



Media Release

Singaporean's Inflation Expectations rise to two-year high of 3.38% amid uncertain but cautiously optimistic outlook

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Singapore, 24 April 2017 (Monday) – Singaporeans' One-year-Ahead median inflation expectations rose sharply to 3.38% in March 2017, its highest level since December 2014, according to the research findings of the latest quarterly survey for Singapore Index of Inflation Expectations (SIInDEX) by the Sim Kee Boon Institute for Financial Economics (SKBI) at Singapore Management University (SMU).

The process of normalisation of the accommodative monetary policy is well underway at the US Federal Reserve Board with the increase in the benchmark interest rate announced after the Federal Open Market Committee (FOMC) meeting in March 2017. This move towards increasing the interest rates happened against the backdrop of historic highs of stock markets around the world. However, concurrently other major economies in the world are still in an expansionary mode with stimulus spending. Though there is clear evidence of nascent growth in the US since the new Trump administration took office with an euphoria surrounding possible fiscal stimulus through promised tax cuts, there is however significant policy uncertainty and waves of populism the world over.

In its World Economic Outlook released in April 2017, economists at the International Monetary Fund (IMF) highlighted that the world economy is expected to grow at a healthier 3.5% in 2017 compared to 3.1% in 2016, mainly due to long awaited cyclical recovery in manufacturing, commodities and globally reduced deflationary risk. The challenges, cautioned the IMF and World Bank economists, are more structural, such as low productivity growth, income inequality and possibly high youth unemployment that might lead to inward looking policies in advanced economies. This in turn might impede trade and globalisation. However, the expected growth spurt in the US as well as higher interest rates, improving oil prices and commodities might signal possible higher exchange rate for US dollar against the Singapore dollar; these, together with higher inflation in the G3-economies (US, Eurozone and Japan) and the region, might translate to higher imported inflation for Singapore.

On the domestic front, there are quite a few areas that consumers might have focused on to form their opinion of expected inflation in the medium and long term, although demand driven price pressure is likely to be more subdued. First, although the labour market is less tight than a year before and unemployment is marginally higher, there is

an expected increase in wages that might pass through to higher overall price levels. Second, the private road transportations also seemed to have turned a corner with higher petrol prices and car parking fees. Finally, the proposed increase in water prices might have also fed into the expected inflation.

The SInDEx was co-developed by Assistant Professor Aurobindo Ghosh of the SMU Lee Kong Chian School of Business with funding from the SMU Sim Kee Boon Institute for Financial Economics. The SInDEx survey, supported and implemented by Agility Research & Strategy, a leading Asian consumer insights and strategy firm with a large client base of Government and Private sector clients, is derived from an online survey of around 500 randomly selected individuals representing a cross section of Singapore households. The online survey helps researchers understand the behaviour and sentiments of decision makers in Singapore households. The quarterly SInDEx survey has yielded two composite indices, median SInDEx1 and median SInDEx5. Medians are less affected by outliers in survey-based methods, hence median SInDEx is used for the current release.

In the latest and twenty-third wave of the SInDEx survey conducted in March 2017, consumers shared their views on expectations of inflation-related variables over the medium term (One-year-Ahead) to long term (Five-year-Ahead).

The results of the March 2017 survey showed that the median One-year-Ahead headline inflation (or CPI-All Item inflation) increased to 3.38% from 2.7% recorded in December 2016. As a comparison benchmark, the *mean* One-year-Ahead headline inflation rate, also moved up to 3.86% in the March 2017 survey compared to 2.95% in its December 2016 survey, breaking its sub 3% value for the first time since December 2015.

Compared to the historical median headline inflation expectations (since September 2011) average of 3.49%, current One-year-Ahead median headline inflation is still lower but it is higher than the recent first quarter average of 3.09%.

Structural challenges to global growth exacerbated by the political and policy uncertainty particularly surrounding global trade in the US and Eurozone might have prompted representative Singaporean households surveyed to believe that One-year-ahead expected overall price changes might be heading up.

In line with the overall headline inflation, the One-year-Ahead median Singapore core inflation expectations (excluding accommodation and private road transportation related costs) saw an increase to 3.37% in March 2017 from 2.82% in December 2016. For a subgroup of the population who own their accommodation and use public transport, the One-year-Ahead median Singapore core inflation rate for the subgroup increased to 3.57% in March 2017 compared to 2.65% polled in December 2016. This subgroup's expectations of inflation closely tracks the Singapore Core Inflation Expectations, as they are not exposed to private transport or private accommodation expenses. These results indicate that there has been a substantial increase in the perception of future price changes in the Singapore core inflation rate which excludes housing and private road transportation. This might be attributed to both domestic and global price pressures and expected increase in oil and commodity prices.

The One-year-Ahead median Singapore Index of Inflation Expectations (Median SInDEx1), a composite weighted index of One-year-Ahead median inflation

expectations, moved up to 3.38% in March 2017 from 2.73% in December 2016 survey. Despite the increase, median SInDEx1 remained marginally lower than its historical average value of 3.5% since its inception in September 2011. SInDEx1 is constructed as an alternative and more stable measure of inflation expectations by putting lower weightage on the more volatile and policy-sensitive components like accommodation, private transportation, food and energy. Median SInDEx1 is less adversely affected by outliers, unlike the original mean SInDEx1.

SMU Assistant Professor of Finance Aurobindo Ghosh, who is the Principal Investigator of the SInDEx Project highlighted, "The level of geopolitical uncertainty arising from inward looking populist and protectionist policies and its impact on the current global capital market is simply phenomenal. Nevertheless, the global economy is projected to grow at a more respectable rate according to the recently released World Economic Outlook in April 2017 against the backdrop of near record highs in global stock markets. The biggest challenge lies with the policymakers having to stay relevant and connected to popular perceptions. Recovery in global market conditions, expected increase in the value of the US dollar compared to global currencies and a neutral stance in the policy and guidance from Monetary Authority of Singapore might have signaled higher inflation in small open economies like Singapore."

For the longer horizon, the Five-year-Ahead median headline (CPI-All Items) inflation expectations in the March 2017 survey also jumped to 4.09% (from 3.50% in December 2016), its highest value since September 2014 although it was still less than its historical average of 4.34%. For the purpose of comparison, survey finding shows that the mean Five-year-Ahead headline inflation recorded 4.6% in the March 2017 survey moved upwards from 3.9% recorded in December 2016 survey.

The Five-year-Ahead median Singapore core inflation rate (excluding accommodation and private road transportation related costs) inched up to 3.74% in March 2017 from 3.36% in December 2016. In summary, the composite Five-year-Ahead median Singapore Index of Inflation Expectations (median SInDEx5) in March 2017 also inched up to 3.89% from 3.4% in December 2016, although this is still lower than its historical median of 4.16%.

"The sharp increase in the expected level in the headline inflation rate might be due to several factors, both international and domestic, such as an uptick in global growth, trade or pass through costs arising from an increase in domestic salaries or transport costs. We do have to highlight that the current rate expressed in survey based measure is still higher than the one that is expected one year back and current rates tracked by Singapore's Ministry of Trade and Industry and Monetary Authority of Singapore. Unlike inflation measures that are based on a fixed basket of goods and services, market sentiments and standard behavioural biases like frequency bias prompts people to overweight daily necessities like food and staples compared to bigger ticket but less frequently purchased items like cars or houses. This tends to give an upward bias to the survey measures if the price increases in frequently purchased items are higher. In our ongoing research, we are trying to identify and reduce the impact of such biases and align it better with observed outcomes in the economy. Having said that, survey based instruments have known to be more effective in identifying changes in directions rather than the actual levels." Prof Ghosh added.

Methodology

Two indices were created, median SInDEx1 and median SInDEx5, to measure the 1-year inflation expectations and the 5-year inflation expectations. The data for the SInDEx survey was collected online from about 500 consumers. The sampling was done using a quota sample over gender, age and residency status to ensure representativeness of the sample. Employees in some sectors like journalism and marketing were excluded as that might have an effect on their responses to questions on consumption behavior and expectations.

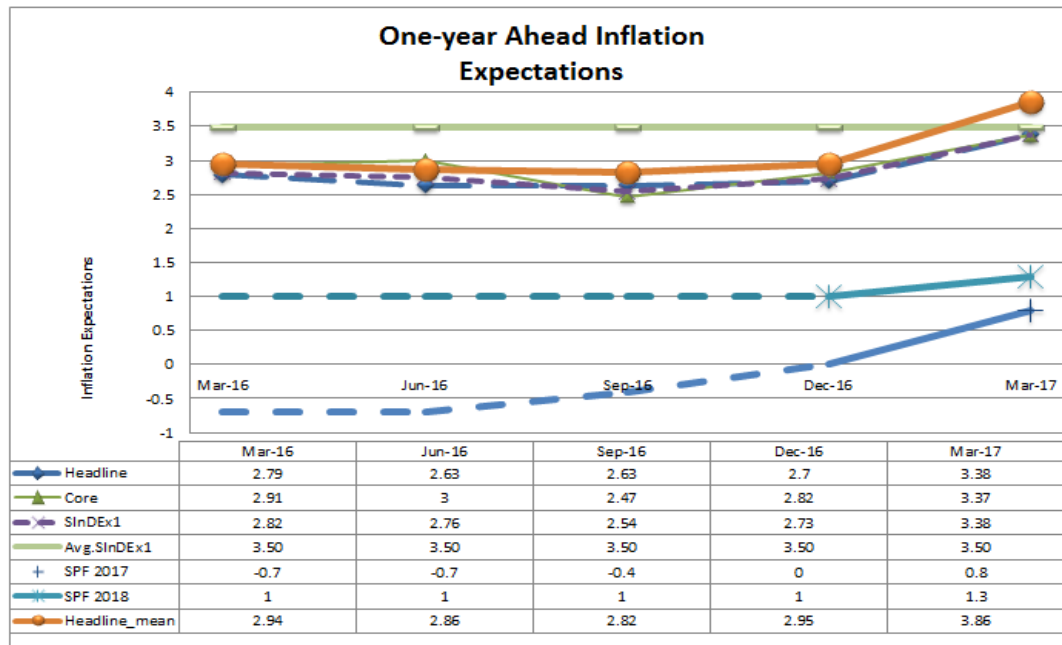


Figure 1: One-year-Ahead-inflation expectations in Singapore

Five-year Ahead Inflation Expectations

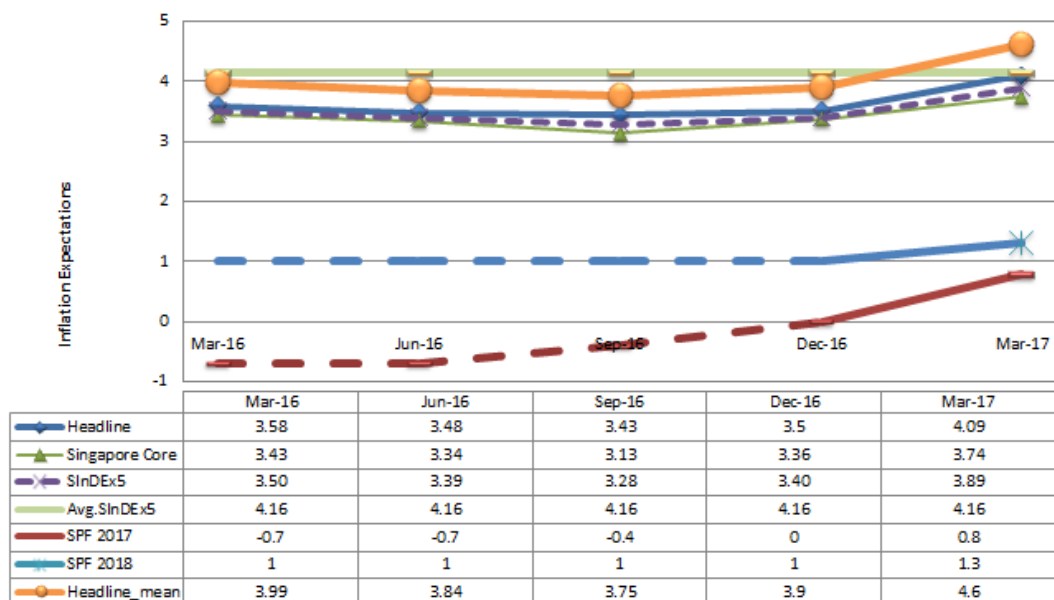


Figure 2: Five-year-Ahead-Inflation Expectations of Singapore

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About Singapore Management University

A premier university in Asia, the Singapore Management University (SMU) is internationally recognised for its world-class research and distinguished teaching. Established in 2000, SMU’s mission is to generate leading-edge research with global impact and produce broad-based, creative and entrepreneurial leaders for the knowledge-based economy. SMU education is known for its highly interactive, collaborative and project-based approach to learning, and for its technologically enabled pedagogy of seminar-style teaching in small class sizes.

Home to around 10,000 undergraduate, postgraduate, executive and professional, full- and part-time students, SMU is comprised of six schools: School of Accountancy, Lee Kong Chian School of Business, School of Economics, School of Information Systems, School of Law, and School of Social Sciences. SMU offers a wide range of bachelors', masters' and PhD degree programmes in the disciplinary areas associated with the six schools, as well as in interdisciplinary combinations of these areas.

SMU has an emphasis on generating rigorous, high-impact, and relevant multi-disciplinary research that addresses Asian issues of global relevance. SMU faculty members collaborate with leading international researchers and universities from USA, Europe, China and India, as well as with partners in the business community and public

sector, through its research institutes, centres and labs. SMU's city campus is a state-of-the-art facility located in the heart of downtown Singapore, fostering strategic linkages with business, government and the wider community. www.smu.edu.sg

About Sim Kee Boon Institute for Financial Economics

The Sim Kee Boon Institute for Financial Economics (SKBI) is the premier Asian institute for research and training in financial economics. It is the think-tank in SMU that spearheads and excels in cutting-edge research in finance and financial markets which is of strategic and practical relevance to the Singapore and regional economies.

Supported by our faculty and in collaboration and partnership with industry experts, relevant government bodies and other world-renowned research agencies, the Institute conducts fundamental and applied research which is driven by industry and societal needs in Singapore and the region. Besides research, SKBI also actively engages in training and consultancy, executive education and research dissemination through organising courses, seminars and conferences. Our purpose-oriented activities are designed to serve as enablers in bridging the gap between theory and practice and to act as accelerators in helping to shape financial policies and regulations, which are especially important given the uncertainty in the global markets.

<http://skbi.smu.edu.sg/>

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We partner with leading brands to provide actionable insights through a suite of data, research and intelligence solutions to boost their market share and help them succeed in a hypercompetitive marketplace.

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