

## Highlights

Since the last *Macroeconomic Review* in October, the global economic downturn has significantly worsened, presenting Singapore with its most challenging external environment in recent history. Almost 60% of our exports are destined for economies that are expected to be in outright recession in 2009. Against this backdrop, the Singapore economy experienced a sharp contraction in economic activity in Q4 2008 and Q1 this year.

More recently, however, global economic indicators have sent mixed signals. Some appear to be stabilising, while others are still worsening, albeit at a slower rate. In this respect, the unprecedented policy actions by governments around the world have played an important role in averting a worst-case scenario thus far. Barring further significant external shocks, the most intense phase of this downturn for Singapore may have already occurred. Nonetheless, the domestic economy is not expected to stage a decisive rebound this year. Indeed, the path to recovery is uncertain and hinges on external developments, including the recent outbreak of swine influenza in Mexico, which has added a new dimension to the risk outlook. With the current world economic downturn likely to be a prolonged one, Singapore's climb out of recession will be slow and gradual. Accordingly, the domestic economy is forecast to contract by 6% to 9% in 2009. Meanwhile, CPI inflation is expected to average between -1% and 0%.

The steep contraction in GDP this year has to be viewed in the context of the external orientation of the Singapore economy. Indeed, the share of external demand in total demand has increased markedly over the last decade, making the economy even more susceptible to global headwinds. However, the extreme openness of the Singapore economy should enable it to pick up more strongly than other countries when the global recovery eventually gets underway. Moreover, Singapore's longer term prospects are being strengthened by the ongoing build-up of capacity in key segments of the domestic manufacturing and services sectors, as well as policy measures which are presently being implemented to enhance workers' adaptability to changing industry needs.

A detailed review of recent developments in the external environment and the Singapore economy can be found in Chapters 1 and 2. Chapter 2 includes an overview of trends in employment and redundancies, explains why the current adjustment in the labour market has been slower compared to past recessions, and highlights the higher proportion of professionals, managers, executives and technicians (PMETs) who have been retrenched. We also review the current price developments in the domestic economy and point to the factors that have contributed to the recent dissipation of price pressures.

Chapter 3 elaborates further on the bleak labour market conditions worldwide and the drawn-out process of rebuilding balance sheets that could forestall a quick rebound in external demand. Empirical studies have found that global downturns associated with financial crises tend to be unusually severe and prolonged. From Singapore's perspective, two sets of considerations underpin the domestic outlook, namely the depth of the downturn and the likely profile of the economy as it recovers from the trough. As far as the employment outlook is concerned, the labour market is likely to weaken further, although prospects vary across industries.

In this issue of the *Review*, we analyse in detail several defining characteristics of the current downturn, such as the sudden and synchronised collapse in exports across East Asia. Box A in Chapter 1 looks at the rise of Asian cross-border production networks and how this could have amplified the impact of the fall in end demand by advanced economies. Box B compares the characteristics of the current economic downturn in Singapore, namely its depth, duration, speed and breadth, with past recessions.

Finally, Box C in Chapter 3 offers a conceptual exposition of how the government's Jobs Credit Scheme will help to cushion the fall in demand for local workers in Singapore, at least in the short term.

To round off the *Review*, we include two Special Features. Special Feature A provides a detailed and timely empirical analysis of the characteristics of business cycles in Singapore to ascertain how quickly external demand shocks diffuse through the Singapore economy and which sectors are more likely to be severely hit. It also identifies co-movements in output and employment between sectors, establishing, for example, that in a small and open economy such as Singapore, even sectors that primarily serve the domestic population are not immune to external economic shocks.

Special Feature B, contributed by Professor Barry Eichengreen of the University of California, Berkeley, draws on the historical evolution of reserve currencies to assess the factors which might impinge on the future of the US dollar in international finance.

The next issue of the *Review* will be released in October 2009.

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