

A Strong 2006 Performance and Official GDP Forecast Revised Up 4.5-6.5% for 2007

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- Singapore Economy performed better than expected in 4Q06, coming in at 6.6%/y, revised up from the 5.9% reported in the advance estimates. This was largely due to stronger growth registered in all the broad sectors during the quarter.
- For the full year, GDP expanded at 7.9% in 2006 from a revised 6.6% in the previous year. The government's outlook for 2007 has improved in part due to the positive global developments in recent months and they have accordingly upgraded their 2007 GDP growth forecast range to 4.5-6.5% (from 4-6% previously)
- We are fairly optimistic that domestic demand, pharmaceuticals, transport engineering, the financial sector and an improving construction outlook would continue lend support to the Singapore economy and we expect GDP in 2007 to expand by a more moderate but respectable 5.2%.
- The improved 2007 economic outlook and the expected delay of the 2% GST hike till Jan 2008 suggests no change in MAS' current 'modest and gradual appreciation of the SGD stance' in April's monetary policy meeting.

The government released the final GDP data for 4Q06 and the whole of 2006 this morning (14 Feb 2007, 8.00am). After expanding 7.0%/y/y in 3Q06, Singapore's 4Q GDP moderated its pace of expansion, coming in at 6.6%, revised higher from the previously announced 5.9% in the Jan advance estimates. The upward improvement which came in better than UOB's expectation (UOB and Mkts: 6.0%) was due to upward revisions to all the major economy segments including a stronger manufacturing sector performance (revised to 7.7% to 7.3%) as well as more buoyant construction activity (revised to 4.7% to 2.3%). Services sector contribution was also revised higher to 6.6%/y/y (from 6.0%). On a sequential basis, the fourth quarter GDP expanded at a faster pace of 7.9%/q SAAR compared to the previous quarter's revised 3.9%.

For the full year 2006, GDP expanded at 7.9%, higher than the revised 6.6% recorded in the previous year. This was slightly higher than our forecast of 7.8% as segments of manufacturing, domestic demand and construction activity provided support to the economy although global electronics demand has visibly weakened in the 2nd half of 2006. The government's outlook for 2007 has improved in part due to the positive global developments in recent months and they have upgraded their 2007 GDP growth forecast to 4.5-6.5%. (Previously, the range was 4-6%.) Going into 2007, we are fairly optimistic that domestic demand, pharmaceuticals, transport engineering, the financial sector and an improving construction outlook would continue lend support to the Singapore economy. After a strong 2006 performance, we expect 2007 to expand by a more moderate but respectable 5.2%, well within the revised official forecast range.

After a strong 2006 performance, we expect growth for Singapore to moderate in 2007 in tandem with an anticipated slowdown in US as well as softer global electronics demand. While manufacturing growth is expected to moderate in 1H07 along with slower non-oil domestic exports, we expect electronics demand to begin recovering by mid-2007. For the next few months, we continue to expect softer global demand for semiconductors and some moderation in the electronics output growth due to base effect as well as weaker growth prospects for our main export markets, the US economy going into 2007.

Nonetheless, there is positive news suggesting that the global chips demand will start picking up in 1H07 with the launch of Microsoft's Vista Operating System to the consumers. However, views on the impact of the Vista debut on PC sales have been mixed. Chip makers like Micron and Samsung have been very upbeat and predicted rising demand for faster chips as the new OS would require more memory in PCs and laptops while some analysts believed that the impact may be exaggerated because about 66% of PCs in US already have enough memory to run Vista. On balance, Vista could encourage some additional corporate and consumer PC upgrades but the spillover benefits to chipmakers may be lower than expected on the account of a more moderate Vista take-up rate. So we may yet see a rebound in electronics as early as end-2Q07 but not in a big way.

In 2006, biomedical and transport engineering were the star performers within Singapore's manufacturing sector. Biomedical manufacturing would continue to support growth in manufacturing sector in, especially pharmaceutical output which has been robust for 2006 (26.7%) notwithstanding the volatile monthly swings. Transport engineering which has been registering healthy double-digit growth since March 2004 is also expected to perform strongly next year. Strong aerospace and related activities are also likely to further support to transport engineering output.

The construction sector provided a pleasant surprise in 2006 as the sector expanded by a revised 2.3% after recording a mild 0.7% growth in 2005 following 5 years of contraction, possibly signaling a revival of the construction industry here. (The revision in the 2005 GDP data led to the construction sector registering a slight positive growth rate instead of a 1.1% contraction.) We anticipate the outlook for construction to shine even brighter in 2007 as the sector is set to be kept busy with the record amount of en-bloc sales in 2006 starting to translate into new property construction and the new commercial developments along Orchard road and the construction of the two IRs. Although the recent Indonesian ban on sand exports to Singapore will increase building costs (estimated at 1-3% increase by government sources), we feel the impact to be mild and with the Singapore government's assurance of fixing the price of construction sand (slightly below the current rate) to ensure stable prices and bearing part of the higher construction costs due to dearer sand supplies, we think it should not derail the recovery of the building sector.

While the USD had strengthened against the SGD overnight, the better-than-expected GDP data released today should have some positive upside to the SGD. Indeed prior to the data release, the pair was trading at 1.5414. Currently, the pair is trading lower at 1.5386 and the SGD NEER continues to trade around 2% above the policy mid-point this morning. Upside on SGD is expected to be capped at 1.5300 against the USD today. The markets are now likely to look towards more Singapore data coming up this week including the FY2007 Budget tomorrow which will probably keep investors cautious especially before the Lunar New Year holidays next week. Downside risks in the Budget for the SGD include a 1% corporate tax cut instead of the expected 2% and increases to stamp duties or other negative changes to property-related items.

The positive outlook for 2006 as evidenced by the upward revision of the GDP forecast range this year plus our expectation of the 2% GST hike coming in only in Jan 2008, may likely indicate MAS will re-affirm its current 'modest and gradual appreciation of the SGD stance' in Apr 07. However, with SGD NEER already at the 2% threshold of our in-house SGD NEER model, we maintain that USD/SGD downside will be limited for now - with the USD/SGD pair probably trading around 1.53-1.545 range. Towards the year-end, with more RMB appreciation (albeit at a gradual pace), we maintain USD/SGD towards 1.48.

Singapore's GDP Grew Faster in 4Q06, by 7.9% q/q saar Compared to 3Q's Revised 3.9%

	Weight 2005	2005	2006	1Q06	2Q06	3Q06	4Q06	1Q06	2Q06	3Q06	4Q06
				y/y % change				s/adj annualised %q/q			
Real GDP	100	6.6	7.9	10.1	8.0	7.0	6.6	9.1	5.4	3.9	7.9
Goods-producing Industries	31.1	8.0	10.2	15.1	10.3	8.9	7.2	3.4	1.5	11.9	11.1
Manufacturing	26.1	9.5	11.5	18.6	11.9	9.5	7.7	3.4	2.3	12.3	11.5
Construction	3.4	0.7	2.7	-0.7	0.9	5.8	4.7	2.0	-6.9	12.5	12.2
Services-producing industries	63.1	6.4	7.0	8.2	6.9	6.3	6.6	9.6	8.6	0.8	7.9
Wholesale/retail trade	10.8	9.6	10.3	14.8	9.5	10.4	6.9	26.2	0.8	8.2	-3.5
Hotels/restaurants	1.8	4.3	5.1	6.2	3.8	4.4	6.1	8.0	5.7	1.5	9.7
Transport & Comms	11.8	4.2	4.3	5.3	4.0	4.0	4.0	3.9	2.9	2.9	6.1
Financial services	10.7	7.6	9.2	8.7	9.6	7.4	11.1	13.6	25.1	-16.2	28.2
Business services	12.6	5.9	5.8	6.1	6.6	5.1	5.4	0.1	9.9	4.0	7.9

Source: MTI, DOS