Philippines Monthly Economic Developments

September 2017

THE WORLD BANK
IBRD • IDA | WORLD BANK GROUP

- The Philippines Stock Exchange index (PSEi) slightly weakened in August.
- The Philippine peso rebounded in early September after a volatile performance in August.
- The strong export recovery continued in July while imports contracted for the second consecutive month.
- Manufacturing activities contracted in July for the first time in two years.
- Higher food and energy prices pushed inflation back up to 3.1 percent in August.
- Credit growth expanded in July with double-digit growth for both business and household loans.
- The government fiscal deficit moderated in July compared to June because revenue growth accelerated.
- In July, the unemployment rate increased marginally, while underemployment improved amidst a decline in labor force participation.

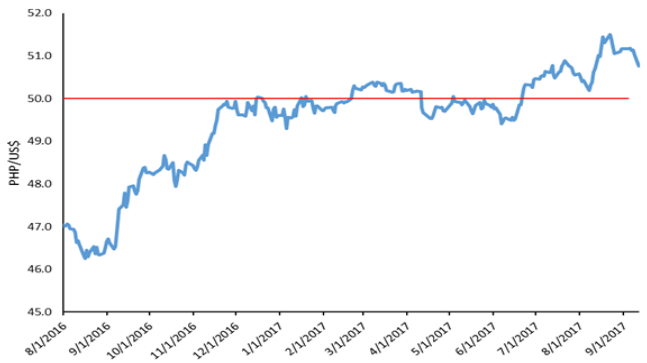
The Philippines Stock Exchange index (PSEi) slightly weakened in August. The PSEi contracted by 0.7 percent month-on month, closing at 7,958 in August which was largely the result of seasonal factors. However, this represents a 2.2. percent improvement on an annual basis, and by end-August the PSEi has expanded by 16.3 percent since January which is comparable to the top performing major stock indices in the region. That was partly due to the return of brisk net foreign buying. In August, it increased to Php2.5 billion from Php1.9 billion in July, a welcome reversal from the Php2.1 billion net-foreign selling registered a year ago.

The Philippine peso rebounded in early September after a volatile performance in August. The peso closed at Php/US$51.17 in end-August, marking a 9.7 percent year-on-year depreciation from the closing in August 2016, and a 1.2 percent month-on-month depreciation from July. The foreign exchange market remained volatile, trading in the range of Php/US$50.26-51.46. In the first week of September, the peso rebounded back to the Php/US$50.00 level mainly due to dampened sentiments vis-a-vis the US dollar and more muted expectations of a new U.S. rate hike. Gross international reserves (GIR) edged up in August to US$81.5 billion from US$81.1 billion in July, but were reportedly lower than the US$85.8 billion in August last year. The change was due to higher international gold prices and inflows from central bank's investments abroad. At its current rate, the GIR covers 8.7 months' worth of imports of goods and payments of services and primary income.

The strong export recovery continued in July while imports contracted for the second consecutive month. Exports grew by double digits for the sixth time in 2017, increasing by 10.4 percent year-on-year in July compared to the 0.8 percent growth registered in June. Export growth was driven by manufactured goods exports which expanded by 8.7 percent year-on-year and accounted for nearly ninety percent of total exports. In particular, electronic goods, which made up half of total exports, grew by 11.9 percent year-on-year, with semi-conductor exports expanding at 13.4 percent. Meanwhile, imports declined at a faster rate of 3.2 percent year-on-year, compared to the 2.5 percent contraction in June. However, the contraction was of the wrong kind, i.e. due to the decline of imports of capital goods (11.5 percent, year-on-year) and raw materials and intermediate goods (8.2 percent, year-on-year). At the same time, imports of consumer goods accelerated further in July, expanding by 10.7 percent year-on-year compared to the 7.0 percent growth registered in June.

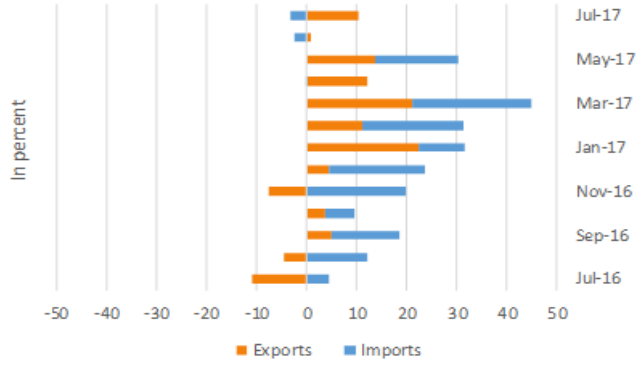
Manufacturing activities contracted in July for the first time in two years. The volume of production index (VoPI) for manufacturing shrank for the first time after registering 24 months of consecutive growth since June 2015. The VoPI declined by 1.1 percent year-on-year in July compared to 12.1 percent growth in July 2016. In all, the manufacturing sector has been shedding growth momentum since January 2017. In July, there was a marked slowdown in factory activities in the chemical, rubber and plastic, and textile industries. Production for footwear and wearing apparel, and fabricated metals remained relatively strong. Meanwhile, the Nikkei Philippines Manufacturing Purchasing Managers' Index (PMI) dropped significantly to 50.6 in August from 52.8 in July, signaling that factory output expansion is still likely albeit at a slower pace. The August decline is attributed to weaker sales to domestic and foreign consumers, coupled with a decline in new exports orders. The average capacity utilization rate marginally eased to 83.7 percent in July from 83.8 percent in June, with 12 of 20 major industries operating at 80 percent and above capacity.

Figure 1: The peso rebounded in early September.



Source: Philippine Statistics Authority (PSA)

Figure 2: Exports maintained their recovery while imports contracted for the second consecutive month.

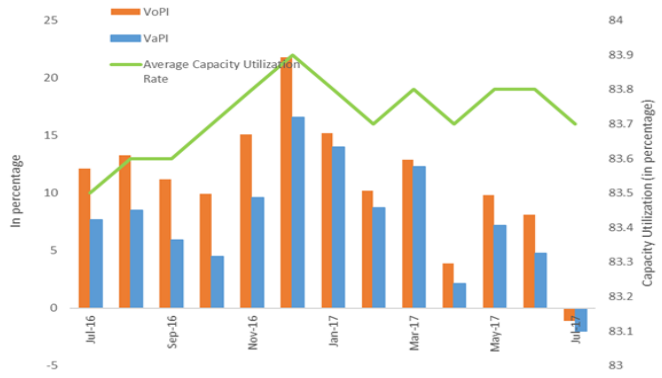


Source: PSA

Higher food and energy prices pushed inflation back up to 3.1 percent in August. The 12-month Consumer Price Index rose again to 3.1 percent year-on-year in August from 2.8 percent in July, moving back towards its peak of 3.4 percent in April. The main inflation driver was food inflation. Food prices grew by 3.7 percent due to faster price increases in fish, and fruits and vegetables as a result of tight domestic supply caused by a series of typhoons that hit the country during the previous month. In addition, a combination of electricity rate adjustments and higher prices for domestic petroleum products contributed to higher energy inflation. Core inflation rose to 3.0 percent in August from a revised 2.8 percent in July, moving again closer to its peak of 3.0 percent in April. The year-to-date average inflation stood at 3.1 percent, falling within the government target range of 2-4 percent. The central bank's monetary board maintained its key policy rate at 3.0 percent during its most recent meeting on August 10.

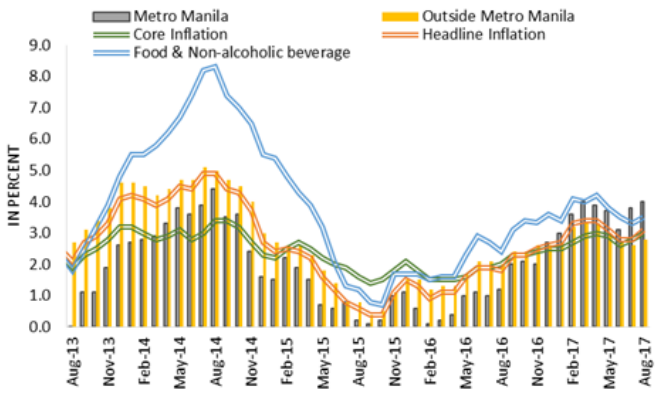
Credit growth expanded in July with double-digit growth for both business and household loans. Domestic liquidity (M3) grew by 13.5 percent year-on-year to about Php10.0 trillion in July, higher than the revised 13.3 percent expansion in the previous month. Demand for credit remained the principal driver of money supply growth. Outstanding loans of commercial banks grew by 19.7 percent year-on-year in July compared to 17.7 percent in July 2016. Bank lending to households increased by 22.3 percent due to the sustained demand in auto loans, credit card loans and salary-based general purpose loans. Meanwhile, lending to businesses expanded by 18.9 percent, driven by credit to real estate activities, wholesale and retail trade, and manufacturing. The banking system remains stable with a non-performing loans ratio of 2.0 percent in July (compared to 2.2 percent a year ago). The capital adequacy ratio of 15.3 percent for the whole banking system remains above the minimum ratio of capital to risk weight assets of 10.5 percent under Basel III.

Figure 3: Factory output contracted for the first time in two years.



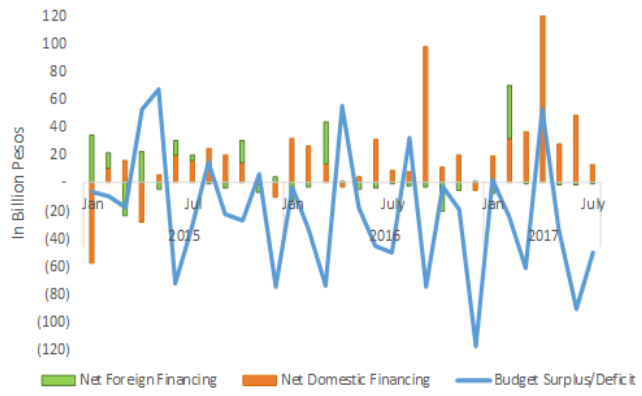
Source: PSA

Figure 4: Headline and core inflation rose again in August.



Source: PSA

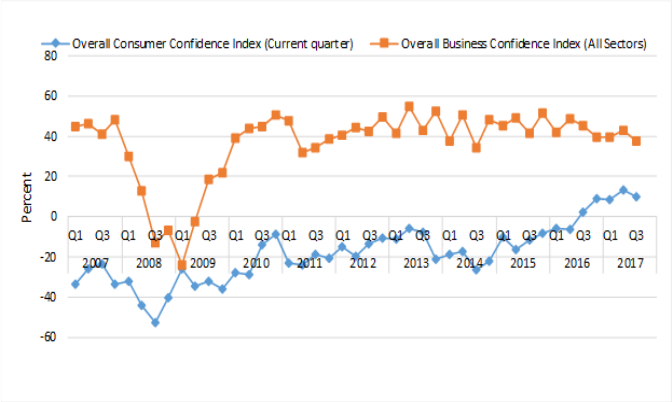
Figure 5: The government fiscal deficit moderated in July.



Source: Bureau of the Treasury

The government fiscal deficit moderated in July compared to June because revenue growth accelerated. Government expenditures reached Php245.0 billion in July, expanding in nominal terms by 11.0 percent year-on-year, more than double the 4.9 percent growth in July 2016. This represents the third consecutive month of double-digit growth in spending, making up for the slow start in the first four months of 2017. Recurrent expenditures and the public infrastructure program fueled this growth in expenditures in July. In particular, maintenance and operating expenses expanded by 41.1 percent year-on-year, personnel costs by 25.8 percent, and infrastructure and other capital outlays by 25.0 percent. Meanwhile, government revenues reached Php195.0 billion in July 2017, expanding by 14.3 percent year-on-year in nominal terms, reversing the 4.6 percent contraction registered a year ago. Revenue growth was due to the rapid acceleration of tax revenue, which grew by 16.4 percent year-on-year in nominal terms. Tax revenues received a boost from the initial Php3.4 billion tax settlement paid by Mighty Corporation for penalties from various tax evasion cases. However, the accelerated revenue growth could not outbalance the continued growth in expenditure. As a result, the fiscal deficit stood at Php50.5 billion in July, similar to the Php50.7 billion budget gap a year ago, but lower than the June fiscal deficit (Php154.5 billion). The government continued to finance its budget gap through domestic sources, as net-domestic financing increased by 44.0 percent year-on-year.

Figure 6: Consumer and business confidence remain in positive territory.



Source: Bangko Sentral ng Pilipinas (BSP)

In July, the unemployment rate increased marginally, while underemployment improved amidst a decline in labor force participation. The unemployment rate slightly increased to 5.6 percent year-on-year in July, from 5.4 percent a year ago, as the country registered an estimated 0.8 million in net job losses. Net job losses occurred in both the agriculture and services sectors, with an estimated 1.1 million job losses in July. The industry sector, on the other hand, registered net job creation of around 0.4 million. Meanwhile, the underemployment rate declined to 16.3 percent in July compared to 17.3 percent a year ago. The decline in both employment and underemployment coincided with the exit of around 0.8 million individuals from the labor force, as the labor force participation rate declined sharply to 60.6 percent in July compared to 63.3 percent a year ago.

Consumer and business confidence moderated in the third quarter of 2017, but remained in positive territory. Based on the *Bangko Sentral ng Pilipinas* consumer expectation survey, the overall consumer confidence index weakened to 10.2 percent in the third quarter of 2017 compared to 13.1 percent in the second quarter on growing concerns over increasing inflation and unemployment, and lack of income rises. However, this remains the second highest level of recorded consumer confidence since the survey started in 2007. Based on the business expectations survey, business confidence declined to 37.9 percent in the third quarter of 2017 compared to 43.0 percent a quarter ago due to the weaker peso, and higher inflation and geopolitical tension.

Please contact Birgit Hansl: bhansl@worldbank.org

Prepared by a World Bank team under the guidance of Birgit Hansl, consisting of Kevin Chua, Kevin Thomas Cruz and Griselda Santos.