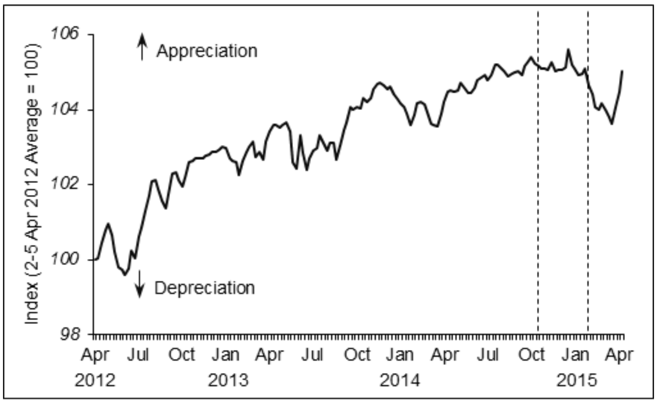
14 April 2015

Monetary Policy Statement

INTRODUCTION

1. In January 2015, MAS reduced the slope of the Singapore dollar nominal effective exchange rate (S$NEER) policy band, with no change to its width and the level at which it was centred. This adjustment to the policy stance, which kept the S$NEER band on a modest and gradual appreciation path, was assessed to be appropriate in view of the more benign inflation outlook.

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



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2. Since the Monetary Policy Statement (MPS) in January, the S$NEER has fluctuated within the lower half of the policy band. It depreciated over February to mid-March amid the broad-based strength of the US$. More recently, the S$NEER has strengthened.

3. The three-month S$ SIBOR rose from 0.67% as at end-January 2015 to 1.01% as at end-March. This reflected market expectations of prospective interest rate hikes in the US and of a strengthening of the US$ against the S$ at a time of general appreciation of the US$ against the major currencies. These expectations also came after six years of very low US rates and a generally strengthening S$ against the US$.

OUTLOOK

4. The Singapore economy is projected to grow at a moderate pace in 2015, with the uplift from the continued recovery in external demand tempered by domestic supply-side constraints. CPI-All Items inflation and MAS Core Inflation will stay subdued this year due to lower oil prices and moderate pass-through of accumulated domestic cost increases.

Growth

5. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, Singapore's GDP growth came in at 1.1% in Q1 2015 on a quarter-on-quarter seasonally adjusted annualised basis, following the 4.9% recorded in Q4 2014. The finance & insurance sector likely registered some pullback in activity, after an exceptionally strong performance in the preceding quarter. Meanwhile, the manufacturing sector remained lacklustre, reflecting the weakness in the electronics, precision engineering and transport engineering clusters. In comparison, the construction sector expanded strongly in Q1 2015, bolstered by the residential building segment.

6. The outlook for the global economy has improved slightly, anchored by a stronger recovery in the G3. The US economy will continue to be the main driver of growth, underpinned by robust private consumption amid sustained improvement in the labour market. The Eurozone and Japan are showing incipient signs of a turnaround, supported by monetary easing and stronger export growth. In comparison, GDP growth in China is slowing on account of sluggish domestic demand, which will have some spillovers to the region. Nevertheless, growth in the other Asian economies will benefit from the G3 recovery and the resilience in private consumption.

7. The sustained, albeit uneven recovery in the global economy should provide a mild uplift to the external-oriented sectors in Singapore. Within manufacturing, the electronics cluster should benefit from the ongoing expansion in the global IT industry, although any gains will be capped by domestic supply-side constraints. An anticipated increase in oil prices during the latter half of the year will provide support to the oil-related manufacturing segments. The domestic-oriented sectors should continue to expand, especially those with firm underlying demand, such as healthcare and education. On balance, Singapore's GDP growth forecast for 2015 remains at 2–4%.

Inflation

8. MAS Core Inflation, which excludes the costs of private road transport and accommodation, eased to 1.2% y-o-y in January–February 2015 from 1.6% in Q4 2014. Compared to a year ago, imported fuel prices in the first two months of 2015 were sharply lower, reflecting the excess supply conditions in the global oil market. Domestic food inflation also declined as the effects of weather-related disruptions to regional food supplies waned. At the same time, domestic cost pass-through to consumer prices was moderate, while enhanced medical subsidies further reduced healthcare costs. Reflecting these factors, as well as weaker imputed rentals on owner-occupied accommodation, CPI-All Items inflation fell to −0.3% y-o-y in January–February 2015 from 0% in Q4 2014.

9. For 2015 as a whole, global oil prices[1] are likely to average significantly below the US$93 recorded in 2014, while domestic food inflation should also be lower. Although underlying cost pressures stemming from the tight labour market remain, the pass-through to consumer prices could continue to be constrained in the near term by the moderate growth environment. MAS Core Inflation is expected to come in at 0.5–1.5% in 2015, unchanged from the January MPS.

10. Car prices and imputed rentals on owner-occupied accommodation will dampen inflationary pressures, amid the expected increase in the supply of COEs and newly-completed housing units. For 2015, CPI-All Items inflation is projected at −0.5–0.5%.

[1] Based on the West Texas Intermediate (WTI) benchmark.

11. MAS Core Inflation and CPI-All Items inflation are expected to ease further before rising towards the end of the year and into 2016, as global oil prices pick up and the effects of the reduction in healthcare costs fade. At the same time, the labour market will be tight. The risk remains that underlying cost pressures in the economy could mount, leading to a stronger pass-through to consumer prices over the medium term.

MONETARY POLICY

12. The Singapore economy is evolving as envisaged in the January MPS. GDP is on track to grow at 2–4% in 2015, and there is no change to the forecasts for CPI-All Items inflation and MAS Core Inflation. External price pressures should be contained, while domestic cost pass-through to consumer prices is expected to be moderate this year. Beyond the near term, underlying cost and price pressures could pick up, given the continued tightness in the labour market.

13. MAS will therefore maintain the 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, and the level at which it is centred. This policy stance is consistent with the benign inflation outlook and moderate growth prospects for the whole of 2015, and appropriate for ensuring medium-term price stability in the economy.