiveness, promote private entrepreneurship, and facilitate economic diversification. Significant progress has been made in implementing these recommendations, such as increasing wage and labor market flexibility, reducing business costs and taxes, and promoting the outward expansion of Singapore firms and Singapore as a business hub.

Looking ahead, economic activity is expected to moderate to more sustainable levels in the near term. Taking into account the softening in global demand, particularly the cresting of the global electronic cycle, output growth could slow to about 4 percent in 2005. The outlook is subject to some uncertainty, especially on the external front. Despite the expected moderation in activity, however, there is likely to be little slack in the economy, reflecting the recent rapid growth. The tightening in the labor market and high energy prices could raise inflationary pressures. Over the medium term, IMF staff expects growth to average around 4-5 percent.

Executive Board Assessment

Executive Directors welcomed the Singapore economy's strong turnaround since mid-2003, which has owed much to a favorable external environment, supportive macroeconomic policies, and continued structural reforms to diversify the economy and improve its competitiveness. Directors considered that Singapore's sustained fiscal surpluses, lack of external debt, comfortable net asset position, healthy reserves, and large current account surpluses provided a strong buffer against exogenous shocks. At the same time, they welcomed the authorities' determination to resist complacency, and to continue to identify new sources of growth in an increasingly challenging regional and global environment.

Directors observed that growth had begun to slow and was likely to return to more sustainable levels as world demand softened. Given the little slack remaining in the economy following the recent rebound, the moderation in activity could be helpful in restraining inflationary pressures coming from tightened labor market conditions and higher energy prices.

Directors saw the current tightening stance of monetary policy as paving the way for an orderly withdrawal of the stimulus provided in recent years. However, if the downside risks to growth—especially from external factors—were to materialize, threatening a sharper deceleration than expected, Directors considered that monetary policy might need to become more supportive.

Directors welcomed ongoing efforts to increase the transparency of the monetary policy framework, which had been effective in keeping inflation low and stable. A few Directors considered that releasing more detailed information about the government's inflation target and exchange rate policies would be helpful.

Directors agreed that the real exchange rate for the Singapore dollar appeared broadly appropriate notwithstanding the large current account surpluses. It was observed that active foreign investment by the government and the government-linked companies may have kept the real exchange rate from appreciating. However, Directors considered that, as domestic investment recovered from its recent low levels, the current account surpluses were likely to narrow in the period ahead. Keeping exchange rate policy biased toward appreciation, together with greater flexibility, would also help in this regard.

Directors commended the authorities' use of fiscal policy in recent years to support the economy, while adhering to the objective of a balanced operational budget over the medium term. The prudent medium-term fiscal framework had resulted in a significant reserves accumulation that had strengthened investor confidence. Some Directors suggested that the strong fiscal position created scope for additional targeted social spending, particularly on the elderly and the unemployed, and personal income tax reductions. Many Directors also supported the authorities' focus on retraining and job-matching schemes to address the structural changes in the labor market and help reduce unemployment further.

Directors welcomed the recent public review of operations of Temasek, the government's investment holding company, as a milestone in enhancing fiscal transparency. Following this example, they encouraged the authorities to consider publishing general information on the Government of Singapore Investment Corporation (GIC), and to develop and disseminate consolidated public sector accounts. Directors also encouraged the authorities to undertake a fiscal Report on the Observance of Standards and Codes (ROSC) in the near future.

Directors supported the authorities' implementation of structural reforms to enhance competitiveness and sustain growth in the medium term. Significant progress had been made in increasing labor market and wage flexibility and reducing business taxes and costs. Also encouraging were the quality upgrading and diversification taking place in the manufacturing sector, and the emergence of Singapore as a hub for regional asset management, health, and education services. Directors welcomed the government's adoption of the recommendations of the Economic Review Committee, aimed at furthering research and development and investment in human capital. Many Directors observed that a faster pace of divestment of those government-linked companies not of strategic importance to the country would promote entrepreneurship and the growth of the private sector. Others, however, agreed with the authorities' careful approach.

Directors viewed the financial system as robust, benefiting from an efficient legal system and good accounting standards. They welcomed the authorities' increasing attention to the regulatory challenges arising from banks' overseas expansion. They commended the progress made in implementing the recommendations of the Financial System Stability Assessment (FSSA), and looked forward to the timely operationalization of the remaining recommendations.

Directors noted that a key challenge of Singapore's aging population was to ensure that the retired are adequately provided for. Thus, they welcomed the recent measures to refocus the Central Provident Fund (CPF) as a core retirement scheme. They recommended that, to make participation in the CPF's investment scheme more attractive, the scheme's transaction costs be reduced, by pooling funds under a smaller number of asset managers with simpler portfolio choices.

Directors welcomed the authorities' continued efforts to improve data quality, which they agreed was broadly satisfactory for surveillance purposes. They encouraged the authorities to begin a comprehensive review of the statistical base by participating in a data ROSC in the near future.

Singapore: Selected Economic Indicators

	2001	2002	2003	2004 Est.		2005 Proj.
Growth (percent change)						
Real GDP	-1.9	2.2	1.1	8.1		4.0
Consumption	3.5	2.5	-0.4	6.3		3.4
Gross fixed investment	-4.5	-9.9	-3.8	7.5		1.9
Change in inventories 1/	-5.7	0.4	-6.2	2.6		1.0
Net exports 1/	3.6	3.6	8.7	-0.1		-0.7
Saving and investment (percent of GDP)						
Gross national savings	43.6	42.5	44.2	45.1		40.3
Gross capital formation	24.9	21.2	13.4	16.3		17.0
Inflation and unemployment (period average, percent)						
CPI inflation	1.0	-0.4	0.5	1.7		1.6
Unemployment rate	3.3	4.4	4.7	4.0		3.5
Central government (percent of GDP) 2/						
Revenue	27.2	23.0	20.8	20.7		20.5
Expenditure	23.7	18.7	14.4	17.6		17.5
Overall balance	3.5	4.2	6.3	3.1		3.0
Money and credit (end of period, percent change)						
M3	4.0	-0.8	5.9	4.6	4/	...
Credit to private sector	16.3	-8.6	5.4	5.1	4/	...
Interest rate (three-month interbank, in percent)	1.3	0.8	0.8	1.4	4/	...
Balance of payments (US$ billion)						
Current account balance	16.1	18.9	28.2	29.8		26.2
(In percent of GDP)	(18.7)	(21.4)	(30.9)	(28.8)		(23.3)
Overall balance	-0.9	1.3	6.8	15.7		1.7
Gross official reserves	75.8	82.3	96.3	112.8		...
Exchange rate						
S$/US$ (end of period)	1.851	1.737	1.701	1.634		...
Nominal effective exchange rate 3/	121.2	120.2	115.7	114.0	5/	...
Real effective exchange rate 3/	108.2	105.7	101.0	98.4	5/	...

Sources: Data provided by the Singapore authorities; and IMF staff estimates and projections.

1/ Contribution to GDP growth.
2/ Fiscal year beginning on April 1.
3/ IMF Information Notice System monthly index (1990 = 100); period average.
4/ As of end-October 2004.
5/ As of end-September 2004.

Statement by the Singapore Authorities
February 7, 2005

Introduction

The Singapore authorities would like to thank the IMF staff for the 2004 Article IV Consultation. The discussions with the staff on various issues pertaining to recent developments and outlook of the Singapore economy, as well as longer-term structural policies were useful and stimulating. The authorities also welcome the three interesting studies contained in the Selected Issues paper, which provided the opportunity to explore topical issues in greater depth. This statement provides an update on the latest economic developments in Singapore and discusses some of the policy issues raised in the Staff Report.

Recent Economic Developments and Outlook

The Singapore economy has rebounded since mid-2003, underpinned by an upturn in demand in key export markets, supportive macroeconomic policies and continued structural reforms, which have strengthened the competitiveness of domestic businesses in international markets. GDP growth reached a four-year high of 8.1 percent in 2004, boosted by double-digit growth in the first half of the year. In the second half, GDP growth slowed to a more moderate pace, with both manufacturing and services sectors recording weaker growth, following above trend rates of expansion earlier in the year.

The strong economic rebound has in turn led to the creation of 66,200 jobs last year. As a result, the unemployment rate fell to 3.7 percent in Q4 2004, down from 4.6 percent as at end-2003. Going forward, Singapore's GDP is likely to grow at a more modest pace of 3-5 percent in 2005, reflecting expectations of weaker growth in the external economies and the global IT industry.

Domestic inflationary pressures have been on the rise as a result of the strong economic recovery and higher commodity prices. Nevertheless, overall CPI inflation was capped at 1.7 percent in 2004. For 2005, CPI inflation is likely to come in at 1-2 percent, reflecting the pass-through of high commodity prices as well as firming domestic cost pressures.`

The government is also pushing on with structural reforms to enhance Singapore's growth prospects. In particular, Singapore will continue to develop technologically advanced industries and applications such as pharmaceuticals, biotechnology and nanotechnology, and move up the "quality ladder" to stay competitive in the region. This strategy has already met with success as observed by the staff in its study on Singapore's export composition. Indeed, there were more than 3,600 high-tech business start-ups in Singapore last year. At least a quarter of them were foreign enterprises from countries in the Asia-Pacific region, attracted by the presence of a diverse pool of international players, the availability of alternative sources of funding, and connectivity to markets within the region and beyond. In addition, Singapore has made considerable progress in developing niche areas in fund management, healthcare, and education.

Monetary and Fiscal Policy

Singapore's overall macroeconomic policy stance has evolved in line with the economy's cyclical developments over the past few years. Fiscal and monetary policies were expansionary in 2002 and 2003, to assist businesses and workers who were adversely affected by the economic downturn and facilitate the recovery process. The policy stimulus was gradually withdrawn with the improvement in underlying economic conditions in 2004 and as the output gap turned positive by the middle of the year.

Monetary Policy

In April 2004, the Monetary Authority of Singapore (MAS) shifted from a neutral to a tighter monetary policy stance in anticipation of rising inflationary pressures amidst a strong cyclical upswing in the economy. The appreciating policy stance of targeting a modest and gradual appreciation of the Singapore dollar nominal effective exchange rate (S$NEER) was subsequently reaffirmed in October.

The MAS is of the view that the appreciating policy stance remains appropriate in anchoring price expectations in the domestic economy, even as economic growth slows to a more moderate pace in 2005. The policy stance will be reviewed in April 2005, taking into account the underlying economic conditions and prospects at that time. Should the outlook change significantly in the interim, the MAS is ready to make the necessary adjustment to the policy stance. Moreover, the flexibility accorded by the exchange rate policy band would, in the first instance, accommodate any unexpected slowdown in economic activity.

The authorities welcome the staff's endorsement of the initiatives taken to enhance transparency of the policy framework. Since the public release of the Monetary Policy Statement in 2001, the authorities have been disclosing information on the historical movements of the S$NEER and on key parameters of the policy band where this would not compromise the effective management of the exchange rate or cause disruption to the markets. As a result, market participants have a very good understanding of the policy stance.

Fiscal Policy

The fiscal stance will be appropriately neutral, in line with expectations for the economy to grow at its potential in 2005. The government will seek to restore budget balance and ensure fiscal sustainability going forward. The FY2005 Budget will be announced on February 18, 2005, and can be expected to address the three-broad areas of enhancing Singapore's economic competitiveness, assisting vulnerable groups such as the elderly and unemployed, and assuring fiscal sustainability.

In addressing the needs of the vulnerable segments, the government will adopt measures that target those who are most in need, while ensuring that there is no erosion of the work ethic. The government has announced its intention to provide greater assistance to Singaporeans through top-ups to a newly-established Community Care Fund[1] and the existing Medifund[2]. A new Re-employment Assistance Programme will be launched to help older, less skilled workers through job redesign, job referrals, and skills upgrading. The experience with the former re-employment scheme has been encouraging with some 21,000 mature workers acquiring new jobs during the recent economic downturn.

Financial Sector Issues

FSSA Recommendations

Many of the FSSA recommendations have been implemented. With regard to the key policy recommendation for anti-money laundering and combating the financing of terrorism, the MAS would like to point out that Singapore has a continuing programme of Mutual Legal Assistance Treaty (MLAT) negotiations with several countries, with a few of them near completion. In November 2004, Singapore also signed a regional MLAT with seven ASEAN countries. The MAS will address the other recommendations where appropriate.

Corporate Governance and Disclosure

The authorities note that Singapore's regulatory regime for listed companies is premised on accurate and timely disclosures by issuers, and effective enforcement when laws are breached. In recent years, Singapore’s disclosure, accounting and corporate governance standards have been substantially enhanced and are in line with international best practices. In particular, failure by listed companies to disclose material information on a timely basis has attracted criminal and civil liabilities under the Securities and Futures Act since 2002. Quarterly reporting for larger listed companies (with a market capitalisation above S$75 million) and mandatory compliance with accounting standards, which are aligned with International Accounting Standards, were introduced in 2003. All listed companies must explain deviations from the Code of Corporate Governance in their annual reports.

The authorities recognise that scandals and failures can occur in any financial centre. No amount of regulation or enforcement can guarantee that a company will never deviate from disclosure rules and corporate governance standards. The hallmark of a well-regulated centre is how effectively it responds and deals with such events. In this connection, the China Aviation Oil case is currently being investigated by the relevant authorities. Appropriate

[1] The Community Care Fund is managed by the community development councils, and is used to fund financial assistance to needy families.

[2] Medifund helps individuals in the low-income group who are unable to pay for their medical care, either by themselves or with the help of their family, despite government subsidies.

enforcement actions will be taken if any laws or regulations are found to have been breached. Once the results of the investigations are clear, the MAS will review the need for any changes to the rules and standards of corporate governance and market conduct.

Other Issues

Central Provident Fund (CPF)

The government is refocusing the CPF as a core retirement scheme, to help ensure that Singaporeans set aside sufficient savings for their retirement years. To improve long-term returns on members' CPF savings, reduce members' investment cost and provide simpler choices, the CPF Board explored the possibility of introducing privately-managed pension plans (PPPs) as an option under the CPF Investment Scheme. Following an extensive industry and public consultation last year, the CPF Board will be assessing the framework for PPPs and studying other pension funds to determine the most appropriate model that would serve the majority of CPF members' needs.

Government-linked Companies (GLCs)

The staff had observed that the performance of Temasek's companies stood in contrast to the generally held view of unprofitable and inefficient state-controlled enterprises. This attests to the fact that GLCs are operated strictly on a commercial basis and enjoy no favours or guarantees from the government. They are held to the same high levels of corporate governance and regulatory standards as other companies in the private sector. On the issue of divestment, Temasek has consistently made clear its intent to divest stakes in companies that are not of strategic interest to the country. This commitment is evidenced by its divestment of stakes in 36 companies over the last two years.

The authorities would like to reiterate that competition has always been a key tenet of Singapore's economic strategy, as it leads to greater productivity gains and more efficient resource allocation. To reinforce Singapore's pro-enterprise and competition policies, the Competition Commission of Singapore was established in January this year following the enactment of the Competition Act.