

3 Labour Market and Inflation

- Labour market conditions continued to improve in Q4 2020. Overall employment contracted at a slower pace, while resident employment exceeded its pre-COVID level as most sectors expanded their local headcount in Q4. Foreign employment, however, saw persistent declines across most sectors, largely reflecting uncertainties in the outlook and difficulties faced by firms in replacing outgoing foreigners due to COVID-related travel restrictions globally.
 - In line with the gradual recovery in economic activity, labour demand is expected to continue to recover in 2021, with most of the job gains accruing to residents. The resident unemployment rate should therefore decline steadily throughout the year. However, some lingering slack could persist due to labour market mismatch and underemployment. Labour cost pressures should also be contained as productivity is projected to step up this year.
 - MAS Core and CPI-All Items inflation turned mildly positive in Q1 2021. Most of the increase in core inflation reflected the dissipation of the effects of government subsidies introduced in Q1 last year, as well as higher imputed costs of travel-related components. At the same time, price increases across most goods and other services in the core CPI basket stayed low. Headline inflation picked up more strongly, on account of higher private transport inflation as the recovery in global oil prices passed through to petrol prices. Firm demand for cars also drove up COE premiums.
 - Underlying inflation is anticipated to pick up gradually this year in tandem with the upturn in external inflation and stronger domestic demand. The step-up in y-o-y inflation in the coming months will, however, largely reflect base effects as prices fell in Q2 last year. The pace of increase in inflation should ease in the latter part of this year as these base effects fade and global commodity prices rise at a more modest pace. While domestic price pressures are expected to pick up and broaden, underlying inflation in the economy is unlikely to accelerate amid the lingering slack in the economy. Effective factor cost increases should remain low, while competitive pressures and the lack of tourism demand will continue to weigh on some retail and services components. For the year as a whole, inflation for most core CPI components is forecast to stay below 1.5%. MAS Core Inflation is expected to come in between 0–1% while the forecast range for CPI-All Items inflation has been revised up to 0.5–1.5%.
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3.1 Labour Market¹

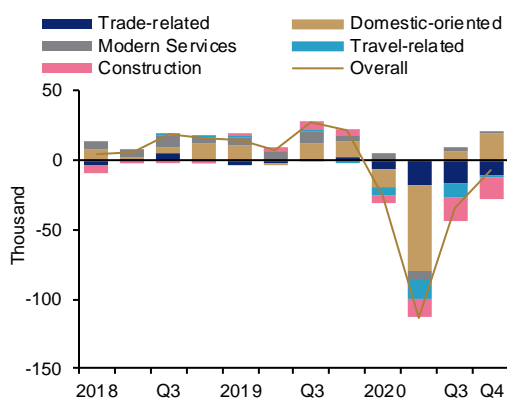
The domestic labour market is recovering

Alongside the pickup in overall economic activity, total employment declined by 7,800 q-o-q in Q4 2020, a significant moderation from the 34,400 contraction in the preceding quarter (**Chart 3.1**). The smaller decline in overall employment reflected robust growth in the domestic-oriented services sector as well as the moderation of job losses in the travel-related, trade-related and construction sectors.

The domestic-oriented² services sector registered strong employment growth in Q4. Job gains in the sector were much stronger than in Q3, underpinned by improvements in the consumer-facing segments—food & beverage (F&B) services, retail services and other community, social & personal services (CSP). While the step-up reflected some year-end seasonal uptick in hiring, further recovery in mobility and private consumption also contributed to the increase. Meanwhile, the construction sector saw a slower rate of employment decline in Q4 as more building activities resumed. With the exception of transport equipment, all trade-related segments recorded a slower pace of decline in employment or a turnaround to growth. At the same time, employment contraction eased in all segments of the beleaguered travel-related sector.

Chart 3.1 Total employment fell at a more moderate pace in Q4

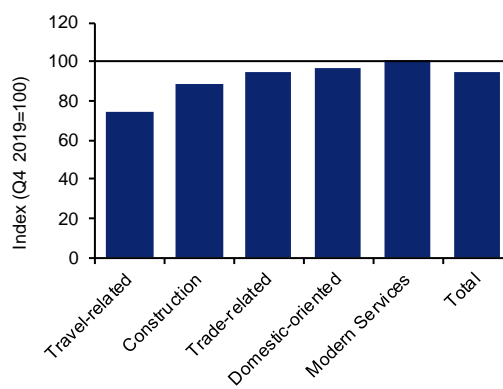
Q-o-q employment change by broad sectors



Source: MOM and EPG, MAS estimates

Chart 3.2 For full year 2020, employment contracted in all sectors, except modern services

Total employment in Q4 2020 by broad sectors and indexed to Q4 2019 levels



Source: MOM and EPG, MAS estimates

For 2020 as a whole, total employment fell by 181,000 or 4.8% from end-2019. Headcount was below pre-COVID levels for all broad subsectors, except for modern services, which registered a modest increase of 4,500 (+0.7%) in 2020 (**Chart 3.2**). The travel-related sector saw the sharpest decline in employment, by more than 25% from 2019. In terms of contributions to the fall in overall employment, the travel-related sector accounted for close

¹ The commentary in this section is mostly based on labour market data up to Q4 2020.

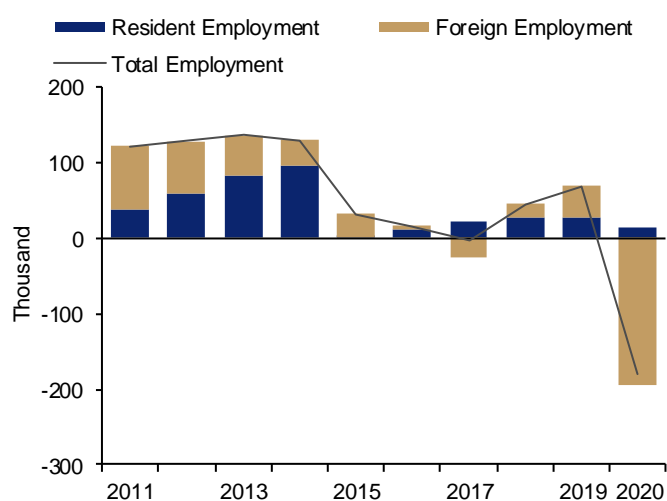
² The “domestic-oriented” sector encompasses land transport, retail trade, food & beverage, real estate, administrative & support services, community, social & personal services (excluding arts, entertainment & recreation) and utilities & others. The “modern services” sector comprises ICT, financial & insurance and professional services. The “trade-related” sector consists of manufacturing, wholesale trade, water transport and other transport industries. The “travel-related” sector is made up of air transport, accommodation, as well as arts, entertainment & recreation industries.

to a fifth of the drop, significantly higher than its employment share of 3%. Construction, domestic work and manufacturing contributed to another 60% of the decline in total employment last year.

The burden of the economy's total (net) employment contraction last year fell entirely on the foreign workforce (**Chart 3.3**). Foreign headcount contracted by 195,900 (-13.7%) in 2020, with most of the decline (77%) being borne by work permit holders. The large fall in foreign workers partly reflected the significant declines in construction, domestic work and manufacturing employment, which employ high proportions of foreigners. In comparison, resident employment rebounded strongly in H2 2020, following the steep contractions in H1, to expand by 14,900 (or 0.6%) for the year as a whole. Consequently, the foreign share of total employment dipped by 3.5 percentage points to 34.2% in 2020.³

Chart 3.3 Foreigners accounted for all of the decline in employment last year

Employment change by residency



Source: MOM

Significant policy support underpinned the recovery in resident employment

Policy support for resident workers likely facilitated the continued strong recovery of resident employment in Q4. Government policies to subsidise wages for resident workers (Jobs Support Scheme (JSS)), match workers to available jobs and training (SGUnited Jobs and Skills Package) and incentivise hiring of residents (such as the Jobs Growth Incentive (JGI)) likely accounted for much of the strong demand for resident workers. (For an analysis of the labour market policy response to COVID-19, please refer to Box B.)

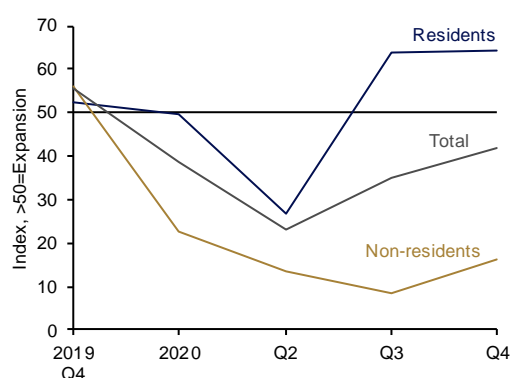
At the same time, border measures to manage the spread of COVID-19 led to some constraints on the hiring of foreign workers, and likely encouraged firms to hire resident workers for some roles that might have been filled by foreign workers in the past. These constraints include travel restrictions that make it difficult for firms to bring in new workers to replace outgoing ones, as well as the higher costs of bringing foreign workers into Singapore due to Stay-Home Notice and testing requirements. There also continued to be restrictions on non-residents' inbound travel to Singapore from countries where COVID-19

³ Excluding foreign domestic workers, foreign share of total employment was 29.3% as at end-2020, down from 33.1% in end-2019.

risks remained high. These constraints, coupled with wage subsidies for residents, have incentivised firms to hire resident workers to meet returning labour demand, supporting the resident employment recovery alongside the normalisation of economic activities. Indeed, MOM's Employment Diffusion Index (EDI) for resident employment registered a reading of about 64 in both Q3 and Q4 2020 indicating that resident employment rose in most sectors of the economy (**Chart 3.4**).⁴ In contrast, the low EDI for non-resident employment suggests that the weakness continued to be fairly broad-based in Q4.

Chart 3.4 Recovery in resident employment has been broad-based

Employment diffusion index

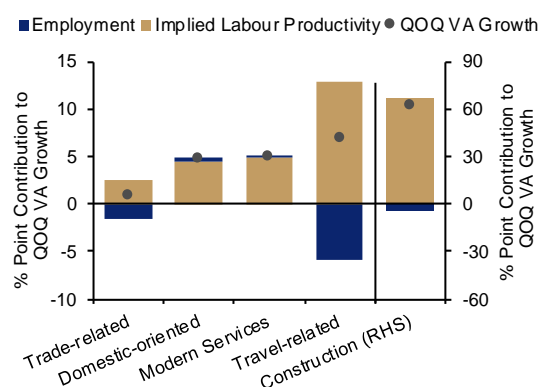


Source: MOM

Note: The series exclude foreign domestic workers.

Chart 3.5 Labour productivity improved

Components contributing to q-o-q VA growth in Q4 2020



Source: DOS, MOM and EPG, MAS estimates

The return of labour demand is being met through a combination of increase in hiring as well as productivity improvements

Apart from renewed hiring, firms have sought to meet recovering labour demand by increasing hours worked and enhancing productivity. Average weekly total paid hours worked per worker rose in December 2020, compared to the same period in 2019, in about a quarter of the 28 segments monitored, mainly in the manufacturing and retail trade sectors. Businesses also appear to be raising labour productivity amid the initial upturn in demand. Labour productivity grew robustly by around 5.6% q-o-q in Q4 2020, even as total employment continued to decline. The strong recovery in overall productivity in Q4 was most evident in the construction sector, although gains were fairly broad-based (**Chart 3.5**). For example, productivity rose significantly in the travel-related sector as all the early recovery in VA was accommodated by higher productivity. Indeed, the travel-related sector continued to shed a significant number of workers in Q4, as cost-cutting manpower consolidation likely continued apace.

Labour market slack is being gradually absorbed

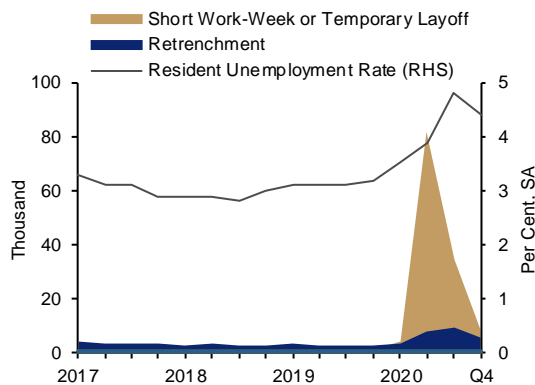
As labour demand recovered, overall slack in the domestic labour market continued to decline in Q4 2020. After rising for five consecutive quarters, total retrenchments fell in Q4, with fewer firms citing 'recession' or 'downturn' as reasons for retrenching workers

⁴ The EDI ranges from 0 to 100 and provides an indication of how widespread employment change is across 203 component industries. The further away the index is above (below) 50, the more broad-based employment expansions (contractions) are. See MOM (2021), "Labour Market Report 2020", March 16.

(Chart 3.6). The number of workers placed on short work-week or temporary layoff—a measure of latent labour market slack—also dropped further in Q4 to around a quarter of the level in Q3. On the whole, EPG’s labour market pressure indicator (LMPI), a summary statistic which captures the extent of labour market tightness using 31 indicators, was significantly less negative in Q4 2020 **(Chart 3.7)**. The negative reading, however, suggests that the labour market still has some degree of spare capacity. For example, the ratio of job vacancies to unemployed persons, while edging up further to 0.77, remained below the historical average of about unity. The resident unemployment rate also stayed elevated even as it eased from its peak in September. Consequently, resident wage growth was still relatively subdued, averaging 1.6% y-o-y in Q4, below its historical norm of 3–3.5%, though higher than the 0.6% growth in Q3.

Chart 3.6 Labour market indicators showed a reduction in the amount of slack ...

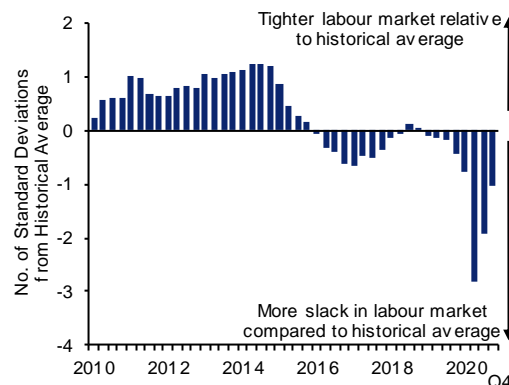
Various indicators of labour market conditions



Source: MOM

Chart 3.7 ... although there is still spare capacity in the labour market

Quarterly labour market pressure indicator



Source: EPG, MAS estimates

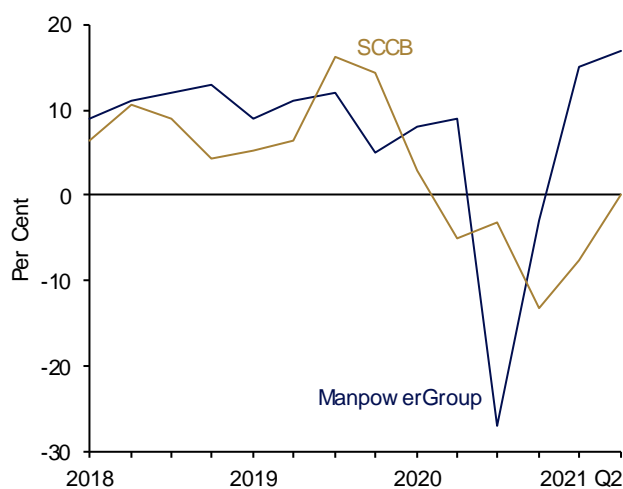
Domestic labour demand is anticipated to pick up further alongside firm GDP growth

The domestic labour market should continue to recover at a steady pace in the quarters ahead. Latest business expectation surveys by the ManpowerGroup and Singapore Commercial Credit Bureau (SCCB) show an improvement in the net proportion of firms expecting to expand headcount in the short term, compared to previous readings **(Chart 3.8)**. The resident unemployment rate also dipped further to 4.1% in February 2021 from the peak of 4.8% in September last year.

However, total employment may not recover completely to pre-COVID levels in the near term, as labour demand in parts of the economy has likely shifted structurally lower. In particular, some of the projected increase in labour productivity is expected to be permanent, as automation and digitalisation initiatives adopted during COVID-19 will allow firms to rely on fewer labour inputs in the medium term. The pandemic may also have accelerated the economy’s shift away from low productivity sectors badly impacted by COVID-19, towards higher VA per worker sectors with strong post-COVID growth prospects.

Chart 3.8 Hiring is likely to pick up

ManpowerGroup and SCCB net employment outlook for Singapore



Source: ManpowerGroup and SCCB

Note: The net employment outlook refers to the percentage of surveyed employers expecting to increase headcount less the percentage of employers expecting to reduce employment during the period. Data for each quarter are based on surveys conducted in the previous quarter.

Against the backdrop of continuing support for resident workers and restrictions on international travel, resident employment is expected to expand more strongly than foreign employment this year. The JGI has been extended to September 2021, while the easing of constraints on the inflow of foreign workers will hinge on the global COVID-19 situation, which remains uncertain amid questions over the efficacy of vaccines and the virulence of new strains of the virus. Robust demand for resident workers should lead to a steady decline in the resident unemployment rate over the year and encourage local jobseekers to enter (or re-enter) the labour force. Shifts towards more flexible working arrangements, including work-from-home, could facilitate a further increase in resident labour force participation. More broadly, the labour force participation rate of resident females has been on a long-term trend increase, closing the gap with that of their male counterparts.

Nevertheless, some moderate amount of labour market slack could persist even at the end of 2021. The persistence reflects the likelihood of some matching frictions in hiring of displaced workers by sectors where labour demand is robust and growing. Further, if jobseekers in short-term jobs, traineeships or company attachments under the SGUnited Jobs and Skills Package are unable to transition to full-time positions, they would, in the near term, add to the number of unemployed workers.

In addition, time-related underemployment remained high at 4.1% in Q4 2020, suggesting that a significant number of resident workers are involuntarily employed in part-time positions.⁵ Even as the resident unemployment rate declines, residents working less hours than desired or in positions that significantly underutilise their capabilities will contribute to underlying labour market slack, thus also capping wage growth this year.

⁵ An individual is considered time-related underemployed if the individual is currently working part-time but is willing and able to engage in additional hours of work. However, the time-related underemployed could also be in part-time employment for reasons other than being unable to find a full-time job, for example, for family or personal reasons.

Wage cost pressures are expected to be contained this year, although there are upside risks

Accordingly, wage growth is projected to remain relatively muted in 2021. Resident wage growth is anticipated to rise only slightly from the 1.4% recorded last year, in part reflecting its lagged response to improving labour conditions. Lingering economic uncertainties and weakened corporate balance sheets should also cap the pace of resident wage increases. Meanwhile, a rebound in productivity should temper some of the increase in effective labour costs to businesses, even as wage subsidies that have sharply lowered unit labour costs taper off over the year.

Nonetheless, labour market conditions could possibly be somewhat tighter than currently projected towards the end of 2021, stemming from stronger-than-expected demand for workers. The anticipated step-up in underlying productivity could also fail to materialise if firms take longer than expected to transit to less labour-intensive methods of production. Against these constraints to the economy's aggregate supply capacity, stronger labour cost pressures could emerge towards the end of the year, and into 2022.

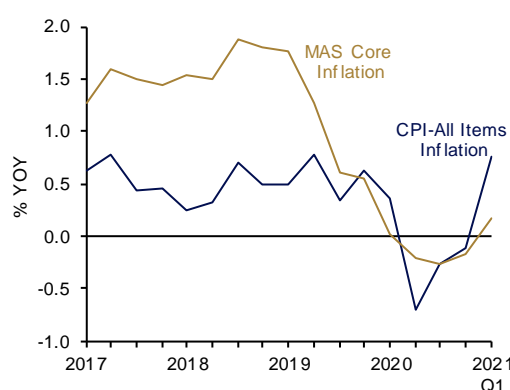
3.2 Consumer Price Developments

Core and headline inflation recorded mild positive increases in Q1 2021

MAS Core Inflation rose to 0.2% y-o-y in Q1 2021, a reversal from the 0.2% decline in Q4 2020 (**Chart 3.9**). The increase was driven primarily by imputed and administrative components in services inflation. Meanwhile, CPI-All Items inflation picked up more strongly to 0.8% from -0.1% over the same period, mainly on account of the turnaround in private transport costs (**Chart 3.10**). Accommodation inflation edged up as well in Q1.

Chart 3.9 Both core and headline inflation turned positive in Q1 2021

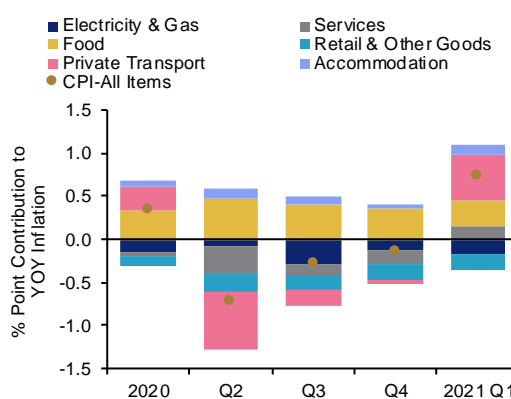
MAS Core Inflation and CPI-All Items inflation



Source: DOS and MAS

Chart 3.10 Headline inflation rose more sharply due to stronger inflation in non-core components

Y-o-y contribution to CPI-All Items inflation



Source: DOS and EPG, MAS estimates

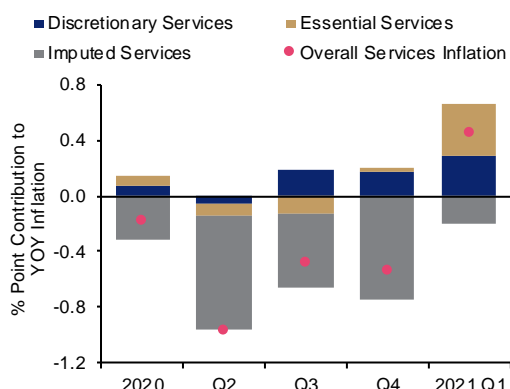
The rise in core inflation reflected fading disinflationary effects from government subsidies, and higher imputed cost of travel-related services

Government measures, specifically enhanced preschool subsidies and subsidies for respiratory illnesses under the Public Health Preparedness Clinics scheme, which dampened essential services inflation over most of 2020, ceased to weigh on inflation in Q1 this year. Meanwhile, travel-related components of the CPI such as airfares and holiday expenses are still largely imputed as these services remain interrupted by the ongoing international travel restrictions. The imputed costs, which are based on price changes in the rest of the CPI-All Items index, rose sequentially and contributed to the bulk of the increase in y-o-y services inflation in Q1 (**Chart 3.11**).⁶

⁶ In line with international practice, prices of items with little or no expenditure are imputed by following the price direction of other sub-indices in the CPI-All Items. The imputed prices do not reflect the actual price changes for the corresponding components. For more details, please refer to the Technical Note in the Department of Statistics' release titled "Singapore Consumer Price Index for March 2021".

Chart 3.11 The increase in services inflation was mainly driven by technical factors

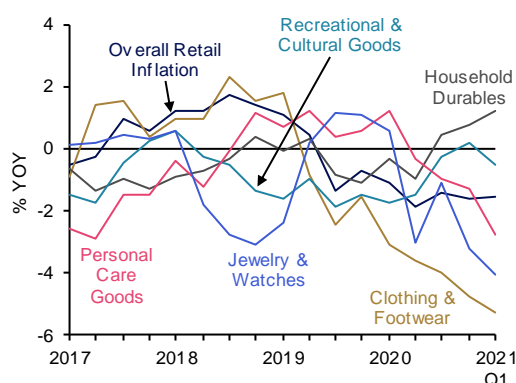
Y-o-y contribution to overall services inflation



Source: DOS and EPG, MAS estimates

Chart 3.12 Most retail goods prices continued to fall at a steep pace

CPI inflation of selected retail goods categories



Source: DOS

Underlying inflation in the economy remained low as price increases were modest for most goods and services

At the same time, inflation in the rest of the core CPI basket stayed relatively subdued. Price increases of prepared meals fell in Q1, in tandem with the easing in F&B sales volumes, which are still 23% below pre-COVID levels in Jan–Feb this year. The shortfall in sales was likely due to constraints on the capacity of F&B establishments as well as the continued absence of international tourism. These factors likely weighed on food services inflation.⁷

Meanwhile, non-cooked food inflation continued to ease, falling further to 2.3% in Q1 2021 from its peak of 4.0% in Q2 last year. Although prices picked up sequentially in the first quarter of this year due to higher seasonal demand during Chinese New Year and poor weather conditions in major food-producing countries, y-o-y non-cooked food inflation continued to edge down. Apart from lower demand dampening price increases for most non-cooked food, global pork prices had decreased alongside the recovery in pork supplies as Chinese producers aggressively rebuilt their herds since the African Swine Fever hit supplies in 2019.

Prices of retail & other goods fell by 1.6% y-o-y in Q1 2021, similar to the pace of decline in Q4 2020 (**Chart 3.12**). As of March 2021, price indices for a wide range of retail goods remained below their Q4 2019 levels. While inflation for telecommunication equipment and household durables rose in Q1, reflecting continuing shifts in household consumption patterns, these were insufficient to offset price weakness in a broad range of other retail goods. The lack of tourist spending as well as strong competitive pressures from e-commerce platforms were likely the main factors keeping overall retail inflation well below its five-year historical average of 0.4% p.a. Notably, the fall in prices was most pronounced in the clothing and footwear segment, which dipped by a record 5.3% y-o-y in Q1 2021.

However, there were also nascent signs of an uptick in inflation in some components of core CPI basket. Pockets of discretionary services, such as point-to-point transport services and recreational & cultural services saw larger price increases, reflecting the further recovery

⁷ The October 2020 *Macroeconomic Review* noted that non-resident expenditure in the domestic economy—a proxy for tourism expenditure—had a direct and significant effect on core inflation. One of the main components driving this result was restaurant food inflation which makes up 8% of the core CPI basket.

in consumption expenditure alongside greater mobility and economic activity in recent months.

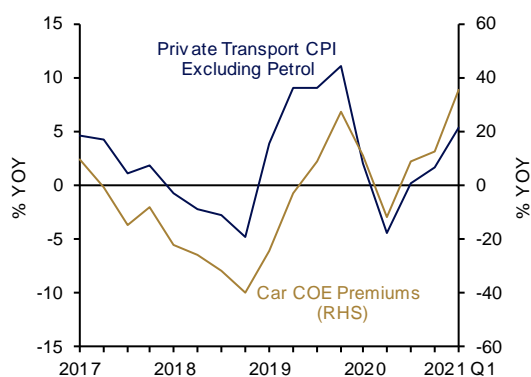
CPI-All Items inflation rose on account of a sharp increase in private transport costs

Inflationary pressures were more evident in the volatile, non-core components of the CPI. Private transport costs rose by 4.4% y-o-y in Q1, a sharp reversal from the 0.5% decline in the preceding quarter, as car prices rose in line with steep increases in COE premiums in December 2020 and January 2021 (Chart 3.13). Moreover, petrol prices stopped declining on a y-o-y basis in Q1 this year, due to the rise in global oil prices and the hike in petrol duties in February.

Meanwhile, accommodation inflation edged up to 0.5% in Q1, from 0.3% in Q4 2020 as rebates for households living in public rental flats ended in Q4 2020 (Chart 3.14).⁸ Demand and prices for rental accommodation have remained firm, notwithstanding the sharp contraction in the foreign workforce last year. The resilient demand for rental housing likely reflected temporary housing needs from Malaysian workers (who would normally commute daily across the border), residents consuming more accommodation services amid the shift to work-from-home arrangements, as well as returning Singapore residents seeking temporary accommodation. Delays in the completion of residential housing units last year may have also contributed to firming rentals.

Chart 3.13 Car prices rose at a faster pace as COE premiums trended higher

Private transport CPI excluding petrol and car COE premiums

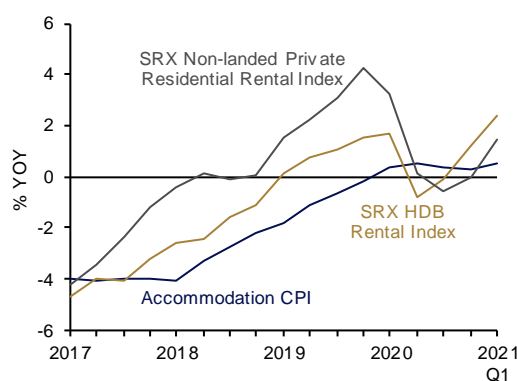


Source: DOS, LTA and EPG, MAS estimates

Note: Car COE premiums refer to the average of COE premiums for Category A and Category B vehicles weighted by their shares of actual COE quotas awarded in each tender. There were no COE bidding exercises in Q2 2020—the datapoint for Q2 2020 in this chart reflects March 2020 weighted average COE premiums.

Chart 3.14 Both HDB and private housing rents increased

Rental price indicators and accommodation CPI



Source: DOS and SRX

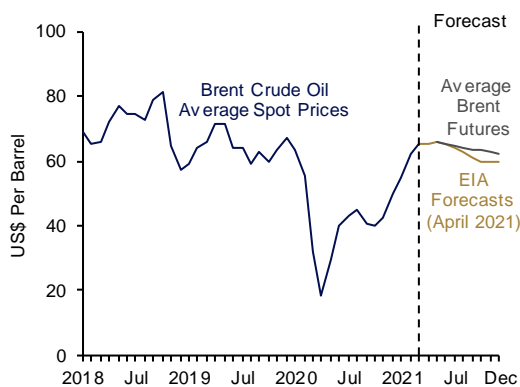
⁸ Households living in public rental flats received 50 per cent rental rebates from October to December 2020 as part of government measures to help households cope with the economic impact of the pandemic.

Global inflation is picking up but is not expected to accelerate beyond the near-term increase

Global price pressures, which had remained subdued since the onset of the pandemic, showed signs of a turnaround in recent months. Notably, oil prices rose by 37% in Q1, fuelled by OPEC+ members' strong compliance to output cuts, as well as expectations of higher oil demand amid improvements in the global macroeconomic outlook. Brent crude oil prices are now projected to average US\$62 per barrel in 2021, up almost 50% from US\$42 last year (Chart 3.15). Apart from higher oil prices, supply-side constraints have also begun to lift producer price inflation in major economies such as the US and China, which could have an impact on global goods inflation in the quarters ahead. For instance, global freight rates soared in H2 2020 amid port congestion and container box shortages along certain global shipping routes. Global food commodity prices also rose further in Q1 this year, due in part to continuing pandemic-induced production disruptions (Chart 3.16).

Chart 3.15 Oil prices have risen and are projected to average higher in 2021

Brent crude oil prices and forecasts

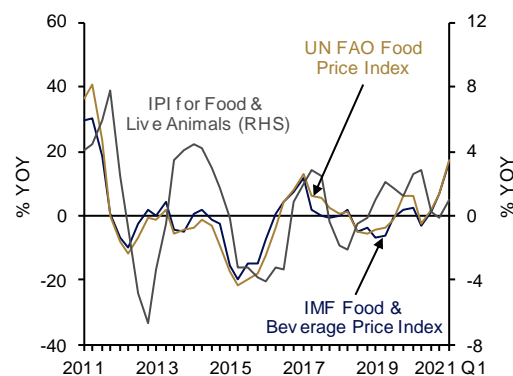


Source: Bloomberg and US Energy Information Administration

Note: Brent futures prices were averaged over working days from 1 March to 31 March 2021.

Chart 3.16 Imported inflation for non-cooked food should pick up alongside global prices

Global food price indices and Singapore's import price index for food & live animals



Source: DOS, IMF and UN Food and Agriculture Organization (FAO)

Note: Latest datapoint for import price index for food & live animals refers to the average y-o-y change in Jan–Feb.

Beyond the near-term pickup, the pace of increase in global prices is not expected to accelerate in the quarters ahead, hence limiting imported inflation in Singapore. Global oil prices should remain relatively stable for the rest of 2021, as surplus oil production capacity will curb further large price increases. Moreover, lingering negative output gaps in a number of Singapore's key trading partners should keep imported inflation contained. Even as some of the pickup in international food commodity prices could result in imported food prices rising in the coming months, the supply-side disruptions to global food production are unlikely to intensify anew, with the vaccine rollout providing some degree of assurance. Meanwhile, the magnitude of increase in Singapore's container freight rates should be well below the hikes seen in international freight indices, as local shipping rates are usually fixed by long-term contracts.⁹ Freight charges also account for a small share (around 3%) of total

⁹ Average Drewry World Container Index rose by close to 40% q-o-q in Q4 last year while Singapore's sea freight transport price index only increased by 2.4% q-o-q. Similarly, while the World Container Index surged by around 67% in Q1 this year, Singapore's sea freight transport price index is expected to show a significantly smaller increase.

operating costs of services firms in Singapore, suggesting that the direct pass-through effects of higher freight rates to consumer prices would be modest.

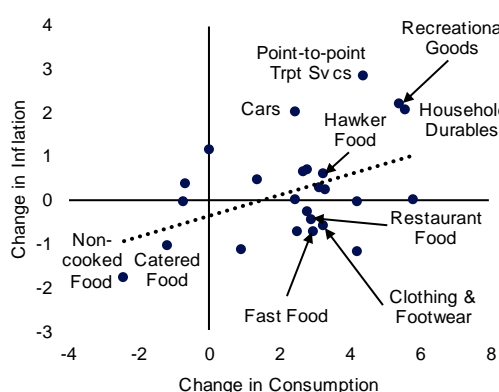
On the domestic front, strengthening private consumption expenditure will support general price increases

The recovering labour market and rising consumer confidence, bolstered by the build-up in household savings, should lead to stronger private consumption expenditure this year (See Chapter 2.3). Individuals' propensity to spend appears to have improved in December 2020 compared to August.¹⁰ Spending on discretionary goods and services, in particular, picked up compared to spending on essentials. The overall improved sentiment and stronger projected consumption expenditure should support a gradual rise in inflation. **Chart 3.17** shows that higher expenditure is typically associated with higher inflation across CPI categories. Moreover, the anticipated further easing of safe distancing measures over 2021 will likely support price increases across more core CPI components (such as recreational & cultural services).

CPI-All Items inflation is expected to remain above MAS Core Inflation this year, reflecting the effects of strong private transport inflation. Households' demand for cars is anticipated to be firm for the rest of the year in tandem with the brighter economic outlook. On the supply side, the drop in the number of cars nearing 9 to 10 years of age should lead to lower de-registration rates, causing COE supply to tighten, although this should be partially offset by a projected increase in the number of revalidated COEs that are expiring this year (**Chart 3.18**). On balance, firm demand and tighter COE supply should lead to resilience in premiums, which will in turn contribute to the strong turnaround in private transport costs this year. Higher private transport costs will be a significant factor driving the rise in headline inflation in 2021.

Chart 3.17 Higher consumption expenditure is typically associated with higher inflation

Demand and price changes across various CPI components

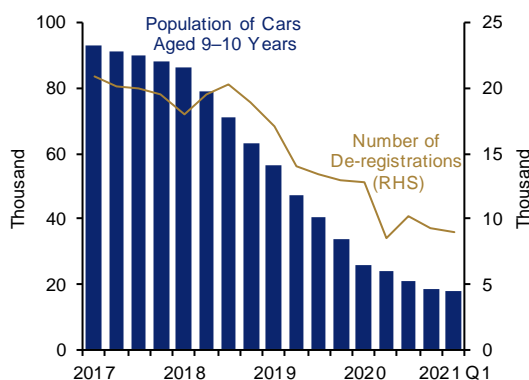


Source: DOS, LTA and EPG, MAS estimates

Note: Changes in inflation and consumption refer to the respective differences in y-o-y rates between Q2 and Q4 2020 scaled by the standard deviation over 2015–20. Consumption changes are based on private consumption expenditure, retail sales and taxi ridership (proxy for point-to-point transport services).

Chart 3.18 Supply of COE quotas is expected to shrink as car de-registrations trend lower

Number of car de-registrations and cars aged 9 to 10 years



Source: LTA

¹⁰ DBS Asian Insights (2021), "No Storm Lasts Forever: Impact of COVID-19 on Financial Wellness", March 2.

Inflation in several CPI components is still likely to remain relatively subdued. While the pace of decline will ease, the rate of inflation for clothing & footwear and personal care products is unlikely to increase markedly on account of competitive pressures from e-commerce platforms, shifts in household consumption patterns and the continuing lack of foreign tourist expenditure. As more social activities resume, the recovery in demand for prepared meals—and concomitant decline in demand for non-cooked food—should also cap non-cooked food inflation, even as imported food costs begin to firm. While the pickup in discretionary expenditure will support some rise in food services inflation, the emergence of cloud kitchens and home food businesses, which was accelerated by the circuit breaker last year, is a further source of competitive pressure for F&B establishments. Catered food inflation will likely also remain weak until business and social gatherings are fully normalised.

Inflation in components that are more significantly affected by administrative measures is projected to continue to come in below historical averages in 2021. Healthcare and education inflation should rise from their lows in 2020, but this pickup would mostly reflect the dissipation of subsidies that were previously introduced. Moreover, enhancements to the Partner Operator (POP) scheme including lower fee caps,¹¹ as well as the COVID-19 subsidies to offset the increase in MediShield Life premium¹² implemented this year will keep education and healthcare inflation low.

Business cost pressures are expected to remain contained

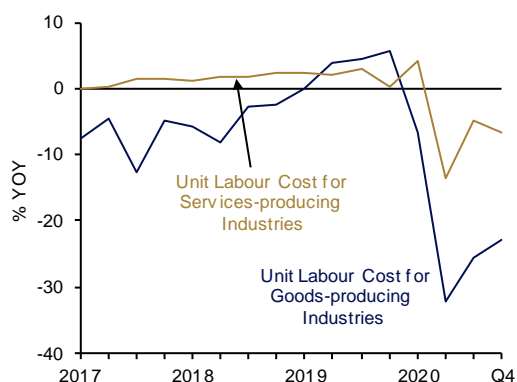
Overall unit labour cost fell by 10.7% y-o-y in Q4 2020, slightly steeper than the 10.2% decline in Q3 as improvements in labour productivity more than offset the smaller drop in labour costs faced by firms (**Chart 3.19**). For 2021 as whole, firms' total labour costs are anticipated to pick up as government wage support measures expire, although productivity gains will partially offset some of the increase. While resident wages are expected to grow at a slightly faster pace this year, the elevated resident unemployment rate and some degree of latent labour market slack should restrain overall wage cost pressures. Meanwhile, commercial rental costs should remain modest as both office and retail rents continued to decline on a y-o-y basis in Q1 2021 (**Chart 3.20**). Moving forward, the reduced need for office and shop space from the structural shift towards hybrid work arrangements and greater e-commerce adoption, respectively, should raise land productivity and contain overall rent pressures.

¹¹ The caps on fees charged by POP centres were reduced by 5% to \$760 and \$1,330 per month for full-day childcare and infant care services respectively in the new POP term.

¹² COVID-19 subsidies are provided to all Singapore Citizens for two years after the increase in MediShield Life premiums in 1 March 2021. The subsidies cover 70% of the net premium increase in the first year, followed by 30% of the net premium increase in the second year.

Chart 3.19 Unit labour costs stayed low as productivity gains offset higher labour costs

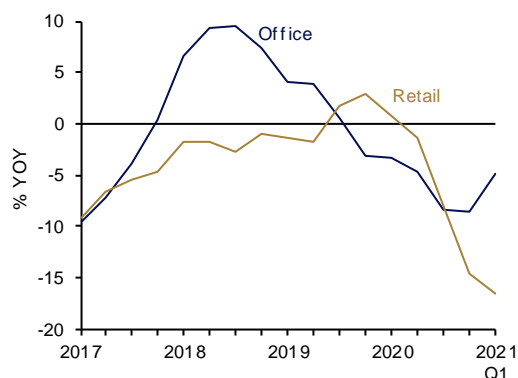
Unit labour cost indices



Source: DOS

Chart 3.20 Weak leasing demand kept retail rents on a decline

URA office and retail rental price index



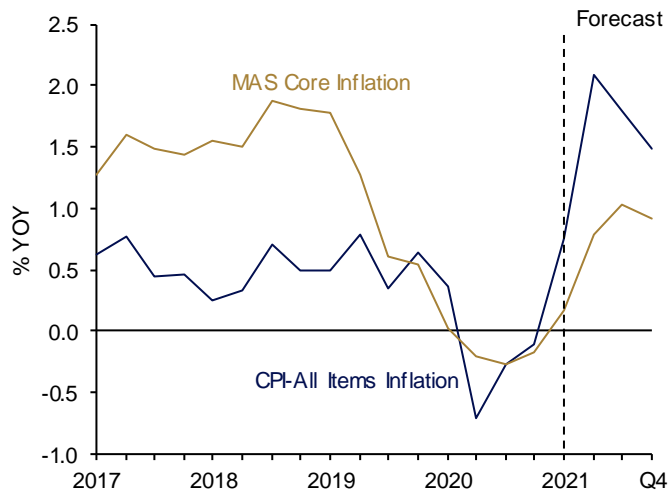
Source: URA

All in, inflation is projected to pick up further through 2021 but underlying price pressures in the economy are not expected to accelerate

In the near term, both MAS Core Inflation and CPI-All Items inflation are anticipated to step up to their highs in Q2–Q3 this year due to the low base in 2020 (**Chart 3.21**). However, the pace of increase in both inflation measures should ease in H2, as underlying external and domestic inflationary pressures are expected to be moderate. The upward pressure on global inflation is projected to ease in the latter part of 2021, in line with more modest increases in global commodity prices and the resolution of supply bottlenecks and disruptions. Divergent economic recoveries across countries also imply that output gaps in a number of Singapore's key trading partners will remain negative, keeping imported inflation contained. On the domestic front, a more broad-based increase in inflation will return as the labour market and private consumption recover further, but the pickup should be gradual due to lingering slack in the labour market (**Chart 3.22**). Structural factors that are encouraging higher productivity should also cap effective land and labour cost increases. Overall, subdued business cost pressures, the continued absence of non-resident spending, and competitive pressures arising from e-commerce should keep inflation for most components below historical averages.

Chart 3.21 Core and headline inflation are expected to rise modestly in 2021

MAS Core Inflation and CPI-All Items inflation forecasts

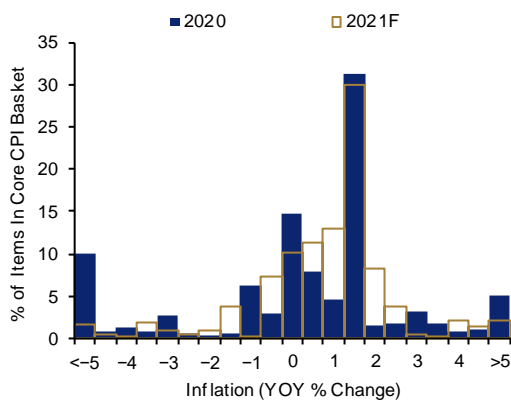


Source: DOS and EPG, MAS estimates

Beyond the near-term step-up, core inflation is forecast to rise gradually, and come in at 0–1% for this year as a whole. The projected turnaround in core inflation from –0.2% in 2020 is largely driven by higher services costs and a smaller decline in the cost of electricity & gas. Higher imputed travel-related prices and the dissipation of disinflationary effects from earlier administrative measures will account for the bulk of the rise in services costs. Meanwhile, headline inflation is estimated to average 0.5–1.5%. The higher forecast range compared to MAS Core Inflation reflects the projected sharp turnaround in private transport inflation this year (Chart 3.23).

Chart 3.22 Inflationary pressures are expected to pick up and broaden this year

Distribution of inflation rates across components of MAS Core CPI basket

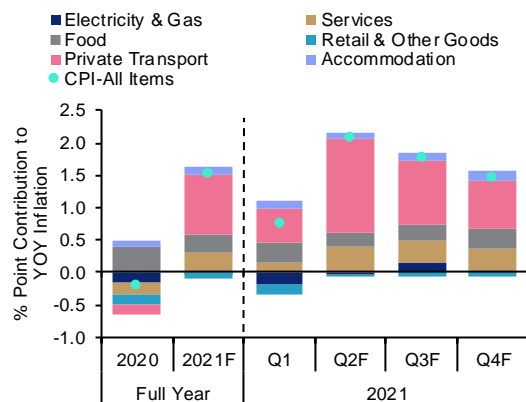


Source: EPG, MAS estimates

Note: % of items in MAS Core CPI basket is derived using the 2019-based CPI weights and inflation rates for the components.

Chart 3.23 Headline inflation is forecast to rise on the back of higher private transport inflation

Y-o-y contribution to CPI-All Items inflation



Source: DOS and EPG, MAS estimates

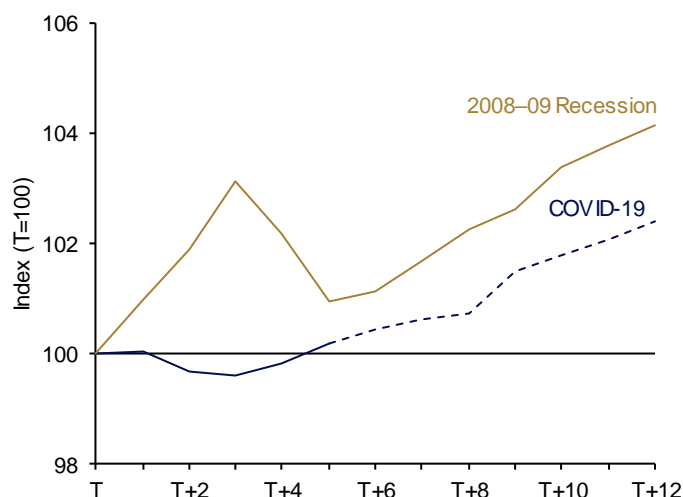
Core inflation is expected to pick up more slowly from the COVID-19 trough compared to the recovery from the 2008–09 recession

The projected rise in core inflation in the quarters ahead is likely to be more gradual than in the aftermath of the 2008–09 downturn. **Chart 3.24** plots the expected trajectory of core prices from the period just before the pandemic to the end of 2022, against the profile of core prices in the twelve quarters from the peak of GDP in Q1 2008.¹³ Core prices continued to rise following the decline in GDP in 2008, driven in part by the lagged pass-through of global commodity prices that were on a powerful up-cycle. In fact, the core price index only started to decline in Q1 2009, when the Singapore economy had troughed. In comparison, core CPI fell almost immediately following the onset of the pandemic and levelled off earlier in the cycle. From its low in Q3 2020, it is expected to rise at a slower q-o-q pace over the next seven quarters compared to the same period from the trough of core CPI in 2009.

The more muted profile of core inflation in the current cycle reflects several factors, including the slower, more uneven GDP recovery this time round and structural factors that were weighing on inflation prior to COVID-19. Unlike the 2008–09 cycle, global food commodity and oil prices were weak in the period before the onset of the pandemic and are expected to only rise modestly going forward given ample supply. In comparison, global oil prices rose 29% in 2010 and a further 40% in 2011. In addition, factors such as the impact of e-commerce, that were insignificant more than a decade ago, will continue to be a drag on retail goods inflation. Travel-related items, which have historically been a significant part of the cyclical swings in core inflation, are also not expected to drive inflation up quickly in this recovery.

Chart 3.24 Core inflation could recover at a more gradual pace compared to the 2008 cycle

Comparison of MAS Core CPI across business cycles



Source: DOS and EPG, MAS estimates

Note: T=Q4 2019 for COVID-19 and T=Q1 2008 for the 2008–09 recession. T refers to the pre-recession peak in GDP levels. MAS' Core CPI forecast (for Q2 2021 to Q4 2022) is shown by the dotted blue line.

¹³ The 2008–09 recession in Singapore began in Q1 2008 when real GDP peaked. Real GDP subsequently troughed in Q1 2009.