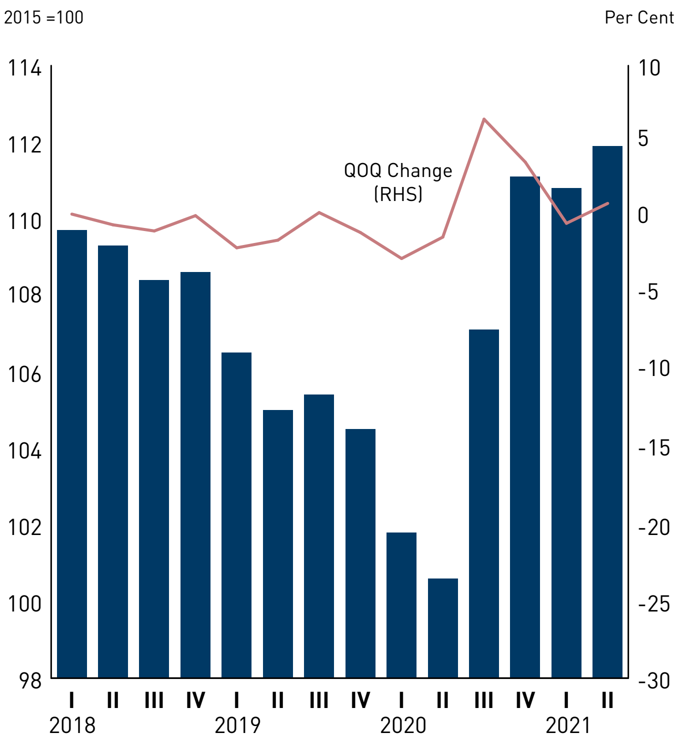
CHAPTER 3
ECONOMIC OUTLOOK

LEADING INDICATORS

On a quarter-on-quarter basis, the composite leading index (CLI) increased by 1.0 per cent in the second quarter of 2021, a turnaround from the 0.3 per cent decline in the previous quarter (Exhibit 3.1).

Of the nine components in the CLI, three components saw a quarter-on-quarter increase, namely wholesale trade, stock price and domestic liquidity. By contrast, the stock of finished goods, money supply, US Purchasing Managers' Index, new companies formed and non-oil sea cargo handled declined compared to the previous quarter. Meanwhile, non-oil retained imports was flat.

Exhibit 3.1: Composite Leading Index Levels and Growth Rate



OUTLOOK FOR 2021

In May, MTI maintained Singapore's GDP growth forecast for 2021 at "4.0 to 6.0 per cent", in view of heightened uncertainties in the external economic environment arising from the COVID-19 pandemic, as well as the domestic health situation.

Since then, COVID-19 cases continue to be on the rise globally due to the spread of the highly transmissible Delta variant. However, vaccination rates have also picked up in key advanced economies such as the US and Eurozone, which have in turn allowed them to press on with their re-opening plans notwithstanding an uptick in cases. By contrast, regional economies which have been slow to vaccinate their populations have had to re-impose restriction measures to curb a resurgence in infections. This has in turn dampened their growth outlook. On balance, the recovery in external demand for Singapore for the rest of the year remains largely on track. Details of the outlook of the key external economies are as follows.

In the US, the pace of economic growth is expected to pick up in the second half of 2021. Continuing improvements in labour market conditions, along with elevated savings due to the disbursement of fiscal stimulus cheques, will bolster personal consumption expenditure, which will in turn support the US' economic recovery. The Eurozone economy is also projected to see a faster pace of recovery in the second half of 2021. The strong pickup in vaccine deployment in recent months has led to a quicker-than-expected resumption in business activity. This has resulted in an improvement in business sentiments and employment expectations, which will support a rebound in domestic demand.

In Asia, China's growth is expected to ease in the second half of 2021 on the back of a moderation in investment growth amidst weaker base effects and credit conditions. The latest COVID-19 outbreak could also weigh on the recovery of consumption in the near term as restrictions have been imposed to contain the virus. In Japan, the pace of economic recovery is projected to quicken in the second half of 2021. While the re-imposition of a state of emergency in Tokyo and Okinawa to slow the spread of the virus is expected to weigh on domestic consumption in the near term, strong external demand will continue to support growth.

Growth in the key Southeast Asian economies in the second half of 2021 is likely to be slower than earlier projected. In particular, the recovery in domestic demand in countries such as Malaysia, Indonesia and Thailand are expected to be dampened by the tightening of restrictions to contain the surge in COVID-19 infections, although external demand should lend some support to their GDP growth.

At the same time, downside risks in the global economy remain. First, there continues to be uncertainty surrounding the trajectory of the COVID-19 pandemic. The ongoing economic recovery in advanced economies could be derailed if vaccination progress stalls due to vaccine hesitancy or if the efficacy of existing vaccines is weakened as a result of virus mutations or waning antibody levels. Meanwhile, effective containment of the outbreaks in regional economies may be impeded by their slow vaccination rollouts, which could then lead to an even sharper and more protracted period of slowdown in these economies. Second, there are upside risks to inflation, especially if supply-side bottlenecks persist alongside a stronger pickup in final demand. This could result in an earlier or larger increase in interest rates than currently anticipated, thereby triggering a sharp tightening of global financial conditions. The latter could in turn lead to a premature withdrawal of policy support in economies with limited fiscal space and delay their economic recovery. Third, continued geopolitical uncertainty involving the major economies could weigh on trade and the global economic recovery.

Domestically, the performance of the Singapore economy in the first half of 2021 was stronger than expected. The COVID-19 situation has also stabilised, with our vaccination programme continuing to make good progress. Barring a major setback in the global economy, the Singapore economy is expected to continue to see a gradual recovery in the second half of the year, supported in large part by outward-oriented sectors. The progressive easing of domestic and border restrictions as our vaccination rates continue to rise will also help to support the recovery of our consumer-facing sectors and alleviate labour shortages in sectors that are reliant on migrant workers.

Against this backdrop, the recovery of the various sectors of the economy over the course of the year is expected to remain uneven. First, the growth prospects for outward-oriented sectors (e.g., manufacturing and wholesale trade) remain strong given the rebound in global demand. In particular, the manufacturing sector is projected to see robust growth, driven largely by the electronics and precision engineering clusters on the back of strong semiconductor and semiconductor equipment demand. At the same time, the growth outlook for the finance & insurance and information & communications sectors remains positive. The former will be supported in part by an expected increase in domestic and foreign credit demand alongside the broader economic recovery in Singapore and the region. Meanwhile, the latter will be bolstered by healthy enterprise and consumer demand for digital solutions & services, as well as games & software publishing activities.

Second, the aviation- and tourism-related sectors (e.g., air transport and arts, entertainment & recreation) are projected to recover more slowly than previously expected. Even though domestic border restrictions may be eased towards the later part of the year, especially for travellers from countries that have managed to control the pandemic and vaccinate a large part of their populations, demand is not expected to return quickly as travel restrictions globally are likely to be lifted cautiously and global travel demand may also remain sluggish amidst the spread of more contagious strains of the virus. As such, activity in these sectors is expected to remain significantly below pre-COVID levels even by the end of the year.

Third, while consumer-facing sectors (e.g., retail trade and food & beverage services) have been adversely affected by ongoing domestic restrictions (e.g., dining-in limits), they should start to recover as the restrictions are eased over the course of the year and consumer sentiments improve in tandem with better labour market conditions. Nonetheless, these sectors are not expected to return to pre-COVID levels by year-end, in part due to the subdued tourism outlook.

Fourth, the construction and marine & offshore engineering sectors are projected to see some recovery from the low base last year. However, labour shortages arising from prevailing border restrictions on the entry of migrant workers, especially from South Asia, are likely to continue to weigh on the recovery of activities at worksites and shipyards. While border restrictions may be eased towards the later part of the year, thus alleviating labour shortages, the output of these sectors is expected to remain substantially below pre-COVID levels even at the end of the year.

Taking into account the better-than-expected performance of the Singapore economy in the first half of the year, as well as the latest external and domestic economic developments, **MTI has upgraded the GDP growth forecast for 2021 to "6.0 to 7.0 per cent", from "4.0 to 6.0 per cent".**