

Philippines Monthly Economic Developments

February 2018

- Recent volatility in the US stock market rippled through global markets, impacting also the Philippine stock exchange in the first two weeks of February.
- The Philippine peso came under renewed pressure in January.
- The Philippine economy expanded by 6.7 percent year-on-year in 2017, fueled by improving external demand.
- The balance of payments registered a higher deficit in 2017.
- Manufacturing activities continued to contract in December and the Purchasing Managers' Index dropped sharply in January.
- Headline inflation surged, hitting the ceiling of the central bank's inflation target range in January.
- Domestic liquidity and credit growth moderated in December.

Recent volatility in the US stock market rippled through the global markets, impacting also the Philippine stock exchange in the first two weeks of February.

After reaching an all-time high of 9,058 on January 29, the Philippines Stock Exchange index (PSEi) suffered its biggest single-day drop in more than a year (by 2.2 percent) on February 5 to 8,611. The PSEi tracked the decline in global equity markets as investors weighed the impact of a potentially faster pace of the US Federal Reserve's policy rate normalization. As a result, the PSEi experienced net-selling amounting to Php7.0 billion in the first two weeks of February, which more than reversed the Php2.2 billion net-foreign buying registered in January. The PSEi closed at 8,487 on February 12, close to the level at end-December.

The Philippine peso came under renewed pressure in January.

After strengthening to below the Php/US\$50.00 mark in December, pressure on the peso mounted in late January and it closed the month at Php/US\$51.42. This represented a 3.0 percent month-on-month depreciation from the Php/US\$49.93 closing in end-December of 2017, and a 3.4 percent year-on-year depreciation from the Php/US\$49.72 closing in end-January 2017. The peso has recently underperformed relative to other regional currencies, partly on concerns on the growing current account deficit of the Philippines. In addition, foreign sentiments on emerging markets have weakened after the US Federal Reserve signified a potentially faster pace of rate hikes and inflation expectations increased. Gross international reserves marginally declined to US\$81.2 billion in January from US\$81.6 billion in December 2017. Import coverage in January declined to 8.2 months' worth of imports of goods and payments of services and primary income from 8.8 months' in January last year.

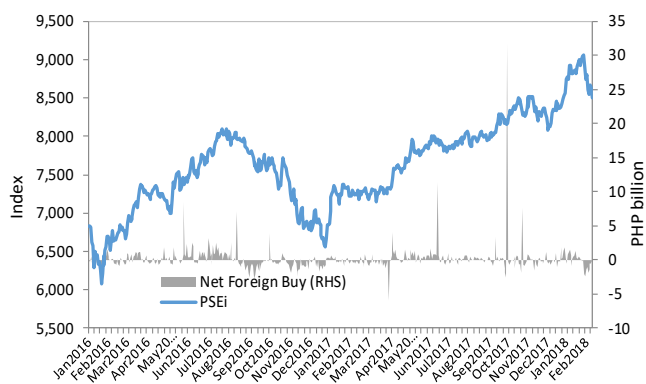
The Philippine economy expanded in 2017 by 6.7 percent year-on-year, fueled by improving external demand.

The Philippine economy benefitted from strong global growth, with exports expanding by 19.2 percent year-on-year in 2017, nearly doubling the 10.7 percent export growth in 2016. Meanwhile, import growth slowed in 2017, to 10.2 percent year-on-year, from 18.4 percent growth in 2016. On the domestic demand side, private consumption moderated to 5.8 percent year-on-year growth in 2017, compared to 7.0 percent in 2016. Rising inflation, weaker consumer sentiments, and a slightly higher unemployment rate contributed to this moderation. In addition, investment growth slowed to 9.0 percent year-on-year in 2017, significantly lower compared to the 23.7 percent registered a year ago. The slowdown in investment growth was driven by the deceleration of growth in durable equipment and construction, from 34.5 to 12.2 percent year-on-year and from 15.1 to 5.7 percent year-on-year in 2017, respectively.

The balance of payments registered a higher deficit in 2017.

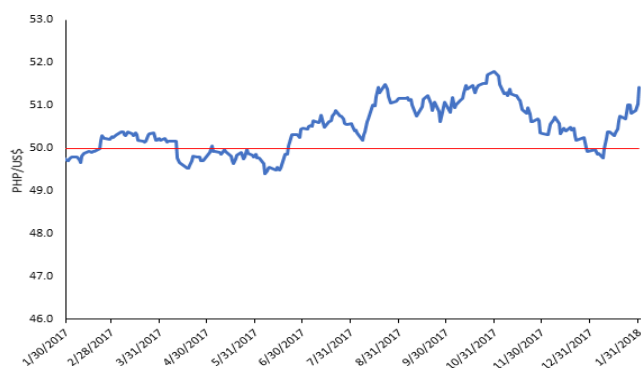
The 2017 balance of payments (BOP) position registered a US\$863.0 million deficit (0.3 percent of GDP) compared to a US\$420.1 million (0.1 percent of GDP) deficit in 2016. The higher deficit was attributed to a widening trade deficit and higher capital outflow, specifically, net outflows of foreign portfolio investments. Meanwhile, personal remittance from overseas Filipinos for the first eleven months of 2017 grew 5.1 percent year-on-year, reaching US\$28.2 billion compared to US\$26.9 billion during the same period in 2016. Net foreign direct investments grew strongly by 20.1 percent year-on-year, reaching US\$8.7 billion for the first eleven months of 2017, driven by higher intercompany borrowings and net investments in equity capital.

Figure 1: Recent global financial market volatility impacted also the PSEI after a strong start in January ...



Source: Philippine Stock Exchange

Figure 2: ... and the peso encountered renewed pressure.



Source: Philippine Statistics Authority (PSA)

Manufacturing activities continued to contract in December and the Purchasing Managers’ Index dropped sharply in January.

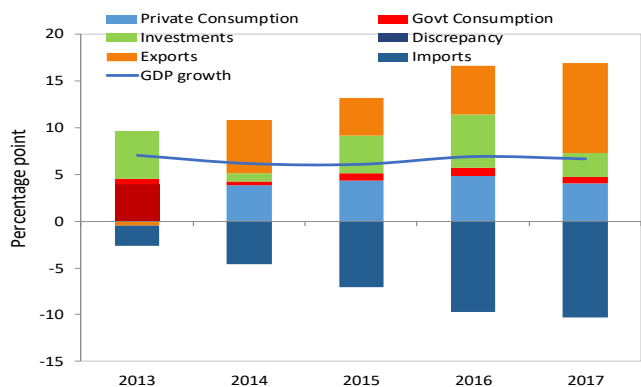
The volume of production index (VoPI) contracted in December 2017 by 9.7 percent year-on-year, a substantial change compared to the 21.7 percent growth in December 2016. The negative VoPI growth represented the fourth consecutive month of contracting manufacturing activities and was due to weaker activities in major sectors such as chemical production, footwear and apparel manufacturing. The Nikkei Philippines Purchasing Managers’ Index (PMI) declined sharply to 51.7 in January from 54.2 in December, but remained in expansion territory. This was due to softer demand and higher input costs, reflected in slower expected growth in output.

Contrary to the strong export performance during 2017, in December exports shrank for the first time in over a year.

Export growth contracted by 4.9 percent year-on-year in December, a reversal from the 2.7 percent expansion in November and the 6.6 percent growth registered a year ago.

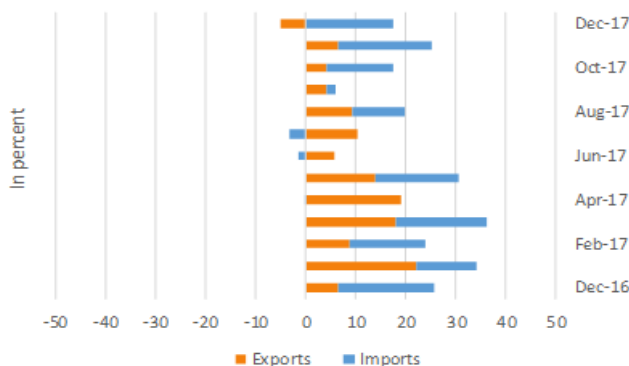
The unexpected sharp decline in exports was driven by the contraction of exports of agriculture goods by 61.7 percent. Meanwhile, import growth remained strong in December, growing by 17.6 percent year-on-year, but slightly lower than the 18.5 percent growth in November. Import growth were primarily driven by raw materials and intermediate goods, and consumer goods, which expanded by 17.0 percent (compared to 14.1 percent in December 2016) and 13.3 percent year-on-year (15.8 percent in December 2016), respectively. However, 2017 was a year of strong export growth, with merchandise exports expanding at 9.5 percent year-on-year, in contrast to the 2.4 percent contraction in 2016. Electronics exports, which accounted for more than half of the export bill, fueled this robust performance. Import growth decelerated in 2017 to 10.2 percent year-on-year from 18.4 percent growth in 2016, due to weaker imports of capital goods and consumer goods, which expanded by 4.2 percent year-on-year (compared to 46.6 percent in 2016) and 8.4 percent (30.1 percent in 2016).

Figure 3: Due to improved external demand, the economy grew strongly at 6.7 percent in 2017.



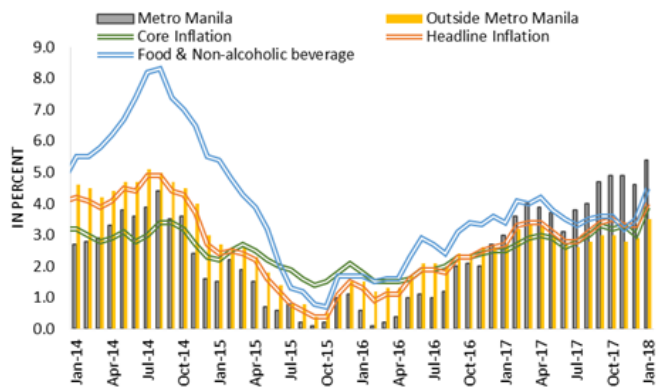
Source: PSA

Figure 4: Export growth rebounded in 2017, while import growth moderated.



Source: PSA

Figure 5: Inflation spiked to a three-year high mainly due to higher food and fuel prices.

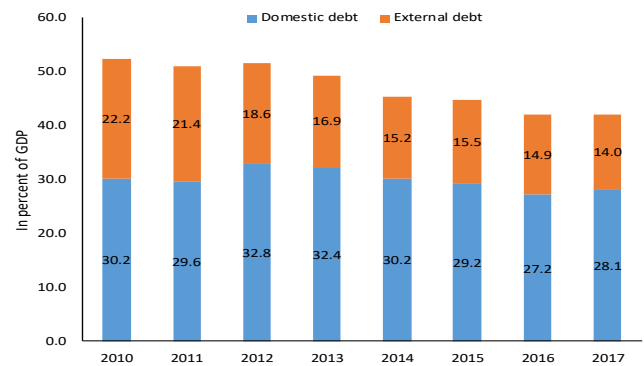


Source: *Bangko Sentral ng Pilipinas (BSP)*

Headline inflation surged in January, hitting the ceiling of the central bank’s inflation target range. The 12-month Consumer Price Index (CPI) picked up to its fastest pace in more than three years, recording a 4.0 percent year-on-year increase in January. This topped the 3.3 percent year-on-year inflation recorded in December 2017 and compared to 2.7 percent in January a year ago. On a month-on-month basis, the increase was 1.0 percent in January, compared with 0.3 percent in December. This increase was mainly due to higher prices for food and fuel. Weather-related production disruptions contributed to food inflation which went up for most commodities including rice, fish, and vegetables. The combination of rising international prices for crude oil and the new fuel excise tax were responsible for higher transportation prices. Excluding volatile food and energy prices, core inflation also climbed rapidly from 3.0 percent in December to 3.9 percent year-on-year in January, partly due to the pass-through effect if a weaker peso. The Monetary Board of the *Bangko Sentral ng Pilipinas (BSP)* decided on February 8 to maintain the key policy rate at 3.0 percent. The BSP revised its full-year inflation forecast to 4.3 percent in 2018 from its previous forecast of 3.4 percent in December.

Domestic liquidity and credit growth moderated in December. Domestic liquidity (M3) grew by 11.9 percent year-on-year to about Php10.6 trillion in December, slowing from 14.0 percent a month before, in November, and 12.4 percent in December 2016. On an annual basis, growth in bank lending net of reverse repurchase placements (RRP) with the BSP, expanded at a slower rate of 19.0 percent year-on-year in December compared to 19.3 percent in November, but still faster than the 17.2 percent in December 2016. Business loans, which comprised 88.9 percent of banks’ aggregate loan

Figure 6: The government maintained its debt-to-GDP ratio in 2017.



Source: *Bureau of the Treasury*

portfolio, net of RRP, went primarily to real estate activities, utilities, and wholesale and retail trade activities. Growth in credit to household slowed to 17.2 percent year-on-year from 20.6 percent in November, but credit card loans continued to expand rapidly. The banking system is stable with the share of non-performing loans at 2.0 percent in December, close to the 2.1 percent of total loan portfolio in December 2016. The latest available capital adequacy ratio is at 15.3 percent.

The national government maintained its debt-to-GDP ratio in 2017. For the second consecutive year, the national government registered in 2017 a 42.1 percent debt-to-GDP ratio, as the national government debt stock grew at a similar pace as nominal GDP. The domestic debt-to-GDP ratio increased to 28.1 percent of GDP in 2017, from 27.2 percent a year ago, as the government continues to favor domestic borrowing to finance its fiscal deficit. On an annual basis, the domestic debt stock of the national government expanded by 12.9 percent, compared to 1.3 percent a year ago. On the other hand, the external debt-to-GDP ratio of the national government declined to 14.0 percent of GDP in 2017, from 14.9 percent in 2016, as the national government external debt increased by just 2.6 percent year-on-year compared to 4.2 percent in 2016.