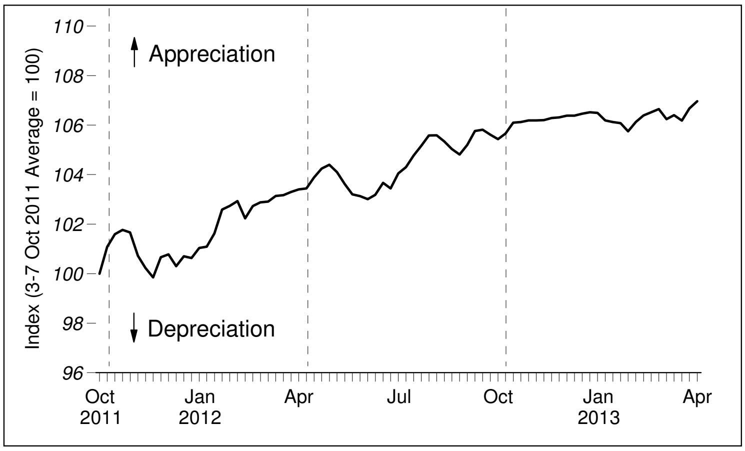
12 April 2013

Monetary Policy Statement

INTRODUCTION

1. In October 2012, MAS maintained the modest and gradual appreciation path of the S$NEER policy band, with no change to its slope, width, and the level at which it was centred. This policy stance was deemed appropriate for containing inflationary pressures amid the ongoing economic restructuring.

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



- - - - - indicates release of Monetary Policy Statement

2. The S$NEER has continued to fluctuate in the upper half of the policy band over the last six months. The broad-based decline in the Japanese yen led to upward pressure on the S$NEER, although a strengthening in the US dollar, due to speculation of an early exit from quantitative easing in the US and renewed uncertainty over the European debt crisis, resulted in bouts of domestic currency weakness. With persistently low interest rates worldwide, the domestic three-month interbank rate has remained generally stable at 0.38% since December 2011.

OUTLOOK FOR 2013

3. Singapore's GDP is expected to grow by 1–3% in 2013. While the economy experienced some consolidation in the first three months of 2013, it should see a gradual improvement for the rest of the year, on the back of a recovery in external demand. CPI-All Items inflation is expected to come in at 3–4%. Although MAS Core Inflation is forecast at 1.5–2.5% for the year as a whole, it is expected to rise moderately in the latter half, reflecting persistent tightness in the labour market.

Growth

4. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, Singapore's GDP declined by 1.4% in Q1 2013 on a quarter-on-quarter seasonally adjusted annualised basis, following an increase of 3.3% in Q4 2012. Industrial production data for the first two months of the year showed that the contraction in the manufacturing sector was mainly confined to the biomedical and transport engineering clusters. Electronics production, which had experienced three consecutive quarters of decline, picked up modestly in January–February. Other sectors, such as financial services and construction, helped to buttress overall economic activity.

5. The outlook for the world economy has improved since late last year, although uncertainties remain, particularly with regard to Europe. The recovery in the G3 as a whole will be underpinned by the gradual pickup in the housing market and private demand in the US, as well as the fiscal stimulus in Japan. At the same time, economic activity in China will be sustained on the back of robust domestic demand, and the rest of Asia will see continued moderate growth. These developments should also provide a modest lift to the global IT industry, following a contraction in 2012.

6. Singapore's manufacturing sector and export-oriented services industries should improve gradually over the course of the year. Domestic-driven sectors, such as construction and related financing and real estate activities, will remain resilient. The level of output in the economy will further converge to its underlying potential, while the labour market remains at full employment, in part reflecting supply-side constraints.

Inflation

7. Imported price pressures have been generally mild in recent months, given favourable supply conditions in commodity markets and the cumulative impact of the S$NEER appreciation. While domestic costs have risen amid a tight labour market, their pass-through to consumer prices has to date been subdued. MAS Core Inflation, which excludes private road transport and accommodation costs, receded to 1.5% y-o-y in January–February 2013, from 2.0% and 2.4% in Q4 and Q3 2012, respectively. Over the same period, CPI-All Items inflation averaged around 4%. There was significant volatility in the monthly readings, mainly from the sharp swings in COE premiums.

8. Looking ahead, supply buffers in the energy and food commodity markets should cap imported inflation. However, continuing tightness in the labour market will add to domestic cost pressures, resulting in a slightly stronger pace of cost pass-through to prices of consumer services. On balance, for the whole of 2013, MAS is lowering its forecast for Core Inflation from 2–3% to 1.5–2.5%, largely reflecting the weaker-than-expected price increases over the past few months.

9. Imputed rentals on owner-occupied accommodation will increase at a slower pace given the upcoming completion of a large number of private housing units. COE premiums have corrected from the high in early 2013, following MAS' tightening of financing restrictions on motor vehicle loans. Although COE premiums could fluctuate as the market continues to adjust to the policy measures, its contribution to CPI-All Items inflation is likely to be lower, and overall inflation should recede from its Q1 high. For the year as a whole, CPI-All Items inflation is expected to come in at 3–4%, down from 3.5–4.5% projected previously. More than half of overall inflation in 2013 will be accounted for by imputed rentals on owner-occupied accommodation and car prices.

Growth

4. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, Singapore's GDP declined by 1.4% in Q1 2013 on a quarter-on-quarter seasonally adjusted annualised basis, following an increase of 3.3% in Q4 2012. Industrial production data for the first two months of the year showed that the contraction in the manufacturing sector was mainly confined to the biomedical and transport engineering clusters. Electronics production, which had experienced three consecutive quarters of decline, picked up modestly in January–February. Other sectors, such as financial services and construction, helped to buttress overall economic activity.

5. The outlook for the world economy has improved since late last year, although uncertainties remain, particularly with regard to Europe. The recovery in the G3 as a whole will be underpinned by the gradual pickup in the housing market and private demand in the US, as well as the fiscal stimulus in Japan. At the same time, economic activity in China will be sustained on the back of robust domestic demand, and the rest of Asia will see continued moderate growth. These developments should also provide a modest lift to the global IT industry, following a contraction in 2012.

6. Singapore's manufacturing sector and export-oriented services industries should improve gradually over the course of the year. Domestic-driven sectors, such as construction and related financing and real estate activities, will remain resilient. The level of output in the economy will further converge to its underlying potential, while the labour market remains at full employment, in part reflecting supply-side constraints.

Inflation

7. Imported price pressures have been generally mild in recent months, given favourable supply conditions in commodity markets and the cumulative impact of the S$NEER appreciation. While domestic costs have risen amid a tight labour market, their pass-through to consumer prices has to date been subdued. MAS Core Inflation, which excludes private road transport and accommodation costs, receded to 1.5% y-o-y in January–February 2013, from 2.0% and 2.4% in Q4 and Q3 2012, respectively. Over the same period, CPI-All Items inflation averaged around 4%. There was significant volatility in the monthly readings, mainly from the sharp swings in COE premiums.

8. Looking ahead, supply buffers in the energy and food commodity markets should cap imported inflation. However, continuing tightness in the labour market will add to domestic cost pressures, resulting in a slightly stronger pace of cost pass-through to prices of consumer services. On balance, for the whole of 2013, MAS is lowering its forecast for Core Inflation from 2–3% to 1.5–2.5%, largely reflecting the weaker-than-expected price increases over the past few months.

9. Imputed rentals on owner-occupied accommodation will increase at a slower pace given the upcoming completion of a large number of private housing units. COE premiums have corrected from the high in early 2013, following MAS' tightening of financing restrictions on motor vehicle loans. Although COE premiums could fluctuate as the market continues to adjust to the policy measures, its contribution to CPI-All Items inflation is likely to be lower, and overall inflation should recede from its Q1 high. For the year as a whole, CPI-All Items inflation is expected to come in at 3–4%, down from 3.5–4.5% projected previously. More than half of overall inflation in 2013 will be accounted for by imputed rentals on owner-occupied accommodation and car prices.

MONETARY POLICY

10. The Singapore economy should experience a modest pace of expansion in 2013. The tightness in the labour market will exert some upward pressures on MAS Core Inflation in the latter half of this year as higher wage costs pass through to consumer prices.

11. MAS will maintain its policy of a modest and gradual appreciation of the S$NEER policy band. There will be no change to the slope and width of the policy band, as well as the level at which it is centred. This policy stance is assessed to be appropriate for containing inflationary pressures, anchoring inflation expectations, and facilitating the restructuring of the economy towards sustainable growth.