DEVELOPMENTS IN THE FIRST QUARTER OF 2015

INTERNATIONAL ECONOMIC ENVIRONMENT

Moderate global economic expansion

The global economic activity expanded with divergent growth momentum across economies in the first quarter of 2015. While the US economy registered broader improvements, the economic recovery in the euro area and Japan progressed at a more gradual pace. In Asia, growth was sustained by the continued expansion of domestic demand.

Most major and regional equity markets ended the quarter higher. In the first half of the quarter, global equity markets initially declined as market sentiments were affected by the sharp decline in oil prices, the downward revision to the IMF and World Bank global growth forecasts, as well as uncertainty over the outcome of the Greek debt negotiations. Nevertheless, most equity markets trended higher from February onwards, which more than offset the initial decline. This was underpinned by policy actions in a few major economies, namely, the commencement of the European Central Bank's (ECB) expanded asset purchase programme and the announcement of monetary easing measures by the People's Bank of China (PBOC), which lifted market sentiments.

The US economy expanded at a faster annual pace of 3.0% in the first quarter (4Q 2014: 2.4%). On a seasonally adjusted annualised basis however, growth moderated to 0.2% (4Q 2014: 2.2%). Private consumption activity improved in the first quarter, benefitting from lower oil prices, stronger labour market conditions and improved household balance sheets. Nevertheless, growth in the first quarter was affected by temporary factors including harsh winter conditions and port congestion. Growth of fixed investment moderated as the slower expansion in non-residential capital expenditure more than offset the faster growth in residential investment. Headline inflation turned negative (-0.1%; 4Q 2014: 1.2%), amid lower oil prices.

Economic activity in the euro area registered a gradual improvement in the first quarter of 2015 (1.0%; 4Q 2014: 0.9%). Overall demand conditions were supported by lower oil prices, accommodative monetary policy and continued depreciation of the euro. Business and consumer sentiments also improved, with the manufacturing PMI increasing to 51.4 during the quarter (4Q 2014: 50.4). The economy, however, entered into deflation (-0.3%; 4Q 2014: 0.2%) due mainly to lower oil prices.

The UK economy continued to expand in the first quarter, albeit at a more moderate pace of 2.4% (4Q 2014: 3.0%). Growth was mainly driven by the services sector, particularly the transportation, storage and communication sub-sector. Inflation rate fell to 0.1% during the quarter (4Q 2014: 0.9%), amid lower food and transportation prices.

Economic activity in Japan remained weak. Retail sales registered a broad-based decline in the first quarter (-4.8%; 4Q 2014: 0.6%) amid lower household consumption. Business sentiments, however, were sustained as reflected by the Tankan survey index for large manufacturers which was unchanged during the quarter. On the external front, exports growth was sustained at 9.1% in the first quarter (4Q 2014: 9.1%) amid continued depreciation of the yen. Inflation (less fresh food) continued to moderate (2.1%; 4Q 2014: 2.7%) on account of lower cost of utilities, furniture, transportation and communication, and recreation. Core inflation (excluding food and energy) was sustained at 2.1% (4Q 2014: 2.1%).

Advanced Economies: Real GDP Growth

	2014			2015
	1Q	4Q	Year	1Q
	Annual change (%)			
US	1.9	2.4	2.4	3.0[a]
UK	2.7	3.0	2.8	2.4[p]
Euro area	1.1	0.9	0.9	1.0[p]

[a] Advance estimate
[p] Preliminary

Source: National authorities

Most central banks in the advanced economies continued to maintain an accommodative monetary policy stance, despite diverging trend in the monetary policy direction across economies. In the US, the Federal Reserve assessed that *"an increase in the federal funds rate target is likely to become appropriate later this year"*[1] amid the reduction in labour market slack. Following the decline in oil prices in January, the Fed lowered its inflation projection for 2015 to 0.6% - 0.8% in March 2015 (December 2014 forecast: 1.0% - 1.6%). In contrast, several central banks increased monetary accommodation amid lower inflation and rising growth concerns. In January 2015, the ECB began its asset purchase programme of EUR60 billion (approximately USD70.9 billion) per month between March 2015 until at least September 2016, to include the purchase of bonds issued by euro area governments, agencies and European institutions. Similarly, the Bank of Japan continued with its annual asset purchases of JPY80 trillion (approximately USD670 billion) amid continued disinflation concerns. Meanwhile, the Swiss National Bank (SNB) and the Bank of Canada reduced their key policy rates by 50 and 25 basis points, respectively to -0.75% and 0.75%, respectively. On 15 January, the SNB also discontinued the minimum exchange rate of CHF1.20 per euro amid more pronounced divergences between monetary policies in the US and euro area. In February and May, the Reserve Bank of Australia lowered its key interest rate by 25 basis points each to 2.0%, while Danmarks Nationalbank (Danish National Bank) cut its policy rate on four occasions by a cumulative 70 basis points to -0.75% in the first two months of the year. Sveriges Riksbank (Swedish National Bank), on the other hand, reduced its policy rate by a cumulative 25 basis points to -0.25% in February and March.

In PR China, economic growth moderated to 7.0% in the first quarter (4Q 2014: 7.3%). By industry, sustained growth in the tertiary sector (services) was offset by slower expansion in the primary (agriculture) and secondary industries (industry and construction). In March 2015, the Chinese government also announced a lower official growth target of *"around 7.0%"*[2] for 2015. To this end, policymakers continued to provide support to economic activity during the quarter through the acceleration of infrastructure projects, monetary stimulus measures and the easing of property market restrictions. Inflation moderated to 1.2% (4Q 2014: 1.5%) amid lower transportation and housing costs.

In Asia, growth continued to expand, albeit at a more moderate pace in most economies. The Chinese Taipei economy continued to expand in the first quarter (3.5%; 4Q 2014: 3.3%), supported by an improvement in private consumption and sustained export growth. Singapore registered sustained growth in the first quarter (2.1%; 4Q 2014: 2.1%), supported by continued expansion in the construction and services industries. In Korea, growth moderated slightly to 2.4% (4Q 2014: 2.7%) as the improvement in private consumption and investment was offset by weaker external demand. Economic activity grew at a slower pace of 4.7% (4Q 2014: 5.0%) in Indonesia as weaker growth in private consumption and government spending outweighed the improvements in investment and net exports.

Regional Countries: Real GDP Growth

	2014			2015
	1Q	4Q	Year	1Q
	Annual change (%)			
PR China	7.4	7.3	7.4	7.0
Indonesia	5.1	5.0	5.0	4.7
Singapore	4.6	2.1^{r}	2.9^{r}	2.1^{a}
Korea	3.9	2.7	3.3	2.4^{a}
Chinese Taipei	3.4	3.3^{r}	3.7^{r}	3.5^{a}

^{a} Advance estimate
^{r} Revised

Source: National authorities

Headline inflation moderated in most Asian economies, with Thailand, Singapore and Chinese Taipei falling into deflation. The moderation primarily reflected the decline in oil prices and its pass-through to lower food, utilities and transportation costs. In contrast, inflation in Indonesia was sustained due to the increase in fuel pump prices after the implementation of subsidy reforms.

[1] "The New Normal Monetary Policy" speech by Janet Yellen at the Research Conference on 27 March 2015
[2] "Report on PR China's Economic, Social Development Plan (2015)" The National People's Congress of PR China official website

Most regional central banks increased the degree of monetary accommodation in the first quarter. Of significance, the Monetary Authority of Singapore reduced the slope of the S$ nominal effective exchange rate policy band in January due to expectations of lower imported inflation following the significant fall in oil prices. Similarly, in response to persistent deflationary pressures and growth concerns, the Bank of Thailand and the Bank of Korea also reduced their respective policy rates from 2% respectively to 1.5% and 1.75%, respectively. Bank Indonesia also lowered its policy rate by 25 basis points to 7.5% as the central bank expected inflation to fall towards the lower end of its 3-5% 2015 year-end target. In India, the central bank lowered the repo rate in January and March by a total of 50 basis points to 7.5%, given expectations of lower inflation. In PR China, the PBOC eased monetary conditions to help lower the funding costs for financial institutions, reduce market interest rates and thereby the financing costs of the corporate sector. Between January to May 2015, PR China's one-year benchmark deposit and loan interest rates were lowered to 2.25% and 5.1%, respectively (Previous: 2.75% and 5.6%, respectively). In addition, the reserve requirement ratio for financial institutions was reduced by a total of 150 basis points in February and April to support lending to small and micro enterprises, the agriculture sector and rural areas.

Brent crude oil prices declined by approximately 29% to average USD55 per barrel in the first quarter (4Q 2014: USD77 per barrel). The decline was driven by high global supply of oil, and to a lesser extent, slower demand in a few major economies. Amid rising oil inventory in major consuming countries, prices declined to a low of USD47 per barrel on 12 January, levels last seen during the Global Financial Crisis. Prices subsequently stabilised towards the end of the quarter to around USD55 per barrel following the decline in US oil rig operations, which pointed to a reduction in US shale oil output in the medium-term.

Most major and regional currencies ended the quarter lower against the US dollar. The broad-based depreciation against the US dollar was attributed mainly to the continued improvements in US economic activity, which supported market expectations for monetary policy normalisation to begin in the second half of 2015. The euro and Japanese yen also depreciated following the implementation of additional monetary stimulus by their respective central banks. In contrast, the Thai baht ended the quarter higher against the US dollar due to lower political uncertainty and the improvement in the country's external position. The Taiwanese dollar also strengthened amid investor optimism that the fall in oil prices will support the economy's growth prospects.

Moving forward, the global economy is projected to be on a moderate growth path, but with diverging growth momentum across major economies. While lower oil prices will have varying impact on economies, overall global growth is expected to benefit from this development. Nevertheless, downside risks to the growth outlook continue to persist, arising from the prolonged weakness in domestic demand and the low inflation in a number of major economies, concerns on the growth prospects of several net commodity-exporting emerging economies and the re-emergence of geopolitical tensions, which could result in heightened financial market volatility.