BOX ARTICLE 1.1

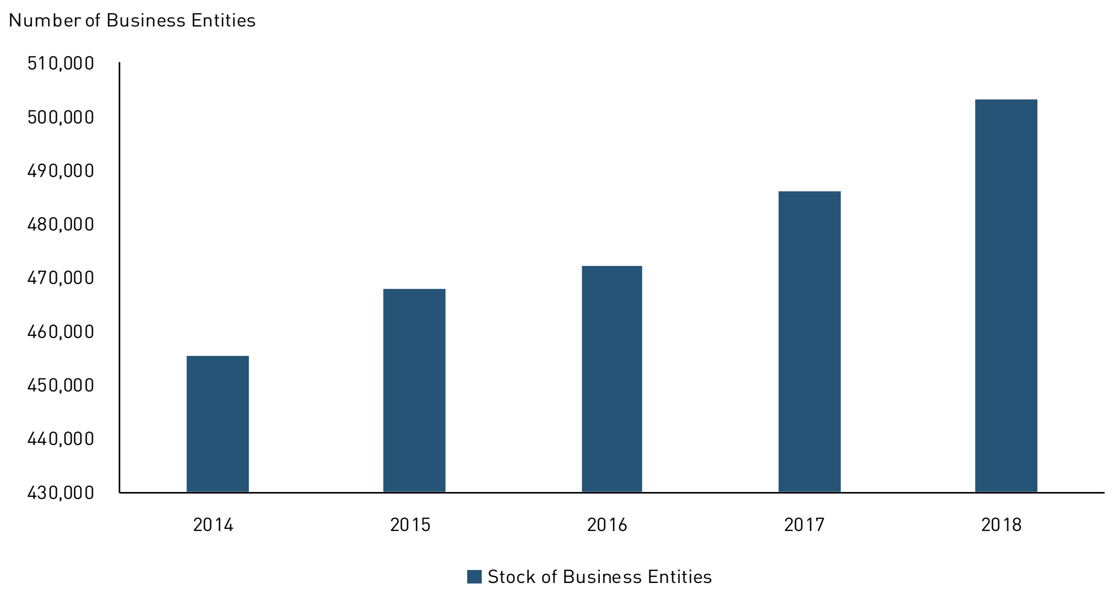
Singapore's Corporate Sector: Recent Trends in Firm Formation and Cessation

In 2017, MTI published an article on the formation and cessation trends of business entities in Singapore over the period of 2010 to 2016.[1] This article examines more recent data from the Accounting and Corporate Regulatory Authority (ACRA) in view of the slowdown in the Singapore economy, with a focus on the formation and cessation of companies and businesses,[2] which make up the vast majority of business entities in Singapore.[3]

The stock of business entities in Singapore grew between 2014 and 2018 on the back of strong net formation of business entities

The total number of business entities in Singapore increased between 2014 and 2018 on the back of strong net formation (i.e., formation minus cessation) of business entities. Over this period, the net formation of business entities averaged 16,520 per year. As a result, the stock of business entities rose from 455,280 in 2014 to 503,130 in 2018 (Exhibit 1).

Exhibit 1: Stock of Business Entities, 2014 – 2018



Source: ACRA

1 "Singapore's Corporate Sector: Recent Trends in Firm Formation and Cessation", Economic Survey of Singapore Second Quarter 2017.
2 A company is a business entity incorporated under the Companies Act consisting of at least (i) one director, (ii) one secretary and (iii) one member. On the other hand, a business is an entity formed either as a sole-proprietorship or partnership consisting of two to twenty members. In terms of liability, a company is a separate legal entity, which means that its directors and members are generally not personally liable for the debts and obligations incurred by the company. On the other hand, business owners are generally accountable for any obligations borne by the business. A more detailed comparison of the different types of business entities in Singapore can be found on ACRA's website.
3 As at end-2018, companies and businesses made up around 67% and 30% of total business entities respectively. The remaining business entities consisted of limited liability partnerships, limited partnerships and public accounting firms.

However, the net formation of business entities softened in the first three quarters of 2019

In line with slower economic growth, the net formation of business entities in the economy has weakened this year. Although still positive, the net formation of business entities was about 9,880 in the first three quarters of 2019, around a third lower than the 14,220 in the same period of 2018 and around a quarter lower than the average of 13,780 in the same period of 2014 – 2018.

The recent decline in the net formation of business entities comes amidst heightened uncertainties in the global economy and the resulting slowdown in the Singapore economy, which have led to a fall in the formation of business entities and an uptick in the cessation of business entities. The following sections describe the formation and cessation trends for companies and businesses in greater detail.

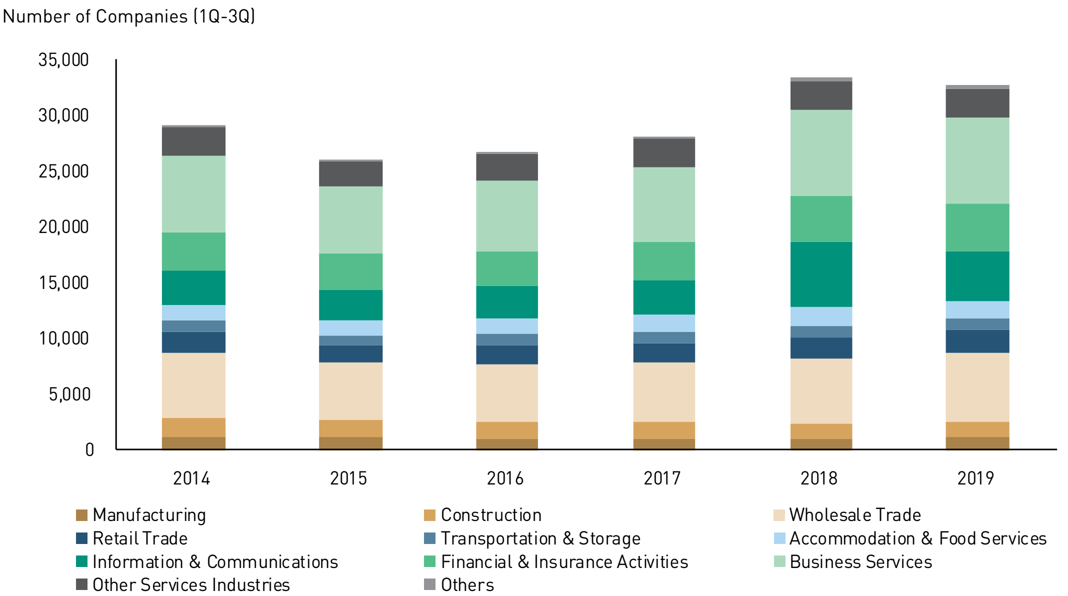
In the first three quarters of 2019, the number of new companies and new businesses formed in Singapore fell slightly

The formation of new business entities is an important indicator of economic health. In particular, the creation of new firms leads to the generation of new jobs and investments. A high level of firm entry may also reflect a vibrant start-up landscape. Conversely, a challenging economic environment is likely to dampen firm formation, as potential entrepreneurs may hold back from setting up new firms given the economic uncertainty and fewer potentially profitable business opportunities.

Against the backdrop of the current slowdown in the Singapore economy, the number of new companies formed came in at 32,650 in the first three quarters of 2019, slightly weaker than the 33,320 recorded in the same period of 2018 (Exhibit 2). However, if we look further back to the five years prior to 2019, the number of new companies formed in 2019 to-date remained larger than the average of 28,660 in the same period of 2014 – 2018. This suggests that overall company formation in the Singapore economy has remained resilient despite weaker economic conditions.

In terms of sectors, the information & communications sector was the main contributor to the on-year decline in company formation in the first three quarters of 2019. In turn, the comparatively weaker company formation in the sector can primarily be attributed to the surge in new companies formed in the IT & information services segment of the sector in the same period of 2018, particularly in areas related to the development of software and programming activities. However, notwithstanding the drop in formation, the 4,310 companies formed in the sector in 2019 to-date was still higher than the average of 3,530 clocked over the same period of 2014 – 2018, underscoring the increasing prominence of the digital economy.

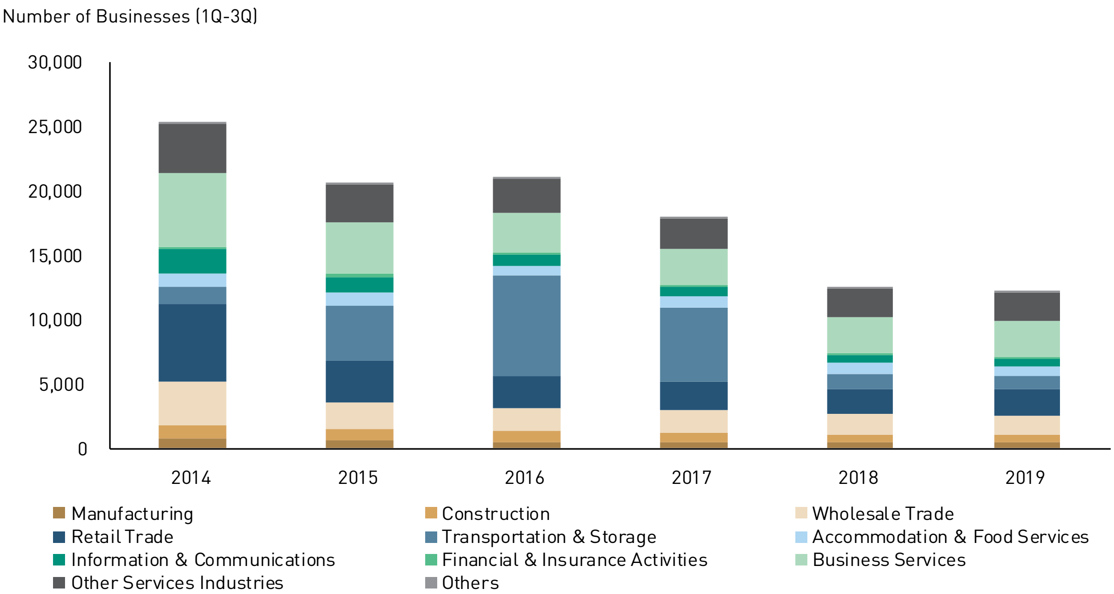
Exhibit 2: Number of Companies Formed by Sectors (1Q – 3Q), 2014 – 2019



Source: ACRA
Note: The "Others" category includes activities not elsewhere classified, such as agriculture, mining and utilities.

As for businesses, the number of new businesses formed also dipped slightly to 12,160 in the first three quarters of 2019, from the 12,520 registered in the same period of last year (Exhibit 3). At a sectoral level, the wholesale trade sector was the key contributor to the decline. The fall in business formation in the wholesale trade sector can in turn be attributed to weak economic conditions in the sector.[4]

Exhibit 3: Number of Businesses Formed by Sectors (1Q – 3Q), 2014 – 2019



Source: ACRA

4 *Based on the Wholesale Trade Index, domestic wholesale sales volume fell by 4.6% and foreign wholesale sales volume contracted by 3.8% on a year-on-year basis in the first three quarters of 2019.*

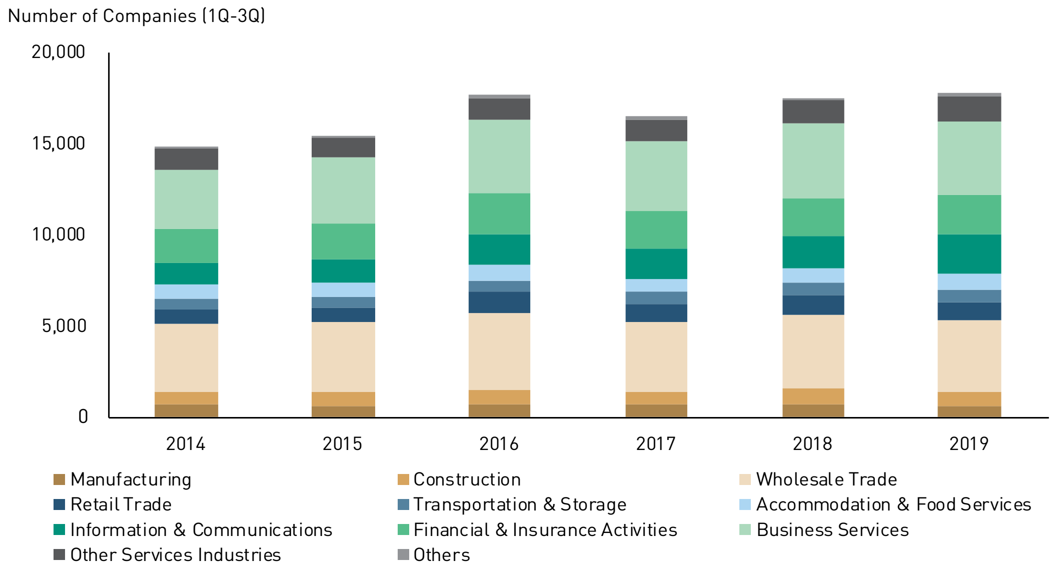
Compared to the last five years, the 12,160 new businesses formed in the first three quarters of 2019 was considerably lower than the average of 19,460 registered in the same period of 2014 – 2018. Although this decline was seen across all sectors, it was driven primarily by the transportation & storage sector. However, the drop in business formation in the transportation & storage sector should be seen in the context of the significant increase in business formation between 2015 and 2017 due to business registrations by drivers providing private car-hire services via platforms such as Uber and Grab. With the regulatory changes in late-2017 that did away with the need for such business registrations,[5] business formation in the sector had fallen in tandem.

While the number of company and business cessations rose in the first three quarters of 2019…

Firm cessation is an inherent part of economic restructuring, in which unproductive firms exit the market, thus freeing up capital and labour so that they can be put to better use. Changes in firm cessation may also be a reflection of the economic cycle, with firm exits increasing when economic conditions weaken.

Amidst the economic slowdown and ongoing economic restructuring, the cessation of companies registered a slight uptick to reach 17,720 in the first three quarters of 2019, from 17,490 in the same period of 2018. The uptick in company cessations was primarily driven by a higher number of company closures in the information & communications sector (Exhibit 4). The latter follows from a sharp increase in the number of start-ups formed in the IT & information services segment of the sector in recent years, some of which would have subsequently ceased operations.

Exhibit 4: Number of Companies Ceased by Sectors (1Q – 3Q), 2014 – 2019

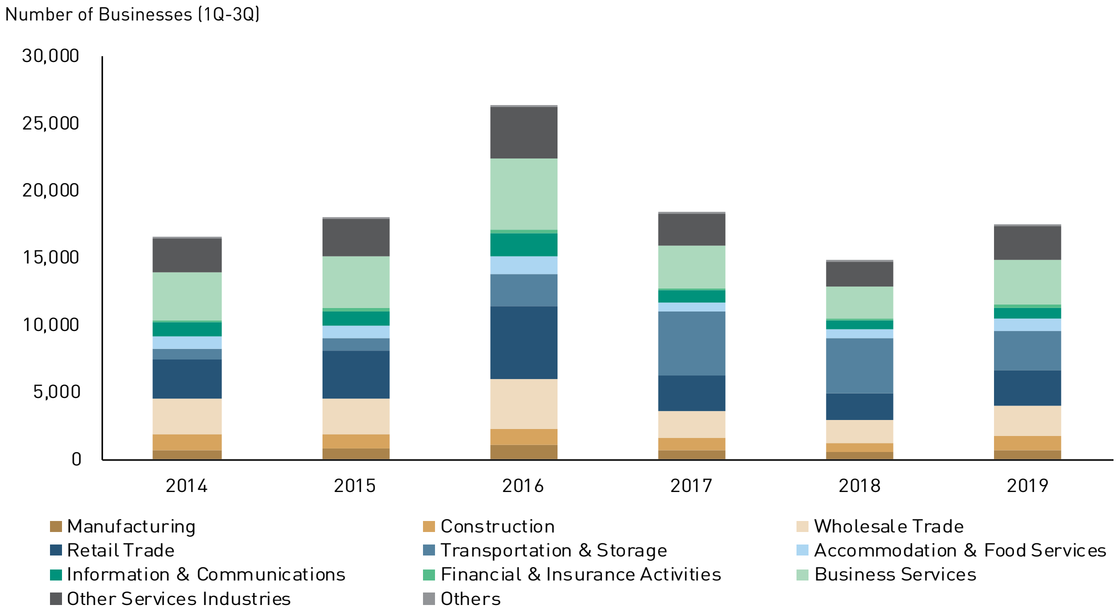


Source: ACRA

5 *Since 1 October 2017, individuals who wish to own a private hire car are no longer required to register a business entity with ACRA.*

Business cessations also rose in the first three quarters of 2019, coming in at 17,430 as compared to the 14,710 recorded over the same period of 2018. The rise in business cessations was broad-based, with all sectors experiencing an increase except for the transportation & storage sector (Exhibit 5). This likely reflects a more challenging environment facing businesses amidst the economic slowdown.

Exhibit 5: Number of Businesses Ceased by Sectors (1Q – 3Q), 2014 – 2019



Source: ACRA

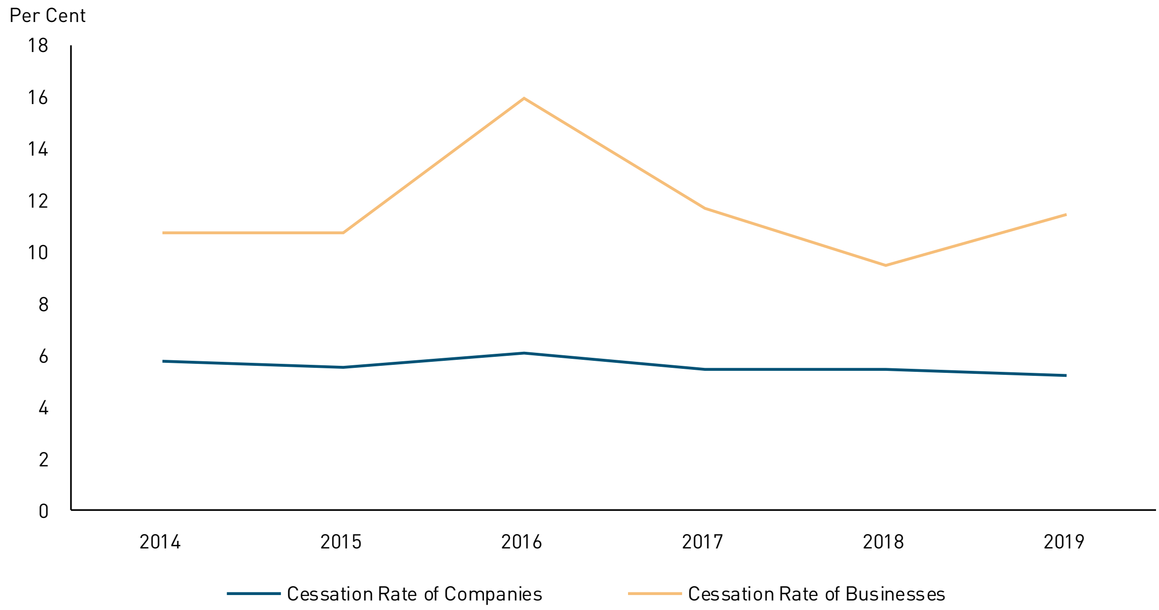
... their cessation rates over a longer time horizon suggest that the overall health of companies and businesses has not deteriorated significantly

It is important to note that while the increase in company and business closures could be driven in part by the slowdown in economic activities this year, it could also partly reflect the rising stock of companies and businesses in the economy over time. To account for the latter, we compute the cessation rates[6] of companies and businesses, and examine how they have changed over time.

From Exhibit 6, we can see that the cessation rate of companies came in at 5.3 per cent in the first three quarters of 2019, comparable to that in the same period of 2018 (5.5 per cent) but lower than the average seen in the same period of 2014 – 2018 (5.7 per cent). For businesses, the cessation rate picked up in the first three quarters of 2019 to 11.6 per cent, from 9.6 per cent in the same period of 2018. The uptick in the cessation rate of businesses (unlike the case for companies) suggests that businesses may be more vulnerable to economic slowdowns than companies, as they likely have weaker balance sheets and may lack access to financing to tide over a period of slower economic growth. Nevertheless, if we take a longer time horizon, the cessation rate of businesses in 2019 to-date remained comparable to the average of 11.8 per cent recorded over the same period of 2014 – 2018.[7]

6 *In this article, cessation rate is defined as the number of firms that had ceased operations in the first three quarters of a particular year out of the total number of firms at the end of the preceding year.*
7 *Excluding 2016, the average cessation rate for businesses in the first three quarters of 2014-2018 was 10.8%.*

Exhibit 6: Cessation Rates of Companies and Businesses (1Q – 3Q), 2014 – 2019



Source: ACRA, MTI estimates
Note: The sharp rise in the business cessation rate in 2016 was primarily due to a spike in business cessation in the retail trade and transportation & storage sectors. In turn, the former was because of sluggish retail (excluding motor vehicle) sales over this period, while the latter could be due to drivers providing private car-hire services exiting the industry.

Overall, the trends in cessation rates suggest that the overall health of companies and businesses has not deteriorated significantly despite the economic slowdown.

Conclusion

Given the economic slowdown amidst heightened global economic uncertainties, the net formation of business entities in the first three quarters of 2019 came in lower than that in the same period of last year, as the formation of business entities fell and the cessation of business entities rose. Although the number of company and business closures this year has inched up, the cessation rates of companies and businesses in the first three quarters of 2019 remained broadly comparable to their respective longer-term averages, suggesting that the overall health of firms has not deteriorated significantly. The Government will continue to monitor the situation closely, and stands ready to step up support for firms and workers if it becomes necessary, with a focus on building capabilities for the longer term.

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