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Economic Focus

Inflation cools in January

Slight decline from December rate . . .

Headline consumer inflation moderated to 4.3% Y/Y in January from 4.4% in December as food inflation slowed. Because food is such a significant component of the index, its slide dominated the impact of higher energy-related costs. The latter, brought about by increased world oil prices, was evident in accelerating inflation rates in indexes for fuel, light and water and services. Aside from these, inflation rates in other items were relatively stable. More details are shown in Figure 1.

. . . on slower food inflation

Slower food inflation was due to declining price increases for most food items, including the important ones of rice, fish, fruits and vegetables and meat. Such moderation may be due to the full restoration of supplies and supply chains damaged during strong typhoons in 4Q09 and the passing of Christmas holidays that cause demand spikes. As shown in Figure 2, food inflation picked up markedly in October and November, flattened out in December and declined in January. It is instructive that soaring sugar prices had negligible impact on January food inflation because sugar is such a small part of the food index.

Moderation in energy-related costs expected

Crude oil prices continued to increase in January and those were reflected in higher price adjustments for refined products at the retail level. In particular, price hikes in gasoline and diesel pushed up inflation in services while similar hikes in LPG and kerosene drove up inflation in fuel, light and water (utilities). Increased water rates also buoyed inflation in utilities. However, similar to December food inflation, inflation in utilities flattened out in January, as seen in Figure 2. We believe this trend will continue in coming months as world oil prices take a breather from recent sharp gains. Those were driven by expectations of a strong global economic recovery. We think that while the recovery will materialize, it will not be dramatic.

No change in inflation and monetary policy outlook

Similar to headline inflation, core inflation also slowed in January, to 3% from 3.2% in December. Both trends support our outlook the central bank will not be changing its overnight borrowing rate in coming months. With recent cuts in pump prices, headline inflation in February is likely to show further moderation. Thus we maintain our belief the policy rate will increase starting in June yet and tightening will be phased in gradually. Our 2010 inflation forecast of 4.2% is also unchanged on the assumption commodity prices will rise modestly and not spike as happened in 2008.

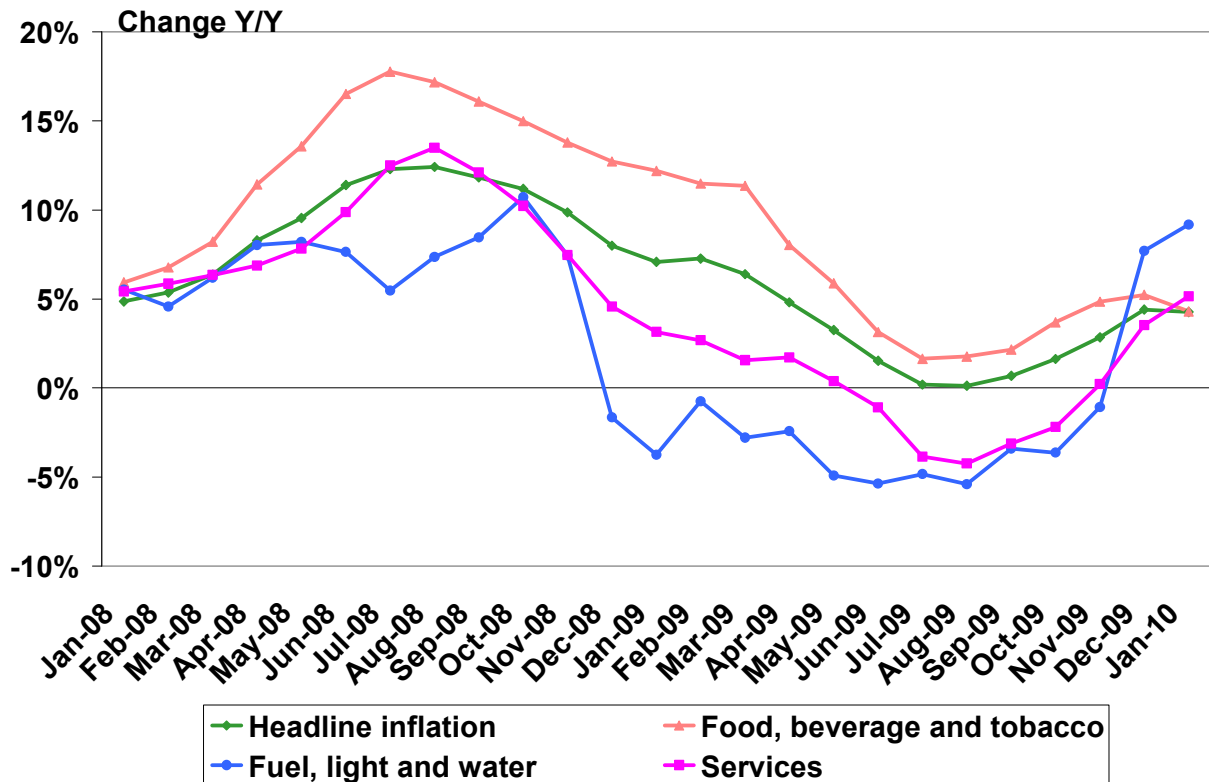
SEE APPENDIX I FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATIONS

Figure 1. Food inflation slows as typhoon effects wear off

	%Y/Y (2000=100) not seasonally adjusted										Weight (%)
	4Q08	2008	1Q09	2Q09	3Q09	4Q09	2009	Nov-09	Dec-09	Jan-10	
Headline inflation	9.7	9.3	6.9	3.2	0.3	3.0	3.3	2.8	4.4	4.3	100.0
Food, beverage & tobacco	13.8	12.9	11.7	5.6	1.9	4.6	5.8	4.8	5.2	4.3	50.0
Clothing	5.0	4.2	3.5	2.6	2.2	2.0	2.6	2.1	2.0	2.0	3.0
Housing & repairs	5.3	4.3	4.1	3.0	2.2	2.1	2.8	2.1	2.1	2.0	16.8
Fuel, light & water	5.4	6.5	-2.4	-4.2	-4.5	0.8	-2.6	-1.1	7.7	9.2	6.9
Services	7.4	8.6	2.5	0.3	-3.7	0.5	-0.2	0.2	3.5	5.1	15.9
Miscellaneous	3.8	3.0	3.3	2.9	2.3	1.9	2.6	1.9	1.8	1.7	7.5
Core inflation	7.7	6.2	6.3	4.4	3.1	2.9	4.1	2.7	3.2	3.0	

Sources: National Statistics Office, CEIC and Kim Eng Securities

Figure 2. Inflation rates in fuel and services likely to flatten too in coming months



Sources: National Statistics Office, CEIC and Kim Eng Securities

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