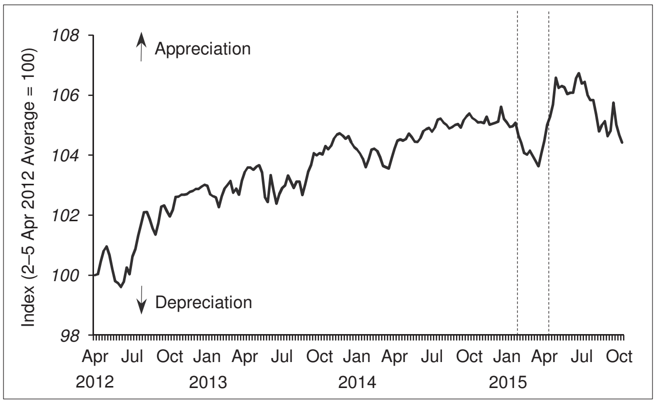
14 October 2015

Monetary Policy Statement

INTRODUCTION

1. In April 2015, MAS maintained the modest and gradual appreciation path of the Singapore dollar nominal effective exchange rate (S$NEER) policy band, with no change to its slope, width and the level at which it was centred. This policy stance, which has been in place since January 2015, was assessed to be appropriate in view of the moderate growth and inflation prospects.

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



indicates release of Monetary Policy Statement

2. Following the Monetary Policy Statement (MPS) in April, the S$NEER appreciated amid a broad-based retraction in US$ strength. Since July, however, the S$NEER has weakened and largely fluctuated in the lower half of the policy band. This reflected renewed expectations of US monetary policy tightening and a rise in global risk aversion, mainly stemming from fears of a more significant downturn in China and other emerging market economies. The three-month S$ SIBOR fell from 1.01% as at end-March 2015 to 0.82% by the end of June, before rising to 1.14% as at end-September 2015.

OUTLOOK

3. The Singapore economy is projected to expand at a modest pace for the rest of 2015 and in 2016, with the uplift from the firmer US economy tempered by weaker growth prospects in the region. MAS Core Inflation will stay subdued in 2015, but should pick up gradually over 2016, largely due to the dissipation of the disinflationary effects of lower oil prices, and budgetary and other one-off measures.

Growth

4. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, the Singapore economy registered marginal growth of 0.1% on a quarter-on-quarter seasonally adjusted annualised basis in Q3 2015, following the 2.5% contraction in Q2. The manufacturing sector continued to decline, reflecting persistent weakness in the electronics, precision engineering, and transport engineering clusters. Growth in financial services was weaker amid the slowdown in lending to the region. In comparison, segments of the wholesale trade and transportation sectors were boosted by an upturn in oil-related activities in early Q3. The domestic-oriented sectors saw further steady growth during the quarter, partly supported by increases in public residential construction.

5. The overall outlook for the global economy has softened compared to the review in April. While the US economy is likely to expand at a stronger pace on robust private consumption, its import demand has been weak. In the Eurozone and Japan, the pickup in economic activity is envisaged to be gradual. China's growth momentum is easing on a sharp deceleration in investment growth. Taken together, these factors will weigh on the region's commodity producers and trade-dependent economies. As a consequence, the growth outlook for Asia ex-Japan as a whole has dimmed.

6. The subdued global growth will exert a drag on the external-oriented sectors in Singapore in the quarters ahead. Within manufacturing, the transport engineering cluster will continue to be hampered by a cutback in oil exploration activities. The weakness in IT production and its supporting industries will also persist due to sluggish final demand and ongoing reconfigurations in the electronics cluster. In comparison, the domestic-oriented sectors should expand at a moderate pace, underpinned by sustained demand for healthcare and education services, as well as public infrastructure spending. GDP growth in Singapore is likely to come in at around 2–2.5% in 2015 as a whole, with risks tilted towards the downside. The economy is expected to expand at a broadly similar pace next year, with cyclical headwinds likely to persist into early 2016.

Inflation

7. MAS Core Inflation, which excludes the costs of private road transport and accommodation, remained subdued at 0.3% y-o-y in July–August 2015, following the 0.2% registered in Q2. Compared to a year ago, imported fuel prices continued to fall in Q2 and July–August, which filtered through to the domestic prices of oil-related items. Services inflation was dampened by enhanced medical subsidies and other Budget measures, SG50-related promotions as well as the modest pass-through of costs to consumer prices. Reflecting these factors, and further declines in imputed rentals on owner-occupied accommodation and car prices, CPI-All Items inflation fell to −0.6% y-o-y in July–August 2015 from −0.4% in Q2.

8. External sources of inflation are likely to stay generally benign, given ample supply buffers in the major commodity markets and weak global demand conditions. Oil prices are projected to remain low and increase only slightly in 2016. On the domestic front, some wage cost pressures remain, but their pass-through to consumer prices will continue to be constrained by the subdued growth environment. Meanwhile, the disinflationary effects of lower global oil prices, Budget measures and SG50 price promotions will begin to fade from the end of this year. As a result, MAS Core Inflation is forecast to rise gradually over the course of 2016 towards its historical average of close to 2%. For the year as a whole, MAS Core Inflation is projected to average 0.5–1.5% in 2016, compared to around 0.5% in 2015.

9. Car prices and imputed rentals on owner-occupied accommodation will dampen overall inflation amid the expected increase in the supply of COEs and newly-completed housing units. CPI-All Items inflation is forecast to come in at around −0.5% in 2015, and −0.5–0.5% in 2016.

MONETARY POLICY

10. The Singapore economy is projected to expand at a modest pace in 2015 and 2016, with growth slightly weaker than earlier envisaged. MAS Core Inflation is expected to pick up gradually over the course of 2016 towards its historical average.

11. MAS will therefore continue with the policy of a modest and gradual appreciation of the S$NEER policy band. However, the rate of appreciation will be reduced slightly. There will be no change to the width of the policy band and the level at which it is centred. This measured adjustment follows the move to reduce the rate of appreciation of the policy band in January this year, and is supportive of economic growth into 2016, while ensuring price stability over the medium term.