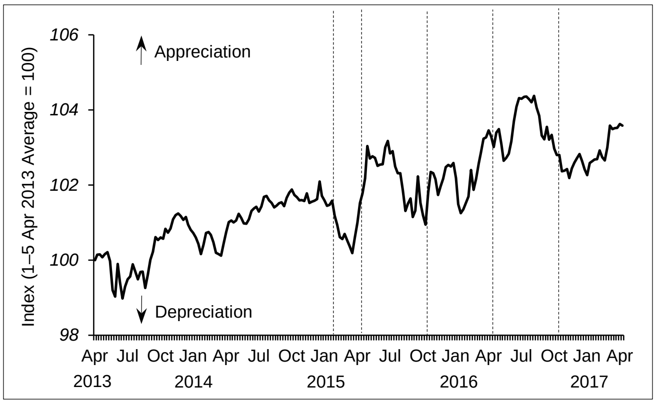
13 April 2017

Monetary Policy Statement

INTRODUCTION

1. In the October 2016 Monetary Policy Statement (MPS), MAS kept the slope of the Singapore dollar nominal effective exchange rate (S$NEER) policy band at zero percent, with no change to the width of the policy band or the level at which it was centred. This policy stance was assessed to be appropriate given the subdued outlook for growth and inflation.

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



indicates release of Monetary Policy Statement

2. Following the October 2016 MPS, the S$NEER has fluctuated around a strengthening trend, appreciating from below the mid-point of the policy band to the upper half of the band. The appreciation from late February 2017 reflected, in part, broad-based US dollar weakness. Meanwhile, the three-month S$ SIBOR rose from 0.87% as at end-October 2016 to 0.95% by end-March 2017.

OUTLOOK

3. Over the last six months, the global economy has picked up and should continue to support Singapore's trade-related sectors. However, activity across the broader domestic economy is likely to be uneven, and overall GDP growth in 2017 will remain modest. MAS Core Inflation will rise from 0.9% in 2016 to average 1–2% in 2017 due to increases in global oil prices, as well as the temporary effects of administrative price hikes. Over the medium term, core inflation is expected to trend towards but average slightly below 2%.

Growth

4. According to the *Advance Estimates* released by the Ministry of Trade and Industry today, the Singapore economy contracted by 1.9% on a quarter-on-quarter seasonally-adjusted annualised basis in Q1 2017, following the 12.3% expansion in Q4 2016 when there was a temporary step-up in a number of externally-oriented industries, such as the biomedical cluster. Despite the pullback in the first quarter, the underlying momentum in the economy remains intact, with output of electronics and its related services segments still at healthy levels. On a year-ago basis, overall GDP grew by 2.5% in Q1 2017.

5. The outlook for the global economy has improved slightly since the October 2016 MPS, although downside risks remain, alongside significant policy uncertainty. Global capital expenditure has begun to turn up amid some strengthening in business sentiment, while improving labour market conditions should sustain final demand in the developed economies. The outlook for China has stabilised on the back of firming corporate profitability and accommodative fiscal policy.

6. Against this external backdrop, activity in Singapore's trade-related sectors should support overall GDP growth in 2017. The turnaround in the global IT cycle will continue to benefit the domestic semiconductor and precision engineering industries. However, the performance in the rest of the manufacturing sector will remain patchy. The modern services cluster is expected to expand at a slightly faster pace in 2017, led by a pickup in the financial sector and firm demand for ICT services. While healthcare and education services will be underpinned by resilient demand, spending on discretionary retail items and other services is expected to be dampened by the still-subdued labour market and weak consumer sentiment. Overall, the economy should expand by 1–3% in 2017, not markedly different from the growth of 2% in 2016.

Inflation

7. MAS Core Inflation, which excludes the costs of private road transport and accommodation, edged up to average 1.3% year-on-year in January–February 2017, from 1.2% in Q4 2016. After turning positive in late 2016, CPI-All Items inflation came in at 0.6% in the first two months of this year, compared to an average of 0.0% in Q4 last year. The increase in both core and headline inflation was largely due to higher prices of oil-related items, such as electricity and petrol, as global oil prices have risen from their 2016 trough.

8. In 2017, energy-related components will be the main drivers of the projected pickup in inflation. While global oil prices would be capped by elevated inventories as well as rising US crude oil production, average prices for the year will still be higher than in 2016. A number of administrative price adjustments[1] this year will also contribute to a temporary increase in CPI inflation.

9. Other domestic sources of inflation remain relatively muted, as conditions in the labour market have slackened since the last policy review. This will dampen underlying wage pressures, even as commercial and retail rents have eased further. The lacklustre economic environment will also limit the extent to which businesses pass on higher import and administrative costs to consumers. Meanwhile,

[1] These include the upward revisions in car park charges and household refuse collection fees which took effect from December 2016 and January 2017 respectively, as well as upcoming increases in water prices and service & conservancy charges (S&CC). U-Save rebates, which have also been increased and will partially offset the impact of higher water prices for eligible households, are not taken into account in the CPI.

housing rents are likely to continue declining this year, given the elevated vacancy rate in the residential property market.

10. MAS' inflation forecasts for 2017 remain unchanged from the October 2016 MPS. MAS Core Inflation is projected to average 1–2%, compared to 0.9% in 2016, while CPI-All Items inflation is expected to rise to 0.5–1.5% from −0.5% last year.

MONETARY POLICY

11. The Singapore economy will continue to expand at a modest pace in 2017. MAS Core Inflation is envisaged to rise gradually, largely on account of higher global oil prices. However, demand-driven inflationary pressures will likely be restrained. Over the medium term, core inflation is expected to trend towards but average slightly below 2%.

12. MAS will therefore maintain the rate of appreciation of the S$NEER policy band at zero percent. The width of the policy band and the level at which it is centred will be unchanged. As indicated in the October 2016 MPS, a neutral policy stance is appropriate for an extended period and should ensure medium-term price stability.