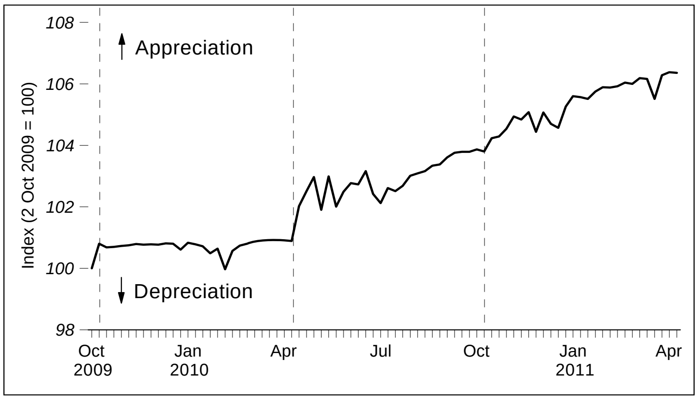
14 April 2011

Monetary Policy Statement

INTRODUCTION

1. In October last year, MAS increased slightly the slope of the S$NEER policy band, with no change to the level at which the band was centred. This policy decision was made in light of upside risks to inflation amidst sustained high levels of domestic economic activity. At the same time, the policy band was widened slightly to accommodate volatility across international financial markets.

Chart 1
S$ Nominal Effective Exchange Rate (S$NEER)



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2. Since then, the S$NEER (Chart 1) has appreciated gradually within the upper half of the policy band. This took place in the context of a general strengthening in regional currencies given broad-based weakness in the US$ and continued investor interest in higher-growth Asian and emerging markets. Amidst conditions of abundant global liquidity, the domestic three-month interbank rate has eased further since end-October last year to 0.44%.

OUTLOOK FOR 2011

3. The Singapore economy saw a step-up in the level of economic activity in Q1 this year following a slowdown in H2 2010. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, Singapore's GDP expanded by 23.5% on a quarter-on-quarter seasonally adjusted annualised basis in Q1 2011. The expansion was broad-based across the trade-related[1] and services sectors, reflecting an improvement in final demand.

4. The global economy is expected to grow at a moderate pace in 2011, notwithstanding the increased uncertainty arising from the spike in oil prices and the calamity in Japan. Supported by a gradual improvement in the labour market and accommodative fiscal measures, the US economy should continue on its recovery path. In Asia ex-Japan, resilient household spending and a pickup in business investment are expected to underpin growth. In Singapore, while a temporary slowdown is forecast for Q2, economic growth is projected to be sustained across a wide range of industries for the rest of the year. Reflecting in part the robust expansion in Q1, GDP growth for the year as a whole is likely to be at the upper end of the 4-6% forecast range.

5. CPI inflation rose from 3.4% in Q3 2010 to 5.2% in the first two months of 2011, while MAS Core Inflation[2] remained at around 2%. The increase in headline inflation was largely due to a sharp rise in COE premiums and imputed rentals, but the contribution of these two factors will ease as base effects dissipate. However, wage pressures have been building up amidst a tightening labour market. Although the pass-through of wages to services costs has been relatively muted so far, the pass-through could strengthen given firm economic conditions. On the external front, global oil and food prices have increased and will remain high. Taken together, headline inflation is forecast to stay elevated and will moderate only gradually to around 3% by Q4 2011. For the whole year, CPI inflation is expected to come in at the upper half of the 3-4% forecast range[3] while MAS Core Inflation will be 2-3%.

MONETARY POLICY

6. Economic activity is likely to be sustained at a high level for the rest of the year, even as the underlying growth momentum moderates. With factor markets tight, domestic cost and price pressures will remain firm.

7. MAS will therefore re-centre the exchange rate policy band upwards. The exchange rate policy band will be re-centred below the prevailing level of the S$NEER. This adjustment takes into account the tighter policy stance adopted in April and October last year, which will continue to have a restraining effect on the economy and prices. There will be no change to the slope and width of the band. This policy will ensure price stability in the medium term while keeping growth on a sustainable path.

1/ These comprise manufacturing (excluding pharmaceuticals), wholesale trade and transport & storage services.

2/ Excludes the cost of private road transport and accommodation.

3/ The 2011 CPI inflation forecast was revised upwards to 3-4% at MTI's Annual Economic Survey media briefing on 17 Feb 2011.