Inflation Monthly DEC 2004

HIGHLIGHTS & OUTLOOK

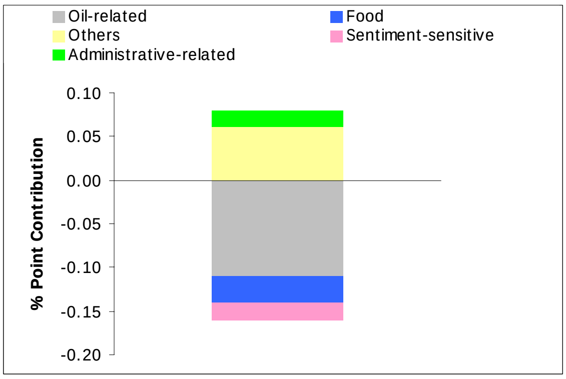
CONSUMER PRICES: EASING OF THE "OIL BURDEN"

CPI (% Growth)	2004		
	Oct	Nov	Dec
y-o-y	1.9	1.7	1.5
m-o-m SA	0.0	-0.1	-0.1

Headline CPI inflation eased further to 1.5% y-o-y in December, from 1.7% in November. The MAS underlying inflation – which excludes private road transport and accommodation costs – also came in lower at 1.8% in December, as compared to 2.0% a month ago. For 2004 as a whole, CPI inflation averaged 1.7%.

On a sequential basis, overall CPI edged down further by 0.1% in December, after falling at the same rate in November. The slip in consumer prices in December was largely on account of lower prices of petrol and some retail items. Cheaper food items also contributed to the lower prices. (Chart 1)

Chart 1
% Point Contribution to CPI Changes (m-o-m SA) in December

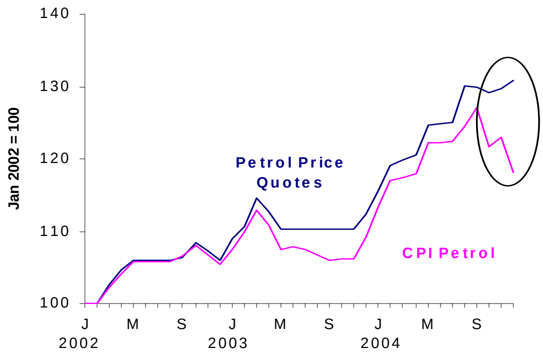


A DOUBLE "RELIEF" FOR PETROL PRICES

After rising for the most part of 2004, petrol prices enjoyed a double relief in December, with a price reduction as well as increased discounts island-wide of at least 10%. In particular, prices were cut by three cents in the month, partially reversing the earlier four-cent hike in late November, and reflected the easing of global oil prices. The West Texas Intermediate (WTI) oil price subsided to around US$40 per barrel in early December – the first significant decline in prices since the heady highs of more than US$55 in late October. This partly reflected easing concerns about winter demand, as well as the unwinding of earlier speculative positions. With global oil prices cooling off, international finished product prices retreated as well, which in turn prompted domestic pump operators to lower prices.

While the price cut was on account of easing external cost pressures, the *price discount* was sparked off by domestic competition. In a bid to retain market share, rising competition within the industry has led to price wars, which have become more intense and frequent than before. This could perhaps explain the seemingly contradictory pricing decisions of pump operators, with discounts offered within weeks of a price hike in some instances. Chart 2 attempts to distinguish the effects of *price cuts* versus *price discounts* by plotting an index of pump prices quoted by the major petrol companies[1] with the petrol index in the CPI basket. While movements in the former only reflect changes in the quoted prices, the latter encompasses the effects of both price changes and discounts.[2] As can be seen in the chart, the two series generally moved in tandem prior to 2003. Since then, the frequent petrol price wars have led to some divergence, which seemed to have widened further in recent months, as competition within the industry intensified.

Chart 2
Petrol Price Quotes and Petrol Index



* Note: Although there was a price cut in December, prices still averaged higher for the month due to an earlier price hike.

PRICES OF HOUSEHOLD SERVICES ROSE AHEAD OF NEW REGULATIONS FOR MAIDS

Prices of household services, which comprise largely foreign maid salaries and levies, have been on a general uptrend, following the government's announcement in September that it would tighten entry requirements for new maids to raise the quality of services. Apart from lifting the minimum age of maids from 18 to 23, new maids need to show proof of at least eight years of formal education. The change in policy has led to concerns that the potential supply of new maids would shrink, as fewer maids would be able to qualify under these new employment requirements. While these stricter regulations only come into effect from 1 January 2005, prices of household services in the CPI have already risen by 1.3% over the last three months of the year.

GOODS & SERVICES INFLATION: IMPLICATIONS FOR 2005

Going forward, the increase in goods inflation is likely to be more moderate, with commodity-related price pressures tapering off, while the uptrend in services inflation is expected to continue. The headline CPI inflation is projected to come in at 1-2% for 2005 as a whole.

POSSIBLE WIDENING OF THE SERVICES-GOODS INFLATION GAP IN 2005…

In the course of the year, we expect further pent-up cost increases to filter through, as the improvement in the economy encourages further pass-through of costs that had built up over the years, but not passed on to consumers due to the weak economic conditions. This is likely to push up services cost inflation, leading to a widening of the differential between the inflation rates of services and goods.

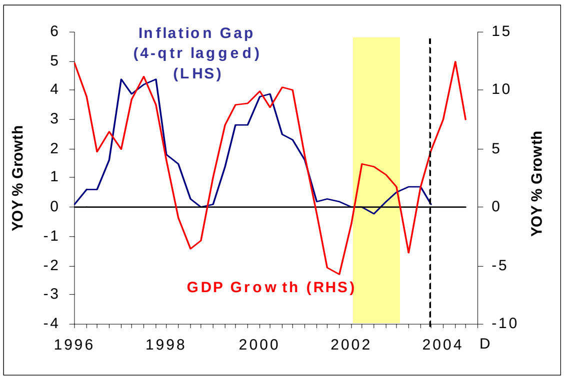
We try to gain further insights into the dynamics of the movements in services versus goods prices by deriving an inflation differential measure. For this analysis, the prices of various items that are either commodity-related (e.g., food and oil-related products)

1 This index is constructed based on selected petrol grades weighted by their respective shares in the CPI basket.

2 In the calculation of the CPI, price discounts are taken into account only if they are generally available, such as, island-wide discounts. As such, discounts at selected locations, for example at the hotly contested Bukit Timah area, are not captured by CPI.

or policy-induced influences (e.g., alcoholic drinks & tobacco) are excluded, as these are exogenous in nature, and could distort the headline figure. As can be seen in Chart 3, the inflation gap (between services and goods) was closely correlated with the business cycle, albeit with a lag of around four quarters. The relationship, however, seemed to have weakened somewhat in this recent period, but this reflected a one-off impact from the Sars outbreak (as highlighted in the yellow region), when the plunge in prices of travel-related services dragged down services inflation relative to that of goods. Hence, in the absence of such one-off price shocks, the strong turnaround in the domestic economy in 2004 (with GDP growth observed to be a leading indicator) suggests that the inflation gap could widen in 2005, with services prices rising at a faster pace as compared to those of goods. In addition to the filtering through of past cost increases, the higher income elasticity of services will also support a faster increase in services prices relative to that of goods.

Chart 3
Services-Goods Inflation Gap and GDP Growth



...SIGNALLING A REVIVAL IN SERVICES INFLATION

In particular, we identify several consumer-related services that are expected to record higher prices this year. First, education costs could be adjusted upwards, with several local education institutions announcing fee hikes this year. To cope with the rising costs over the years, monthly school miscellaneous fees would be hiked by around $0.50-$2.00 from January 2005. Likewise, tertiary tuition fees at polytechnics and universities including NUS, NTU and SMU will be revised upwards by 5-15% from July 2005. In fact, tuition fees for tertiary education are likely to see further increases in the years ahead, with tertiary institutions such as SMU given greater autonomy to set their fees.

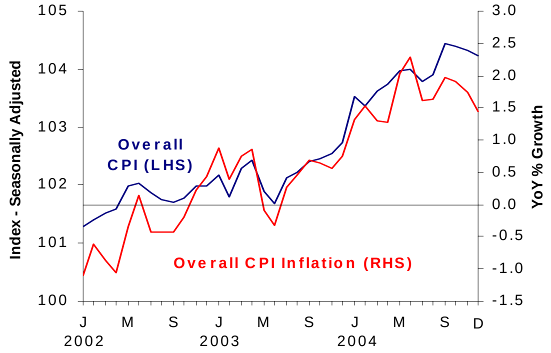
Second, public road transport costs could be adjusted upwards, with rising labour and fuel costs. Although the Public Transport Council has yet to seek an increase in fares, record-high oil prices in 2004 could induce operators to do so as they have been bearing the brunt of higher fuel costs. Thus, it is likely that some second-round effects of high oil prices would be passed on to consumers eventually.

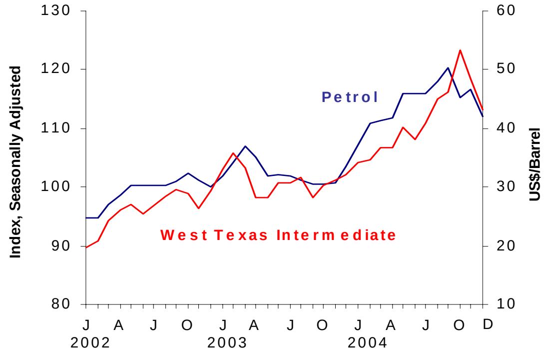
Third, prices of household services could rise further, as the full brunt of the new foreign maid requirements come into effect on 1 January 2005. Anecdotal evidence from maid agencies suggests that a shortage of suitable maids have already emerged in January this year. Apart from the shrinking supply, the more stringent requirements on age and education could also mean these maids would command higher salaries. Nonetheless, the full impact of this policy change is yet to be determined, as maid agencies recently appealed to MOM to allow maids to be brought in from new source countries such as Cambodia and Vietnam.[3] If this were to be approved, it would alleviate the shortage of maids and lift some of the upward pressure on household service prices.

[3] Currently, Singapore employs about 150,000 maids from Indonesia, the Philippines, India and Sri Lanka.

Headline CPI inflation moderated to 1.5% y-o-y in December, from 1.7% in November. The seasonally adjusted CPI also edged down by 0.1%.

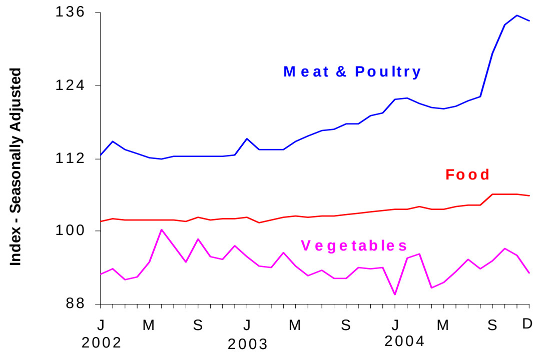
The fall in the overall CPI was attributed to cheaper petrol during the month. The easing of global oil prices and domestic competition contributed to lower petrol prices.

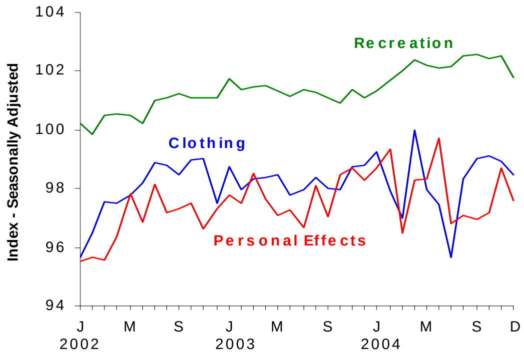




Food prices edged down with cheaper vegetables. Meat & poultry prices also retreated slightly for the first time since the poultry ban was lifted.

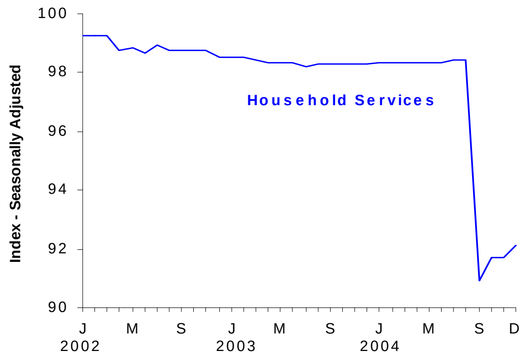
Prices of some sentiment-sensitive retail items such as clothing, personal effects and recreation weakened as well.

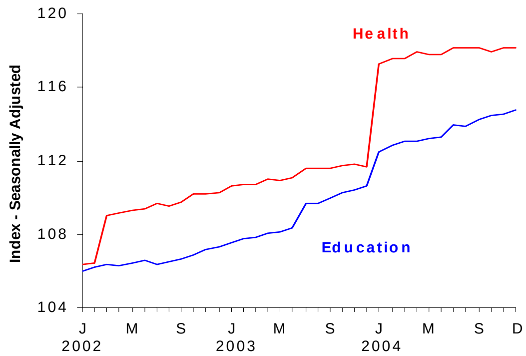




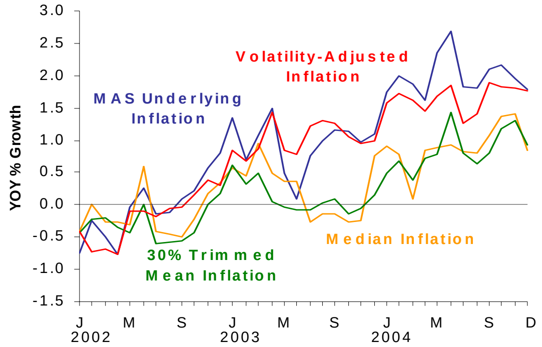
Prices of household services trended up, possibly reflecting more stringent regulations for foreign maids that commence in January 2005.

Healthcare costs were stable while education costs inched up.





Except for volatility-adjusted inflation which remained unchanged, all other core inflation measures came in significantly lower in December. In particular, the MAS underlying inflation came in at 1.8%.



Note: CPI SA series are used only when seasonality is detected. Otherwise, non-SA series are used.

ECONOMIC POLICY DEPARTMENT

CONSUMER PRICE INDEX

Period	All Items	Food	Clothing	Housing	Tpt & Comm	Education	Health	Misc
Weights	10000	2752	443	2292	1803	729	305	1676
	Index – Seasonally Adjusted							
2002 Jan	101.3	101.6	95.7	99.9	97.9	106.0	106.4	104.9
Feb	101.4	102.1	96.5	99.5	98.1	106.2	106.5	105.1
Mar	101.5	101.9	97.5	99.5	98.3	106.4	109.1	105.0
Apr	101.6	101.8	97.5	99.3	98.6	106.3	109.1	104.7
May	102.0	101.9	97.8	99.6	99.0	106.4	109.1	106.0
Jun	102.0	101.9	98.2	99.7	98.7	106.6	109.3	107.4
Jul	101.9	101.8	98.9	99.8	98.8	106.3	109.5	105.3
Aug	101.8	101.7	98.8	99.6	98.7	106.5	109.5	105.4
Sep	101.7	102.2	98.5	99.5	97.9	106.7	109.8	105.2
Oct	101.8	101.9	99.0	99.6	98.2	106.8	110.2	105.4
Nov	102.0	102.0	99.0	99.9	98.5	107.1	110.4	105.7
Dec	102.0	102.1	97.5	99.8	98.4	107.3	110.6	106.0
2003 Jan	102.2	102.3	98.7	99.4	99.1	107.6	110.7	106.4
Feb	101.8	101.4	97.9	99.1	99.2	107.7	110.8	106.2
Mar	102.3	101.9	98.3	99.1	99.6	107.8	110.8	107.4
Apr	102.4	102.4	98.4	100.4	98.7	108.0	110.8	105.9
May	101.9	102.4	98.5	99.4	98.0	108.1	110.8	104.6
Jun	101.7	102.3	97.8	99.5	98.2	108.3	111.0	104.6
Jul	102.1	102.5	98.0	99.4	98.1	109.7	111.4	105.6
Aug	102.2	102.6	98.4	99.3	98.1	109.7	111.5	106.2
Sep	102.4	102.8	98.0	99.2	98.0	110.0	111.7	107.1
Oct	102.4	103.0	98.0	98.6	98.2	110.2	111.7	107.5
Nov	102.6	103.1	98.7	98.4	98.5	110.4	112.0	107.7
Dec	102.7	103.4	98.8	98.3	98.9	110.6	112.0	108.0
2004 Jan	103.5	103.6	99.3	99.0	99.5	112.5	117.3	108.6
Feb	103.4	103.6	97.9	98.8	99.8	112.9	117.7	108.3
Mar	103.6	104.0	97.0	98.7	99.4	113.1	117.6	109.5
Apr	103.8	103.7	100.0	98.9	99.2	113.0	117.7	109.0
May	104.0	103.6	97.9	99.2	99.9	113.2	117.6	110.0
Jun	104.0	104.0	97.4	99.3	99.9	113.3	117.7	110.4
Jul	103.8	104.3	95.6	99.1	99.6	114.0	118.0	108.9
Aug	103.9	104.4	98.3	98.9	99.8	113.9	118.2	108.9
Sep	104.4	106.2	99.0	99.0	100.1	114.2	118.2	108.3
Oct	104.4	106.0	99.1	99.3	99.5	114.5	117.9	108.8
Nov	104.3	106.0	98.9	99.3	99.9	114.6	118.3	107.8
Dec	104.2	105.9	98.5	99.3	99.5	114.8	118.6	108.0

Source: Department of Statistics

ANNEX 2

SELECTED INFLATION INDICATORS

Period	CPI	Import Price Index	Non-fuel Primary Commodities	Opec Oil Price
	YOY% Growth			
2002 Jan	-1.1	-2.8	-8.7	-24.4
Feb	-0.6	-2.8	-7.6	-25.6
Mar	-0.9	-2.3	-4.6	-4.4
Apr	-1.1	-2.7	-5.2	0.5
May	-0.3	-3.2	-6.3	-5.8
Jun	0.1	-3.7	-2.7	-8.9
Jul	-0.4	-3.2	0.2	6.0
Aug	-0.4	-2.0	1.4	5.7
Sep	-0.4	-1.3	7.9	13.8
Oct	-0.2	-0.5	13.5	40.2
Nov	0.2	-1.1	11.3	37.2
Dec	0.4	0.0	11.4	59.6
2003 Jan	0.9	1.0	11.8	65.5
Feb	0.4	2.5	11.5	66.7
Mar	0.8	2.1	7.3	30.4
Apr	0.9	0.0	7.2	1.9
May	-0.1	-1.2	6.9	3.6
Jun	-0.3	-0.3	3.9	12.7
Jul	0.3	0.1	1.4	9.3
Aug	0.5	0.6	4.0	10.7
Sep	0.7	-0.9	3.1	-4.7
Oct	0.6	-1.0	6.8	3.8
Nov	0.6	0.4	9.6	17.4
Dec	0.7	0.2	12.2	4.8
2004 Jan	1.3	0.3	15.8	-0.3
Feb	1.5	-2.0	19.2	-6.4
Mar	1.3	-1.9	23.7	9.3
Apr	1.3	-0.3	24.7	27.8
May	2.0	2.6	21.8	41.9
Jun	2.3	2.9	22.2	28.9
Jul	1.6	3.0	22.9	32.0
Aug	1.6	3.6	19.7	40.9
Sep	2.0	3.5	17.7	53.5
Oct	1.9	4.3	12.1	59.0
Nov	1.7	2.8	10.3	35.5
Dec	1.5	1.6	8.5	21.2

Source: Department of Statistics, IMF and Bloomberg