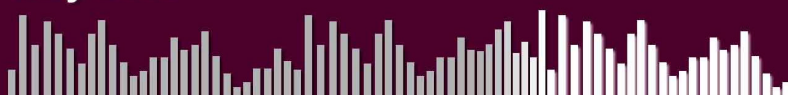


# Inflation Monthly

## July 2005



## CPI Inflation on the Uptick

CPI (2004 = 100)		
% Growth/ Level	Jun 05	Jul 05
y-o-y	-0.2	0.1
m-o-m	-0.9	1.1
Index	99.3	100.4

- **Headline CPI inflation registered 0.1% in July**

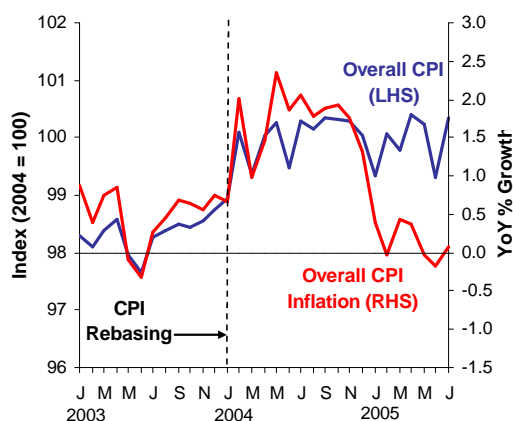
The MAS underlying inflation measure came in at 1.1%, up from 0.8% in the previous month.

- **On a m-o-m basis, CPI went up 1.1% largely due to higher housing costs**

Housing costs rose in July, reflecting the absence of S&C rebates and the 13.7% hike in electricity tariffs for Q3. Public transport costs also came in higher as operators hiked bus and MRT fares. Education costs at various local universities were raised – the first increase in four years.

- **Lower retail prices and private road transport costs weighed down on the CPI**

Prices of retail items fell on a y-o-y basis as the traditional GSS “tailing-off” effect was more muted this year. Private road transport costs edged down, due to lower petrol and car prices.



## Recent Developments

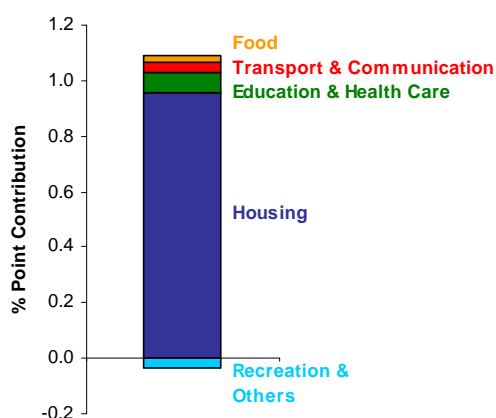
### Headline CPI Inflation Rebounded in July

Headline CPI inflation rose 0.1% year-on-year (y-o-y) in July, after coming in at -0.2% in June. This brought average inflation for the first seven months of the year to 0.1%. The MAS underlying inflation measure – which excludes private road transport and accommodation costs – came in at 1.1% y-o-y, up from 0.8% in the previous month. It averaged 1.0% over the period Jan-Jul 2005.

### CPI Uplift Largely Supported by Higher Housing Costs

On a month-on-month (m-o-m) basis, the CPI increased 1.1% in July – the largest m-o-m increase thus far this year – largely due to higher housing costs, as well as hikes in university tuition fees (subsumed under education & health care) and public transport fares (transport & communication). (Chart 1)

**Chart 1**  
**% Point Contribution to CPI Change (m-o-m), July 2005**



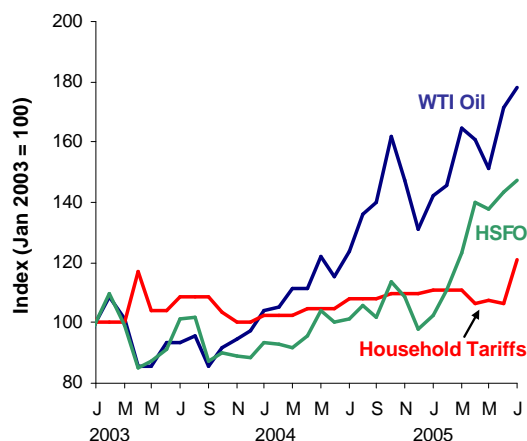
### ABSENCE OF SERVICE & CONSERVANCY REBATES AND HIKE IN ELECTRICITY TARIFF LED TO A RISE IN HOUSING COSTS

As expected, accommodation costs came in higher in July, contributing 1.0% point to the overall rise in the CPI. The increase was mainly due to the absence of service & conservancy (S&C) rebates during the month.<sup>1</sup> In addition, electricity tariffs saw a significant upward adjustment of 13.7% for the period Jul-Sep, reflecting a higher HSFO forward price<sup>2</sup> of US\$39.32 per barrel (compared to US\$30.09 in the preceding quarter), as global oil prices continued their ascent. (Chart 2)

<sup>1</sup> For 2005, S&C rebates are given out in the months of January, March, June, September and December.

<sup>2</sup> Electricity tariffs are revised on a quarterly basis to reflect the forward price of 180-centistoke high sulphur fuel oil (180-CST HSFO) for the quarter.

**Chart 2**  
**WTI Oil, HSFO and Household Electricity Tariffs**



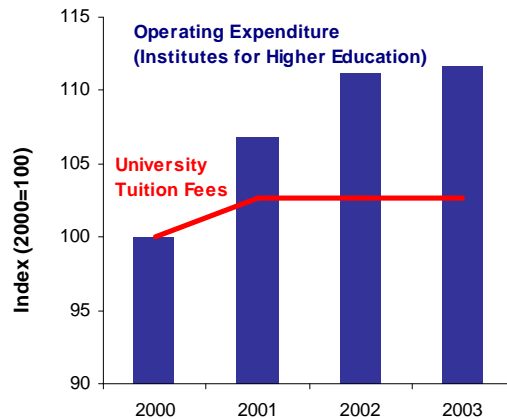
### REVISION IN TERTIARY TUITION FEES BOOSTED EDUCATION COSTS

Apart from the rise in housing costs, the upward revision in university tuition fees – the first hike in four years – also contributed to the CPI increase during the month. As part of the government’s plan to grant greater autonomy to the local universities in setting their fee structures as well as to cope with rising operational expenditures, the freeze on tuition fees has been recently lifted. The National University of Singapore (NUS) and Nanyang Technological University (NTU), for instance, have both raised the fees of non-medical courses by 5% (S\$300), while the Singapore Management University (SMU) has increased its fees by 15% (staggered over three years for existing students). The steeper hikes at SMU reflected the expectation of higher wages and operating costs in the years ahead, as it targets to double its faculty size from the current 155 to 350 by 2012 to cater to a proportionate rise in student population. At the same time, fees at the five polytechnics have also gone up by 8% (S\$100) for the first time in four years.

Indeed, data from the report on *Education Services*, published by the Department of Statistics, shows that the overall operating expenditure of institutes for higher education has risen by around 12% over the period 2000–2003.<sup>3</sup> (Chart 3) In comparison, education fees at these institutions had gone up by only about 3% over the same period (using tuition fees paid by a typical non-medical student as reference). The three-year “fees freeze” has left the government and the educational institutions bearing the brunt of rising costs.

<sup>3</sup> The latest survey was carried out in year 2004 for reference year 2003.

**Chart 3**  
**University Fees and Operating Expenditure of Institutes for Higher Education**



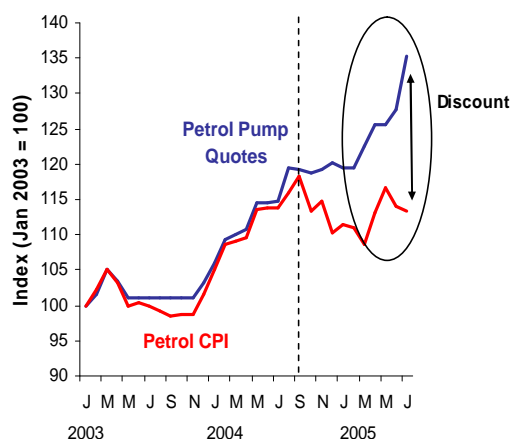
### HIGHER PUBLIC TRANSPORT COSTS PARTIALLY OFFSET BY DECLINE IN PRIVATE ROAD TRANSPORT COSTS

Public transport operators SBS Transit and SMRT Corporation, having kept fares unchanged since 2002, were granted the maximum allowed fare hike of 2.4%<sup>4</sup> by the Public Transport Council (PTC) in July. One reason cited for the fare increase was the escalating operating costs that stemmed largely from the rapid rise in diesel prices and wages. SBS Transit revealed that total operating cost for bus and rail operations increased 7% over the period 2002-2004. In particular, fuel cost for buses alone rose by some 41%, from \$39 million to \$55 million during the same period. Similarly, SMRT's group expenditure on diesel and electricity also went up by more than 40% from 2002 levels. Moreover, operators have been absorbing the 2% rise in Goods and Services Tax (GST) since 2002, as well as other operating costs arising from quality improvements such as upgrading of existing fleet of vehicles and expansion of transport network.

On the flip side, private road transport costs continued to trend downwards as COE premiums dipped to a 12-year low, largely due to the weakness in replacement demand for cars (as discussed in the May and June 2005 issues of the *Inflation Monthly*). Despite petrol companies raising pump quotes by six cents in mid-July, petrol prices were on average lower, reflecting discounts of up to 25% offered during the first half of the month. (Chart 4)

<sup>4</sup> Maximum permissible fare adjustment is calculated using the formula:  $0.5CPI + 0.5WI - 0.3$ . CPI and WI refer to the change in Consumer Price Index and Average Monthly Earnings (Annual National Average) over the preceding year respectively. The 0.3% is the productivity extraction to be used for the next three years. In the current review by PTC, for example, the CPI and the WI was 1.7% and 3.6% respectively.

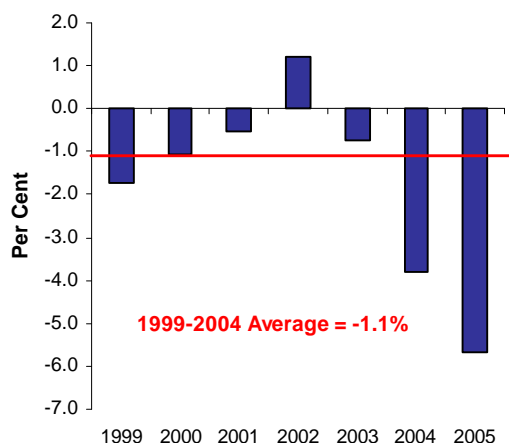
**Chart 4**  
**Petrol Pump Quotes and Petrol CPI**



**“TAILING-OFF EFFECT” OF THE GREAT SINGAPORE SALE FAILED TO MATERIALISE**

Unlike last year when prices of retail items such as clothing and footwear rebounded as the end of the Great Singapore Sale (GSS) approached in July, this “tailing-off” phenomena has been more muted this year.<sup>5</sup> (Chart 5) One possible explanation for this is that retailers could have cut prices further towards the end of the sale period this time round, encouraged by the positive response to the Sale. For instance, according to Visa and MasterCard, credit card spending was generally stronger than what they were in the same period a year ago. In addition, this year’s GSS could have received a boost from the International Olympic Committee (IOC) meeting in July.

**Chart 5**  
**“July GSS Effect”: % Change in Prices of Retail Sales Items over May-July**



<sup>5</sup> This year’s GSS ended on 24 July, having stretched over the same period as last year’s Sale.

## Outlook

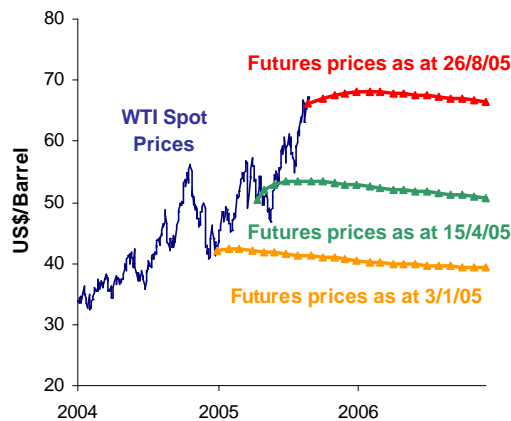
### Potential Inflation in the Pipeline

#### OIL PRICES REMAIN THE KEY RISK FACTOR

Going forward, there are several inflation risks in the external environment, chief among them the unrelenting rise in global oil prices. In particular, the emergence of numerous idiosyncratic risks in August lifted up oil prices further. These shocks include various geopolitical developments in the Middle East as well as the devastating impact on production and refinery facilities in the Gulf of Mexico caused by Hurricane Katrina. Hurricane Katrina has forced operators to shut down more than a tenth of US' refining capacity and a quarter of its oil output. The loss in refinery capacity was estimated to be up to 1.9 million barrels per day (mbd), which compares with the output of the oil refinery sector in Singapore of around 1.3mbd. The culmination of these shocks led to the price of WTI oil hitting a record high of above US\$70 per barrel at one point in August.

Although prices have recently retracted lower to around US\$65 per barrel, they are likely to stay high in the near term. (Chart 6) Market analysts have warned that the restoration of damaged refinery facilities in the Gulf of Mexico may take up to two months, and there remains the risk of more of such storms to come after Hurricane Katrina, especially during the months of September and October.<sup>6</sup> Hence, oil markets could remain jittery in the interim, with production and refinery facilities in the Gulf of Mexico left paralysed, and refinery utilisation rates globally already stretched.

**Chart 6**  
**WTI Spot and Futures Prices**



As global oil prices continue to soar, many countries that hitherto have been “shielded” from the full pass-through of high oil price may now be forced to face the harsh realities that persistently higher oil prices have on domestic costs. For example, regional countries such as Indonesia, Malaysia and Thailand that used to provide heavy fuel subsidies have been forced to rethink their policies due to escalating fiscal costs. The Indonesian authorities are currently working on plans for subsidies to be cut, while Thailand has decisively abolished diesel subsidies since July. Similarly, the Malaysian government has raised petrol and diesel prices four times since last October, in a bid to free up funds for national development. The latest to join the ranks is India, which has recently hiked petrol and diesel prices by 7% and

<sup>6</sup> According to the US Department of Energy, the months of August to October are likely to be the peak period for hurricane activity, and this may well be the most active hurricane season on record for the Atlantic.

6.3% respectively. Meanwhile, oil refineries in China are also lobbying for similar policies to be implemented. In time to come, the reduction in fuel subsidies in these countries could ultimately lead to second round effects and feed into dearer imports for Singapore.

### **CPI INFLATION IS EXPECTED TO REMAIN UNCHANGED AT 0-1% IN 2005**

Indeed, the impact of persistently high oil prices on the domestic economy is also slowly filtering through, and we can expect prices of items with heavy oil content registering a gradual pickup in the coming months. Petrol pump quotes were hiked twice by a total of 17 cents in August, while price wars have clearly dissipated in frequency and intensity. To cope with higher diesel costs, cab operators have adjusted taxi fares (effective 1 August 2005), with meters going up by 10 cents every 25 seconds of waiting time, instead of 30 seconds previously. City Gas has also increased gas tariffs by 2% (effective 1 September 2005), from 15.70 cents to 15.98 cents per unit. In addition, electricity tariffs could see further upward adjustment in Q4 as the price of HSFO rises further. Higher oil prices may also have indirect effects on inflation. For example, rising fuel costs are resulting in higher operating costs for airlines, forcing them to pass on these cost increases to consumers in the form of higher surcharges or airfares. Similarly, restaurant meals may become more expensive with higher utility bills.

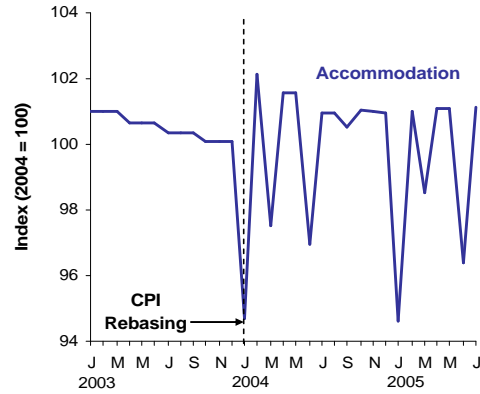
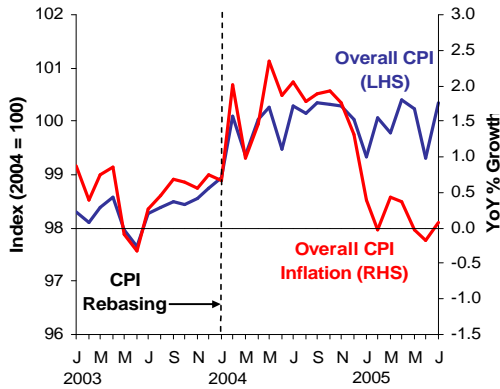
Prices of non-fuel commodities such as rubber and metals have also rallied strongly. In addition, as the domestic economy continues to expand, some wage-cost and demand-induced price pressures may be expected to emerge.

Taking all these into consideration, headline CPI inflation is expected to pick up in H2 2005 and come in at 0-1% for the year as a whole, before rising to 1-2% in 2006. The MAS underlying inflation measure is projected to be around 1% this year and 1-2% in 2006.

## Summary of Recent Domestic Price Developments

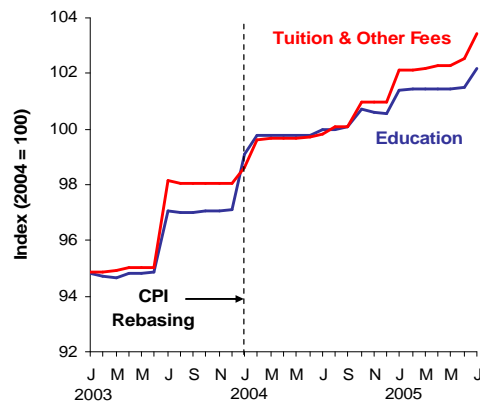
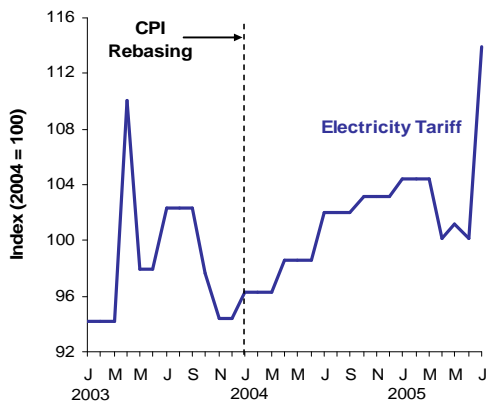
Headline CPI inflation rose to 0.1% y-o-y in July, from -0.2% in June. On a m-o-m basis, the CPI went up 1.1%.

Withdrawal of service and conservancy (S&C) charges rebates led to a rebound in accommodation costs.



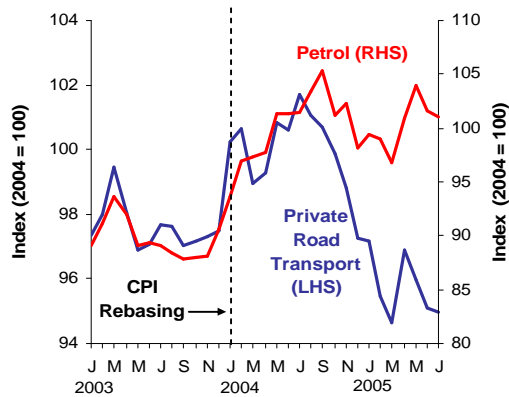
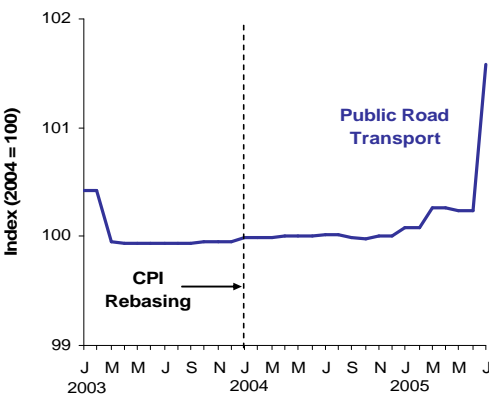
Electricity tariffs jumped 13.7% on the back of rising fuel cost.

Similarly, education costs climbed higher as universities and polytechnics revised fees for the new academic year.



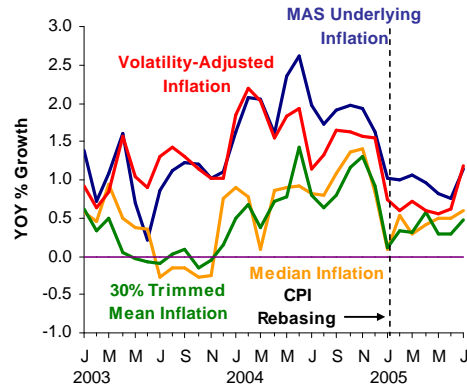
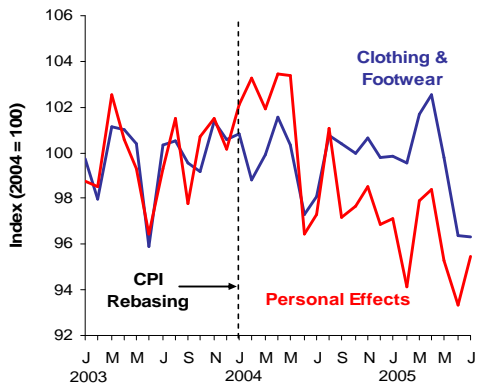
Bus and MRT fare hikes led to higher public road transport costs.

Private road transport costs edged down, due to lower petrol and car prices.



Prices of clothing & footwear came in flat compared with the previous month, while prices of personal effects increased.

All measures of core inflation came in higher. The MAS underlying inflation measure rose to 1.1% (y-o-y), from 0.8% in the previous month.



## Statistical Appendix

**Table A.1**  
**Consumer Price Index**

	All Items	Food	Clothing & Footwear	Housing	Tpt & Comm	Educ- tion & Stationery	Health Care	Recreation & Others
Weights	10000	2338	357	2126	2176	819	525	1659
	INDEX (2004 = 100)							
2004 Aug	100.1	99.8	100.7	100.8	100.6	100.0	100.2	99.3
Sep	100.4	101.1	100.4	100.4	100.4	100.1	100.1	99.4
Oct	100.3	100.8	100.0	100.8	99.9	100.7	100.0	99.6
Nov	100.3	100.8	100.7	100.8	99.3	100.6	100.1	100.0
Dec	100.0	100.7	99.8	100.8	98.4	100.6	100.1	99.9
2005 Jan	99.3	101.0	99.9	96.9	98.4	101.4	100.2	100.0
Feb	100.1	101.5	99.6	100.9	97.4	101.4	100.2	100.0
Mar	99.8	100.8	101.7	99.2	96.9	101.4	100.1	101.6
Apr	100.4	101.0	102.5	100.5	98.0	101.4	100.3	101.6
May	100.2	101.1	99.8	100.5	97.5	101.4	100.2	101.8
Jun	99.3	101.1	96.4	97.4	97.1	101.5	100.3	101.4
Jul	100.4	101.2	96.3	101.9	97.3	102.2	100.5	101.2

Source: Singapore Department of Statistics

**Table A.2**  
**Selected Inflation Indicators**

	CPI	Import Price Index	Non-fuel Primary Commodities	OPEC Oil Price
	YOY% GROWTH			
2004 Aug	1.8	3.6	19.7	40.9
Sep	1.9	3.5	16.7	53.5
Oct	1.9	4.3	12.5	59.0
Nov	1.8	2.8	10.6	35.5
Dec	1.3	1.6	8.9	21.2
2005 Jan	0.4	1.4	5.3	33.9
Feb	0.0	2.3	4.7	42.4
Mar	0.4	4.2	9.4	53.6
Apr	0.4	5.6	6.9	53.4
May	0.0	3.2	7.3	28.1
Jun	-0.2	5.1	8.3	49.8
Jul	0.1	5.9	7.8	46.2

Source: Singapore Department of Statistics, IMF and Bloomberg