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Effects of Brexit on Singapore

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ABSTRACT

Britain voted to leave the European Union (EU) at The United Kingdom European Union Membership referendum on 23 June 2016. This move stunned the global financial market with the concern that it may hurt the global economy. Some equity markets fell by as much as 7% in value (the Dow Jones industrial average fell by 600 points or 3.5%), erasing nearly $3 trillion in equity value.

The Brexit vote has slowed down the UK economy and has become the worst performing in the G7, has been the best performing prior to the referendum. An extra £25 billion was added to the Autumn Budget to support the economy. The office for Budget Responsibility estimates the economy growing by just 1.5 per cent down from the previous estimate of 2 per cent. Business investment was also affected by Brexit, with The Bank of England expecting the level of business investment to be around 25 per cent lower by 2019 relative to pre-referendum estimates.

The Brexit referendum has created a havoc in various sectors of the industry spanning across the globe. This paper is aimed at assessing the implications of Brexit on Singapore's real economy – in terms of trade, investment flows, and tourism.

Keywords: *Brexit, Referendum, Equity Market, G7.*

1. INTRODUCTION

Singapore is one of the largest trading partners of the United Kingdom in Asia and one of the few countries the UK has a trade surplus with. Singapore accounts for half of the UK exports to the Association of Southeast Asian Nations, worth £5.6 billion. The United Kingdom is also one of the countries that invest heavily into Singapore, with total foreign direct investment into Singapore exceeding £30 billion.

The exit of one the major country like Britain from the European Union is unprecedented and there's one thing that foreign exchange markets really don't like, its unstable political systems.

Following the Brexit vote, the British pound has declined sharply in value against other major currencies like US Dollar and Yen. The drastic drop in the value of the Pound Sterling is only further going to drive how this instability is damaging the British currency.

Little is yet known about what form the exit negotiations will take and whether Britain will retain access to Single Market (Soft Brexit) or will have to leave the EU completely and renegotiate new trade agreements with the EU and other countries (Hard Brexit). Although, there have been hints at "Hard Brexit" with the hope that it will help the poor people of Britain. No matter the form of exit, this will no doubt result in increasing the cost of trade and investment between the countries.

We can already see how Brexit has rattled international markets and significant threats to the global markets in the future. Nevertheless, it presents an opportunity for Britain to establish new trade relations renegotiate trade agreements.

2. IMPACT ON FINANCIAL MARKET

The equity market in Singapore has responded negatively to the Brexit referendum as the Straits Times Index (STI) was down by 2.1% on the day of the referendum. The SGD is its strongest in history against the pound at 1.81 per GBP.

The depreciation of the Pound Sterling will surely affect the Singapore exporters that have strong relations to the UK markets or with earnings denominated in GBP.

London has established itself as the financial capital of Europe with much larger market capitalization than most of the European cities such as Paris and Frankfurt, but things could soon change.

Other European cities with harmonized financial standards are likely to gain power as Europe's financial capitals. This would likely affect the Singapore financial market because of the strength of the Singdollar against the GBP.

If exports are less, companies that are dependent on foreign exchange services and banks may not be in need of such services, which could, in turn, affect banks' fees and revenues.

Chart 1: Brexit Impact on the Equity Market

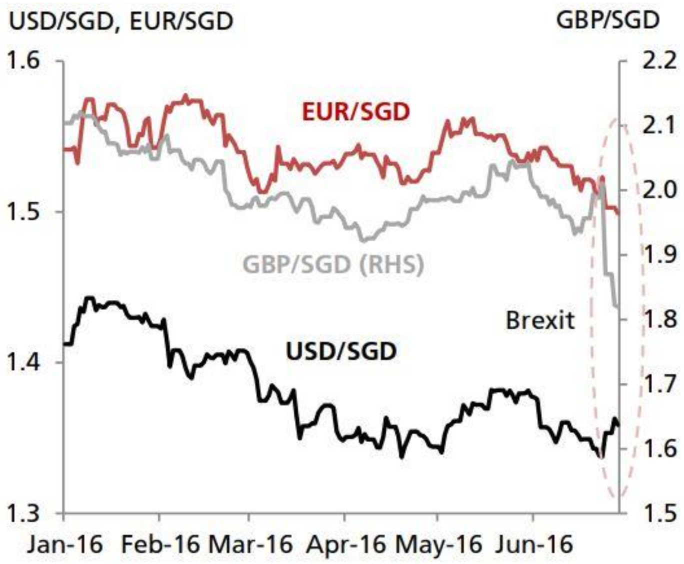

Chart 2: Brexit Impact on other Currencies

3. IMPACT ON INVESTMENT FLOWS

Foreign Direct Investment (FDI) is the investment made by a company or an individual in his personal capacity in one country in business interests in another company, in the form of either establishing business operations or acquiring business assets in the other country, such as ownership or controlling interest in a foreign company.

Many countries promote and welcome FDI as it generally increases productivity, which increases output, which in turn, increase wages. Productivity is one of the direct benefits of FDI, whereas new technological knowhow is one of the indirect benefits. Singapore is one of the major recipients of FDI.

Singapore is one of the UK's largest trading partners in the Asia Pacific Region. Both the countries signed an Agreement on Promotion and Protection of Investment on 22nd of July, 1975 which governs their commercial relationship. Prior to Brexit, any investment in (into) Britain had the advantage of an unlimited opportunity for growth and expansion within the European Market (EU Single Market).

The Brexit vote caused major disruptions in the investment flows vis-à-vis the financial markets majorly through fluctuations and changes in the exchange rates which affected the value of the Pound Sterling and the overall Business Environment. There will also be a reduced access to the EU market, which could further dampen the business environment.

Many Singapore Companies with investment in the UK are apprehensive of the future because of the devaluation the Pound Sterling. This has a direct impact on the profitability of the company. Victor Mills, the Chief Executive of the Singapore International Chamber of Commerce described the current situation as “uncharted waters”. He expects the volatility to continue until UK’s exit terms are known.

Around 25% of the entire FDI portfolio in Singapore comes in from the European Union. Most of the investments from and inside of the European Union (EU) were coming from the UK. Brexit would directly lead to not only a lesser amount of investment into Singapore from the UK but also from the European Union (EU) as well. This subsequently led to higher costs and lower profits for the British firms to expand their businesses in Singapore and vice versa.

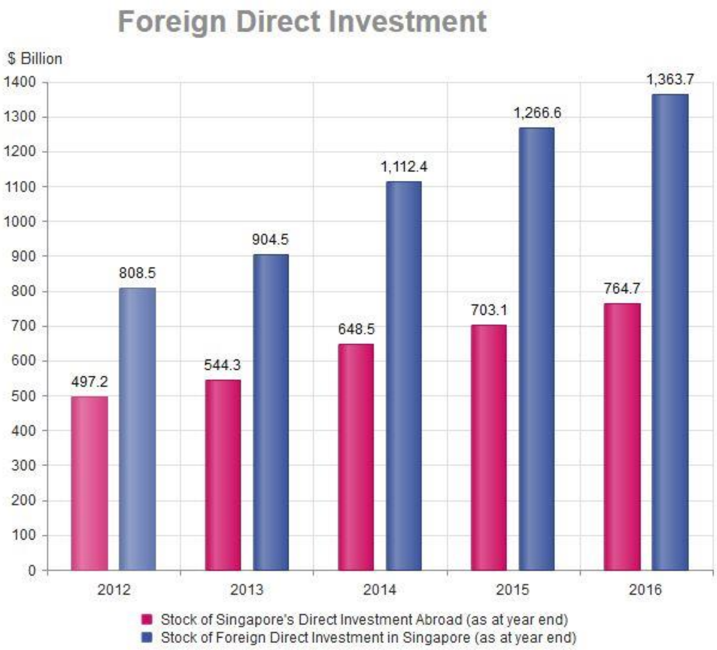

Chart 3: Foreign Direct Investment

4. IMPACT ON TOURISM

Tourism is one of the major sources of revenue for the Singapore economy. It is one of the sectors which is growing at a constant pace over a number of years. The Great Britain Pound has been falling continuously against the Singapore Dollar since 2015. Post-Brexit, the Pound Sterling continued to weaken against the Singapore Dollar making the already strong demand for travel to the UK even stronger.

Travel booking companies like Wego.com and TripZilla.com said that they would see more amounts of tourists going to the UK after Brexit and lesser amounts of inbound tourists into Singapore. Ms. Winnie Tan, CEO, TripZilla.com, said that she expects a lesser amount of inbound tourists from the UK due to the weakness in the pound and the uncertainty around Brexit’s economic impact as the UK made almost 30 percent of the total tourists from the European Union.

Ms. Jane Chang, head of marketing communications at Chan Brothers Travel, a travel booking company based in Singapore said that its company has experienced a 30 per cent increase in demand for travel to the United Kingdom.

Thus, a strong Singapore Dollar would make travelling to the UK cheaper and much more enjoyable whereas a weak Pound Sterling would lead to fewer amounts of inbound tourists into Singapore.

5. CONSLUSION

There are many potential reasons for the outcome of the Brexit referendum. Until the exact conditionality and specifics are not known, we can only analyze on the short to medium term basis. The impact caused by the referendum is much deeper and widespread than generally perceived. Countries that are strongly dependent on the UK for their businesses would have to adopt separate policies, one for the European Union in general and one specifically pertaining to the UK.

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