Philippines Monthly Economic Developments

June 2017

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- The Philippine stock exchange index (PSEi) rallied in May, as it benefited from strong foreign purchases.
- Gross Domestic Product (GDP) posted a 6.4 percent year-on-year growth in the first quarter of 2017.
- In April, manufacturing activities expanded at a slower rate while average capacity utilization eased.
- Exports expanded in April by 12.1 percent while imports contracted for the first time in nine months.
- Headline and core inflation finally started to ease in May.
- The government posted a fiscal surplus in April, as both national government revenues and expenditures contracted for the first time in 2017.
- The Lower House approved the first comprehensive tax reform package.

While the Philippine peso traded in May in a relatively stable foreign exchange market, it continues to depreciate on an annual basis. Foreign exchange markets were less volatile during May, resulting in the peso trading within a relative narrow range of Php/US$49.65-50.00. The peso closed at the end of the month at Php/US$49.87, representing a slight 0.3 percent month-on-month depreciation from the Php/US$49.70 closing in end-April. However, on an annual basis, the peso continued to depreciate at 6.6 percent from the Php/US$46.78 closing in end-May 2016, similar to a 6.3 percent year-on-year depreciation in April.

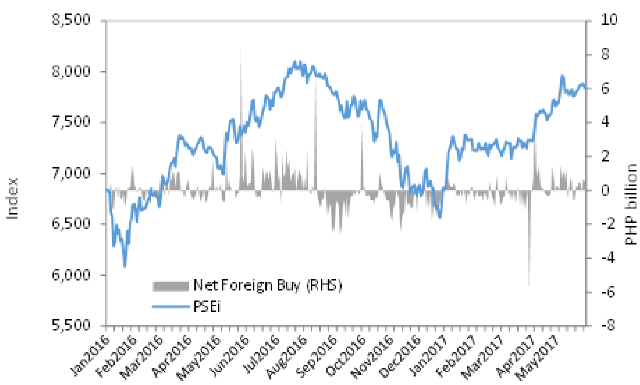
The Philippine stock exchange index (PSEi) rallied in May, as it benefited from strong foreign purchases. In May, the PSEi improved by another 2.3 percent month-on-month, closing at 7,837. It reached its highest level of the past nine months. This also represents the third consecutive month of expansion for the PSEi, which built on its 4.8 percent gain in April. Overall, the index has expanded by 8.1 percent year-on-year, and 14.2 percent since January this year as foreign funds continued to flow back into stock exchange. Net-foreign buying totaled Php8.6 billion, compared to Php13.4 billion in May 2016.

Gross Domestic Product (GDP) posted a 6.4 percent year-on-year growth in the first quarter of 2017. This marked a decline from the 6.6 percent year-on-year growth during the fourth quarter of 2016 and 6.8 percent in the first quarter of 2016. Export and consumption growth remained strong, with 20.3 percent and 5.3 percent respectively, but government consumption and investment growth weakened on an annual basis to 0.2 and 7.1 percent respectively. This quarterly growth outcome was in line with the World Bank growth projection, given the high base in quarter one 2016, when large election-related spending boosted growth uncharacteristically. Mirroring a slower expenditure execution in the first quarter on the fiscal side, public construction grew by only 2 percent in the first quarter of 2017, compared to 38.5 percent growth in the same period a year ago. On the production-side, the services sector was the main driver of growth in the first quarter, expanding on an annual basis at 6.8 percent. At the same time, industry growth decelerated to 6.1 percent year-on year, from 9.3 percent in the first quarter of 2016. Agriculture recovered with 4.9 percent year-on year growth, compared to a contraction of 4.3 percent in quarter one 2016.

In April, manufacturing activities expanded at a slower rate while average capacity utilization eased. The volume of production index (VoPI) grew in April at 5.9 percent year-on-year, slowing from 10.1 percent in April 2016. This was the slowest recorded growth in the VoPI since January 2016. Production activities remained upbeat for metal products, furniture, and petroleum products; however, factory activities slowed notably for transport equipment and chemical products. The average capacity utilization rate eased slightly to 83.7 percent in April (from 83.8 in March), but remained higher than the 83.4 percent recorded in April last year. Meanwhile, the Nikkei Philippines Manufacturing Purchasing Managers' index (PMI) rose to 54.3 in May from 53.3 in April, signaling optimism driven by new orders and strong purchase activity.

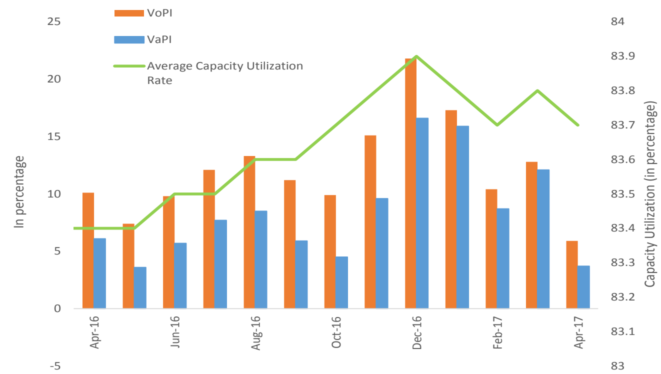
Exports expanded in April by 12.1 percent while imports contracted for the first time in nine months. Philippine exports grew in double digits for the fourth consecutive month, contrary to the 3.4 percent contraction in April 2016. Exports of electronics products continued to account for the largest share of the total export bill, 50.9 percent. At the same time, imports contracted by 0.1 percent year-on-year in April, a sharp reversal from the 35.9 percent expansion in the same month in 2016, due a decline in both consumer goods and capital goods imports.

Figure 1: The PSEi reached its highest level in nine months.



Source: Philippine Stock Exchange

Figure 2: Manufacturing activities expanded at a slower rate.

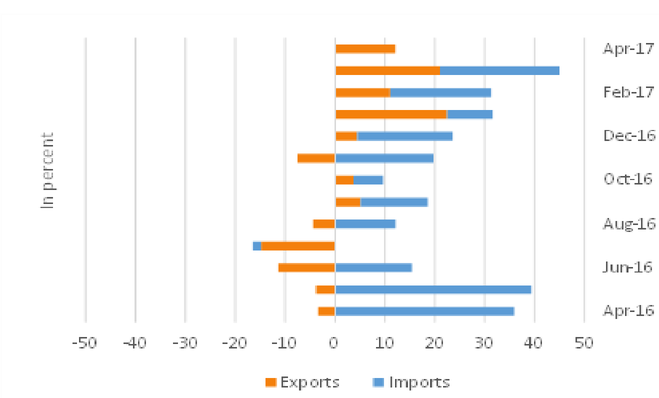


Source: Philippine Statistics Authority (PSA)

Headline and core inflation finally started to ease in May. The 12-month Consumer Price Index declined to 3.1 percent year-on-year in May, after peaking at 3.4 percent in April. This ended a nearly uninterrupted trend of accelerating inflation, which started at 1.1 percent in March–April last year. In May, inflation slowed across all commodities. Food inflation decelerated already for the second consecutive month, from its peak of 4.0 percent in March, due to lower prices for staple foods such as fish, oils and fats, sugar and vegetables. Energy prices softened due to a combination of lower international crude oil prices and lower power generation charges. Core inflation, which excludes volatile food and energy prices, also retreated. It declined to 2.9 percent year-on-year in May from its peak of 3.0 percent in April (compared to 1.6 percent in April 2016). This resulted in a year-to-date average headline inflation rate of 3.1 percent, which is within the central bank's target range of 2-4 percent. The next monetary board meeting is scheduled for June 22, and key policy rates are liely to be kept on hold.

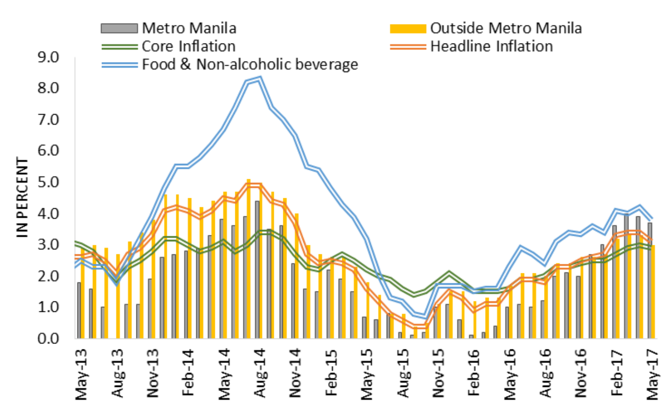
Strong credit growth continued, highlighting ample liquidity in the banking system. Domestic liquidity (M3) continued to grow in April at 11.2 percent year-on-year to Php9.5 trillion, driven by strong commercial lending increases. Lending from commercial banks expanded by 19.2 percent year-on-year in April, compared to 17.3 percent in April a year ago. Over the first four months of 2017, credit growth averaged 18.9 percent. Firm loans constitute nearly 90 percent of the total loan portfolio, and grew in April on an annual basis of 18.4 percent, largely directed to the real estate, manufacturing, and wholesale and retail trade sectors. Household loans grew in April at an even faster annual rate of 24.3 percent, based on a continued expansion in salary loans and motor vehicle loans. The banking system remained strong with a non-performing loans ratio of 2.0 percent in March, and a capital adequacy ratio at 15.6 percent based on recent available data.

Figure 3: Exports continued to grow in double-digits.



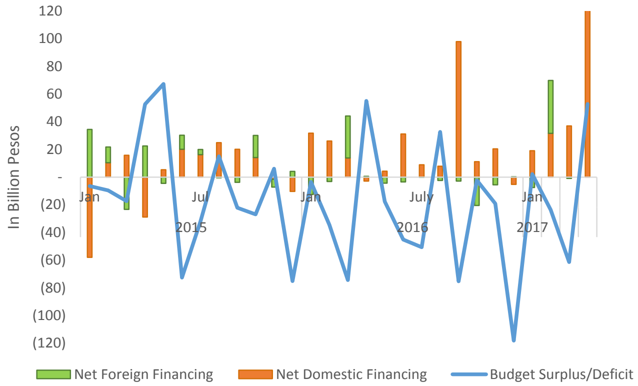
Source: PSA

Figure 4: Headline and core inflation eased.



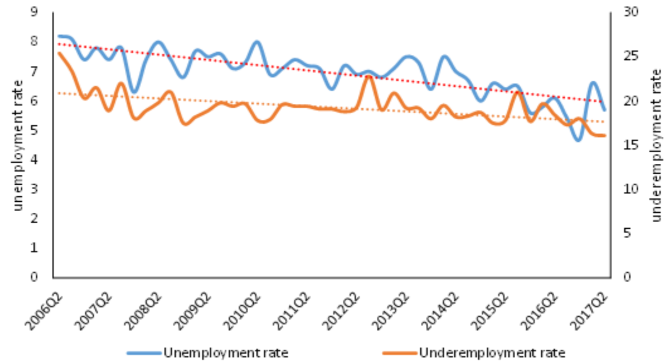
Source: PSA

Figure 5: The government posted a fiscal surplus in April.



Source: Bureau of the Treasury

Figure 6: Both the unemployment and underemployment rates improved.



Source: PSA

The government posted a fiscal surplus in April, as both national government revenues and expenditures contracted for the first time in 2017. After a weak start for expenditure execution in the first quarter, government spending continued to fall below expectation in April. Expenditures reached Php183.1 billion, declining in nominal terms by 4.5 percent year-on-year (a reversal from the 22.4 percent growth in April 2016). The decline in public spending was led by a sharp contraction in capital spending: maintenance and operating expenditures fell in nominal terms by 27.5 percent year-on-year (compared to 23.7 percent growth in April 2016) and infrastructure spending decreased by 21.2 percent year-on-year in nominal terms (compared to 82.1 percent growth in April 2016). The Department of Budget and Management attributes the drop in infrastructure spending to the delay in the start of new big-ticket projects and lower disbursements of the Department of Public Works and Highways. Meanwhile, revenue growth also decreased in nominal terms by 4.4 percent year-on-year in April, reaching Php235.9 billion. Non-tax revenues dropped in nominal terms by 54.2 percent year-on-year in April as a result of a delay in remitted dividends from government-owned and controlled corporations. Tax revenue growth slowed in April to 3.8 percent year-on-year in nominal terms from 11.4 percent in April 2016 as both the Bureau of Internal Revenue and the Bureau of Customs failed to meet their collection targets. As a result, the government registered a Php52.8 billion surplus in April, which was 4.2 percent lower than the Php55.0 billion surplus of April 2016.

The Lower House approved the first comprehensive tax reform package. House Bill No. 5636, which consolidated the Department of Finance's version of the tax reform bill (House Bill 4774) with 54 other related tax bills, was approved by the House of Representatives on May 31 by 246 votes against 9 (and one member abstaining). The main features of the bill include the lowering of personal income taxes, limiting exemptions to the value added tax, adjusting the excise rates for fuel and automobiles, and the introduction of an excise tax to sugar sweetened beverages. Next, the Senate will debate the tax reform proposal once it resumes session in late July.

In April, the unemployment and underemployment rates declined. Although the unemployment rate declined to 5.7 percent in April year-on-year, compared to 6.1 percent in April 2016, the country posted an estimated 0.4 million in net job losses. The services sector, which accounts for about sixty percent of all jobs, recorded year-on-year net job losses of 557,000 in April. This coincided with the exit of some 549,000 individuals from the labor force, leading to a decline in the labor force participation rate to 61.4 percent in April from 63.5 percent in the same period last year. Both the agriculture and the industrial sector saw on an annual basis a small net job creation of around 125,000 and 39,000 workers respectively. Meanwhile, the underemployment rate continued to improve, declining in April to 16.1 percent year-on-year, its lowest level in over a decade. This is compared to 18.3 percent a year ago, and constitutes 962,000 less underemployed workers.

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