DEVELOPMENTS IN THE FOURTH QUARTER OF 2015

INTERNATIONAL ECONOMIC ENVIRONMENT

Moderate global growth

Global economic activity continued to expand at a moderate pace in the fourth quarter of 2015. The advanced economies registered modest improvements, but with the pace of growth remaining constrained by crisis-related legacies, including high indebtedness and labour market weaknesses. In Asia, economic activity continued to be supported by domestic demand amid weak export performance. Monetary policy stances experienced a more pronounced divergence given the differing country-specific domestic challenges.

Global financial markets remained volatile in the fourth quarter. Investors' sentiments were boosted in the beginning of the quarter following expectations of continued easy monetary policy in the advanced economies and the announcement of additional monetary policy easing by several Asian central banks, including the People's Bank of China (PBOC). However, heightened volatility re-surfaced in December. While the US Federal Reserve's decision to raise interest rates removed some uncertainty from the financial markets, investors' sentiments were more affected by concerns over global growth prospects in some of the major emerging economies. This was further compounded by persistent high uncertainty surrounding renewed downward pressure in global energy prices. Given these developments, most major and regional currencies depreciated against the US dollar towards the end of the year.

In the energy market, Brent crude oil prices declined sharply to an average of USD45 per barrel in the fourth quarter (3Q 2015: USD51 per barrel). This was mainly due to the protracted oversupply in the oil market following a large build-up in OECD oil inventory and OPEC's continued high production rate. In December 2015, prices declined further due to OPEC's decision during the month not to cut its high level of production, as well as the increase in Fed funds rate on 16 December, which triggered a new round of liquidation of positions in the oil market. As a result, Brent oil prices hit an 11-year low of USD36 per barrel on 22 December and ended the quarter at USD37 per barrel.

Growth in the US economy moderated to 1.8% in the fourth quarter (3Q 2015: 2.1%), due mainly to a slower expansion of private consumption and investment activity. Nevertheless, consumer spending remained the key contributor to growth, supported by continued favourable labour market conditions. Meanwhile, growth in fixed investment moderated, as a slowdown in industrial and commodity-related capital spending offset the improvement in residential investment. On a seasonally adjusted annualised basis, the overall growth momentum slowed to 0.7% (3Q 2015: 2.0%). Headline inflation rose to 0.5% (3Q 2015: 0.1%), due mainly to the increase in prices of shelter and medical care services.

The euro area economy grew at an annual pace of 1.5% (3Q 2015: 1.6%). On a quarterly basis, the growth momentum was sustained at 0.3%, supported by a continued expansion of economic activity in the core economies, in particular Germany and Spain. Domestic demand in the region was supported by a gradual improvement in the labour market and accommodative monetary conditions. Headline inflation was sustained at a low rate of 0.1% during the quarter, while core inflation increased slightly (1.0%, 3Q 2015: 0.9%).

Economic activity in the UK expanded at a more moderate pace in the fourth quarter (1.9%; 3Q 2015: 2.1%). The services sectors remained the key contributor to growth, particularly the business services and finance sub-sector. Headline inflation remained flat (3Q 2015: 0%), as the growth in the prices of clothing and footwear was offset by the decline in the cost of food.

Growth in the Japanese economy moderated to 0.5% (3Q 2015: 1.7%). On a seasonally adjusted annualised basis, economic activity contracted by 1.4% (3Q 2015: +1.3%). Growth was mainly affected by a significant decline in

private consumption, amid weak wage growth. On the external front, exports contracted, due mainly to slowing demand from most of its key trading partners. Headline inflation (excluding fresh food) registered a marginal positive growth of 0.1% (3Q 2015: -0.1%), while core inflation (excluding food and energy) was sustained at 0.8%.

Advanced Economies: Real GDP Growth

	2014		2015		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
US	2.5	2.4	2.1	1.8[a]	2.4[a]
Euro area	1.0	0.9	1.6	1.5[p]	1.5[p]
UK	2.8	2.9	2.1	1.9[p]	2.2[p]
Japan	-1.0	0.0	1.7[r]	0.5[p]	0.4[p]

[a] Advance estimate
[p] Preliminary estimate
[r] Revised

Source: National authorities

During the quarter, monetary policy in the advanced countries remained accommodative, albeit with diverging trends across economies. In the US, the Federal Open Market Committee (FOMC) decided to increase the target range for the federal funds rate (FFR) for the first time since 2006 by 25 basis points to 0.25-0.5%. The decision was premised upon solid growth in household spending and business fixed investment, as well as notable improvements in the labour market throughout the year. The FOMC, however, highlighted that the timing and pace of future adjustments in the FFR will be gradual and data dependent while remaining below levels that are expected to prevail in the longer run. In contrast, the European Central Bank (ECB) lowered the interest rate on the deposit facility by 10 basis points to -0.3%, and extended its asset purchase programme of EUR60 billion monthly purchases for at least an additional six months until the end of March 2017. Similarly, the Reserve Bank of New Zealand (RBNZ) lowered its benchmark official cash rate by 25 basis points to 2.50% amid rising growth concerns and lower inflation. Across other advanced economies, central banks in Australia, Canada, Denmark, Norway and Sweden reiterated their commitment to maintain accommodative monetary conditions by keeping policy rates unchanged during the quarter.

Growth in PR China moderated slightly the fourth quarter (6.8%; 3Q 2015: 6.9%). While growth in the services sector moderated (8.2%, 3Q 2015: 8.6%), it continued to outperform the secondary industry (industry and construction) (6.1%, 3Q 2015: 5.8%). During the quarter, the Chinese government implemented a series of wide-ranging policy measures to support domestic demand. These included lower taxes on car purchases, higher infrastructure investment and increased lending to targeted sectors. Further monetary policy easing measures were also introduced following the sharp correction in the stock markets. Nevertheless, growth continued to face headwinds arising from excess capacity in heavy industries and the property market and the weaker sentiments after the correction in the Chinese equity markets. Meanwhile, inflation moderated to 1.5% (3Q 2015: 1.7%) due to lower prices in the food and housing sub-sectors.

In Asia, several economies registered moderate improvements. In Singapore, growth improved to 2.0% (3Q 2015: 1.8%), underpinned by an improvement in construction activity in the public sector. Similarly, growth of the Korean economy also picked up in the fourth quarter to 3.0% (3Q 2015: 2.7%), driven mainly by an improvement in private consumption amid sustained investment activity and stronger export performance. The Indonesian economy registered higher growth of 5% (3Q 2015: 4.7%), reflecting mainly an increase in investment, particularly in infrastructure, amid sustained private consumption but weaker exports. Likewise, growth in the Philippines improved (6.3%; 3Q 2015: 6.1%), driven by stronger private consumption and investment. In Thailand, despite a contraction in exports, economic activity expanded at a pace of 2.8% (3Q 2015: 2.9%), supported by a broad-based improvement in domestic demand. Meanwhile, in Chinese Taipei, economic activity remained in contraction, but at a slower pace of 0.3% (3Q 2015: -0.6%). The improvement in private consumption during the quarter was offset by a contraction in investment activity and exports.

Regional Countries: Real GDP Growth

	2014		2015		
	4Q	Year	3Q	4Q	Year
	Annual change (%)				
PR China	7.2	7.3	6.9	6.8	6.9
Philippines	6.6	6.1	6.1	6.3	5.8
Indonesia	5.0	5.0	4.7	5.0	4.8
Thailand	2.1	0.8	2.9	2.8	2.8
Korea	2.7	3.3	2.7	3.0[a]	2.6[a]
Singapore	2.1	2.9	1.8[r]	2.0[a]	2.1[a]
Chinese Taipei	3.6	3.9	-0.6	-0.3[a]	0.9[a]

[a] Advance estimate
[r] Revised

Source: National authorities

Headline inflation in most regional economies picked up modestly in the fourth quarter with the waning impact of the late-2014 decline in energy prices. The Chinese Taipei economy exited deflation while prices contracted at a slower pace in Thailand. However, inflation moderated in Indonesia as the impact of subsidy rationalisation on fuel prices dissipated.

In this environment, monetary policy remained accommodative across the region, with a few central banks lowering their key policy rates during the quarter. In October, the Monetary Authority of Singapore (MAS) reduced slightly the rate of appreciation of the Singapore dollar nominal effective exchange rate (S$NEER) policy band following a weaker-than-expected growth outlook. The People's Bank of China (PBOC) lowered its key policy rate by 25 basis points to 4.35% and reduced the reserve requirement ratio (RRR) for large financial institutions by 50 basis points to 17.5%. Banks lending to SMEs and the agricultural sector also received an additional 50 basis points reduction to their respective RRR. Additionally, the PBOC removed the ceiling on deposit rates, improving market-oriented interest rate setting. In December 2015, the Central Bank of the Republic of China (Taiwan) lowered its key policy rate by 12.5 basis points amid moderate global and domestic growth outlook. In the same month, Bank Indonesia (BI) reduced its RRR by 50 basis points to 7.50%. In January 2016, BI lowered its key policy rate by 25 basis points to 7.25%.

Downside risks to the global outlook remain elevated. This is reflected in the re-emergence of heightened volatility in the financial markets in the early weeks of 2016, following concerns over the growth prospects of the major economies, the fall in energy prices and global policy shifts. Going forward, although the global economy is projected to expand further, growth will be moderate and uneven. The pace of recovery will remain modest in the major advanced economies. Meanwhile, in Asia, domestic demand is expected to continue to support growth.