Monitoring the Philippine Economy
Year-End Report for 2017

Project of Angelo King Institute

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Growing at 6.7 percent in 2017, the Philippine economy realized robust full-year forecasts despite domestic and international economic challenges.

Economic performance: Aggressive government spending on infrastructure projects, growth of the manufacturing sector, and an uptick in the agriculture sector strengthen the Philippine economy.

Philippine economic growth slightly decelerated but maintained its momentum. The Philippines registered a growth of 6.7 percent, which was slightly slower than the 6.9 percent exhibited in 2016. Its growth rate was ranked third in the region, next to China and Vietnam who were able to attain economic growth of 6.9 percent and 6.8 percent, respectively. Despite the various economic challenges mainly associated with depreciation of the peso and rise in commodity prices, Philippine growth was still able to meet expectations. On the demand side, private consumption and investments declined with a widened trade gap while government spending expanded. On the supply side, the industry sector and the service sector slowed down while the agriculture sector thrived.

- **Major components of aggregate demand**

    - **Household consumption eased.**[2] Private consumption posted a slower growth of 5.8 percent from 7.0 percent y-o-y growth the previous year. The slowdown was mostly caused by decreases in consumption of major expenditure items, specifically, alcoholic beverages and tobacco (-4.0 percent growth from 5.9 percent growth in 2016), transport (4.9 percent from 10.6 percent), recreation and culture (1.3 percent from 7.7 percent), health (5.0 percent from 7.3 percent), and food and non-alcoholic beverages (5.5 percent from 6.9 percent). Also, higher commodity prices and continuing peso depreciation against the US dollar triggered the decline. On the other hand, remittances grew 5.3 percent, surpassing the government's target of 4.0 percent annual growth and recording a high total of US$31.29 billion in 2017.[3]

    - **Investments experienced a significant slowdown.**[4] Fixed capital formation recorded a 9.0 percent growth, lower than 23.7 percent the previous year. Decrease in private purchases due to lower project activations from concerns of an

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oversupply in domestic markets contributed to the slowdown. Moreover, the sizable decrease in growth of investments in durable equipment to 10.4 percent from 35.5 percent growth the previous year was a significant contributor to the slowdown. Construction and Breeding Stocks and Orchard Development (BSOD) recorded a low growth of 5.7 percent and 3.4 percent, respectively. On the other hand, Intellectual Property Products (IPP) recorded the highest growth of 40.0 percent due to increased investments in computers and software throughout the year.

- **Government consumption improved.**[5] Fiscal spending registered a robust 11.0 percent growth relative to 8.2 percent growth the previous year, reflecting reduced underspending than the previous administration. This acceleration in government consumption is mainly attributable to the *Build Build Build* infrastructure program of the current administration. Fiscal spending is foreseen to remain robust and even accelerate in the coming years in line with the goals set by the Philippine Development Plan 2017-2022 of the administration.

- **Impressive import and export performance boosted full-year trade growth.**[6] With accelerated growth in both imports and exports, total trade for 2017 posted an improved growth of 9.9 percent compared to 5.8 percent the previous year. Imports and exports exceeded government expectations with growth of 10.2 percent and 9.5 percent, respectively. However, in spite of the depreciating peso, the full-year deficit or trade gap widened to US$29.8 billion from a full-year gap of US$26.7 billion the previous year. While peso depreciation may make exports more attractive (price-wise) to foreign buyers and imports less attractive to domestic buyers, probably in consumer goods, forecasts for the sector indicate similar trade gaps in the near-term given the various ongoing public-sector infrastructure projects that require more imports of equipment or machinery than consumer goods.

- **Major components of aggregate supply**

  In this report, we present results from an alternative to the "traditional" (TRAD) method of decomposing growth of GDP in constant prices into sector contributions. This alternative method is a "generalized" (GEN) growth decomposition that applies to GDP in constant prices (e.g., in the Philippines) and to GDP in chained prices (e.g., in Canada and the US). While TRAD recognizes only "quantity" growth as the source of a sector's contribution to GDP growth, GEN posits that a sector's contribution comes from "quantity" growth and from "real price" growth where this price is, by definition, the ratio of a sector's deflator to the overall GDP deflator. The GDP deflator as the common denominator of the above ratio makes real GDP the numeraire and, thus, this ratio is the relative price or exchange value of the GDP of a sector in "GDP units," i.e., the "real price" of a sector's GDP. Therefore, a sector's positive "quantity" growth contribution will be diminished if accompanied by a negative "real price" growth of the same sector that may even result in a negative net contribution by the sector to GDP growth. On the other hand, a sector's positive "quantity" growth contribution will be enhanced if accompanied by a positive "real price" growth (see Table 3).[7]

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[5] https://www.dbm.gov.ph/index.php/secretary-s-corner/press-releases/list-of-press-releases/695-government-spending-in-2017-up-by-11-underspending-net-of-interest-payments-cut-to-2

[6] http://www.neda.gov.ph/2018/02/09/2017-ph-trade-growth-exceeds-govt-expectations/

[7] The results in Table 3 are AKI-DLSU *Philippine Economic Monitor* calculations by applying the data in Table 1 to a "generalized" (GEN) exactly additive decomposition of GDP growth into *pure growth effect* (PGE) and *price change effect* (PCE) as an alternative to the "traditional" (TRAD) GDP growth decomposition. Analytically, PGE is the result of real GDP or "quantity" growth holding real price constant and PCE is the result of relative price or "real price" growth holding quantity constant. The GEN formulas for PGE and PCE and the TRAD formula are given, respectively, by equations (12), (13), and (17) in Dumagan, Jesus C. (2016), "Effects of Relative Prices on Contributions to the Level and Growth of Real GDP," Working Paper Series No. 2016-036, Angelo King Institute for Economic and Business Studies, De La Salle University, Manila. This alternative framework follows from the decomposition of "aggregate

- **Service sector remained to be the major contributor.**[8] Although the sector experienced a slower growth of 6.8 percent than the 7.5 percent the previous year, it still contributed over half of the nation's GDP. Consequently, the sector contributed 4.29 percentage points to annual GDP growth from the supply side. Public Administration & Defense: Compulsory Social Security posted the fastest growth of 7.8 percent among the sector components. Meanwhile, Financial Intermediation; Real Estate Renting & Business Activities; Trade & Repair of Motor Vehicles, Motorcycles, Personal and Household Goods; Transportation, Storage and Communication; and Other Services attained slower growths.

- **Industry sector achieved the fastest growth.**[9] The industry sector posted the fastest growth of 7.2 percent in 2017. The sector accounted for approximately one-third of the nation's GDP, contributing 1.74 percentage points to annual GDP growth from the supply side. Manufacturing had the fastest growth of 8.4 percent. While, Construction and Electricity, Gas and Water Supply reported a slower growth of 5.3 percent and 3.4 percent, respectively.

- **Agriculture sector attained appreciable growth uptick.**[10] With favorable weather conditions in 2017, the agriculture sector was able to attain a growth of 4.0 percent, appreciably higher than 1.2 percent the previous year. The sector contributed 0.65 percentage points to annual GDP growth from the supply side. Agriculture and Forestry established a faster growth of 4.0 percent. While, Fishing continuously declined with a 0.9 percent decrease. Better results could be achieved if the weather would continue to be favorable and farming strategies would be improved.

Figure 1. Contributions to GDP growth (y-o-y, %) from Aggregate Supply
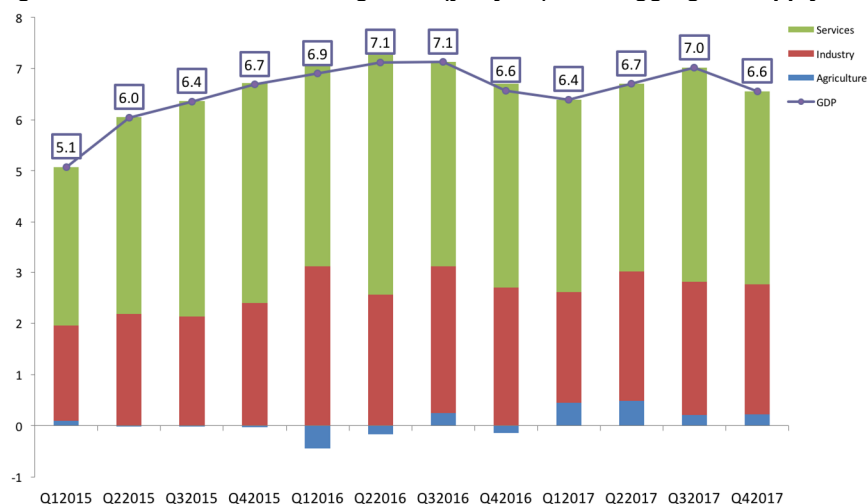
Source: Author's calculations based on data in Table 2 below.

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labor productivity" (ALP) growth in Dumagan, Jesus C. (2013), "A Generalized Exactly Additive Decomposition of Aggregate Labor Productivity Growth," Review of Income and Wealth, 59 (Issue 1): 157-168, where ALP is the ratio of GDP to total labor employment. Thus, by removing the labor variable, the decomposition of ALP growth in the latter paper yields the decomposition of GDP growth into PGE and PCE in the former paper which is implemented in Table 2.

[8] https://psa.gov.ph/regional-accounts/grdp/highlights
[9] https://psa.gov.ph/regional-accounts/grdp/highlights
[10] https://psa.gov.ph/regional-accounts/grdp/highlights

Challenges facing the economy

- **Peso-dollar exchange rate average depreciates[11]. Based on** monthly averages in 2017, the peso weakened by 5.8 percent to ₱50.40/US$ from the previous 2016 average of ₱47.49/US$1. With numerous factors affecting the peso-dollar exchange rate, it is expected that the peso will continue to depreciate against the dollar this year. The peso is vulnerable and it is speculated to be "Asia's worst performer" in 2018 as the current account deficit would continue to widen. Hopefully, the macroeconomic fundamentals and domestic economy performance would eventually help stabilize the peso.[12]

- **Unfavorable economic factors may jeopardize the economy.** Depreciation of the peso, higher crude oil prices, and rising consumer prices partly from the TRAIN LAW present challenges the Philippine economy has to overcome. The fiscal reform through the TRAIN LAW will affect not only the domestic market but foreign investment as well. With higher taxes, it may discourage investors from staying in the country.

- **Weather disturbances threaten the economy.** Unexpected inclement weather conditions, natural disasters, and the like disrupt agricultural activities and negatively affect the domestic supply in the country. These harsh conditions may worsen poverty level, unemployment rate, and threaten food security, especially for the poor Filipinos. Infrastructure improvements are imperative to augment agriculture sector's resiliency.

Other economic news

- **Stock market reports a remarkable PSEi.[13]** The Philippine stock market registered a noteworthy growth in 2017. On December 29, 2017, the PSEi closed at a new high record of 8,558.4 index points, which is higher than the PSEi a year ago by 25.1 percent. The stock market is expected to keep its stellar performance as a result of investor and consumer confidence, and considering as well the sustainable growth performance of the domestic economy.

- **Full-year inflation remains within target range.[14]** Full-year inflation for 2017 was recorded at 3.2 percent. This was higher than the recorded full-year inflation of 1.8 percent the previous year but it was within the government's target range of 2.0 percent to 4.0 percent. Inflation surged mainly due to higher price increases for selected food items and upward price adjustments for domestic petroleum prices and electricity rates. Weather disturbances and trade imbalances contributed to the accelerated inflation, but these were eased by the slower price increase in vegetables, and lower prices of sugar, jam, honey, and confectionery.
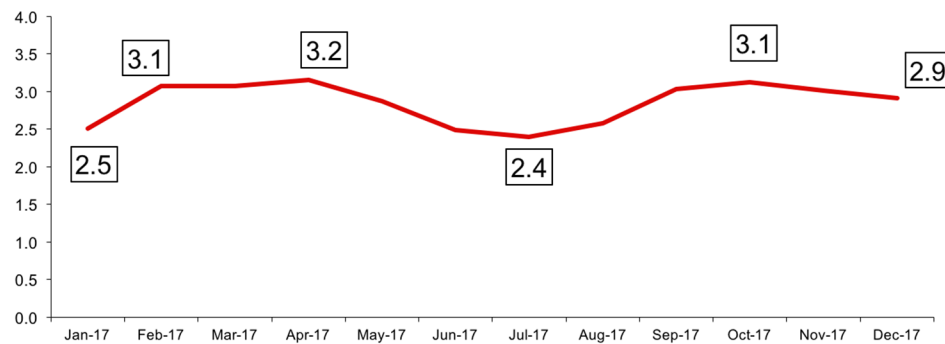
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[11] http://www.bsp.gov.ph/statistics/spei_new/tab12_pus.htm
[12] https://www.bloomberg.com/news/articles/2017-12-21/philippine-peso-seen-as-asia-s-laggard-for-2018-as-deficit-grows
[13] http://www.bsp.gov.ph/downloads/publications/2017/annrep2017.pdf
[14] http://www.bsp.gov.ph/downloads/publications/2017/annrep2017.pdf

Figure 2. Consumer price index (y-o-y, %)

Source: Graph prepared by author based on Philippine Statistics Authority data.

- **In the Industry sector, manufacturing consistently contributes the most to the economy.**[15] PSA reported on its Monthly Integrated Survey of Selected Industries (MISSI) that manufacturing, the industry subsector that consistently contributes the most to GDP, had an average capacity utilization of 83.9 percent as of November 2017. Majority of the manufacturing establishments in the country have been operating above 80.0 percent capacity since 2010. But manufacturing has posted a decline of 8.1 percent y-o-y in the volume of production index (VoPI). The reduction in output was due to decreases in the production of chemical products (-62.7 percent), tobacco products (-48.3 percent), footwear and wearing apparel (-23.9 percent), textiles (-33.8 percent), rubber and plastic products (-8.4 percent), and food manufacturing (-0.3 percent). Reversing this development for the long-term appears imperative since a vibrant manufacturing has traditionally been the bedrock in the transition from agriculture to industrial development. However, against tradition, the Philippine economy has bypassed the manufacturing base of industry to anchoring economic growth on the service sector which now comprises over 50 percent of the economy. Hopefully, the government's policies for growth acceleration and inclusion will eventually raise per capita purchasing power and expand demand for domestic manufacturing products, as those noted above, to induce the economy's manufacturing revival for sustainable growth.

- **Unemployment rate remains stable.** A full-year unemployment rate of 5.7 was reported for 2017. It is expected to be stable for the next 3 years as there is a steady source of possible employment in the manufacturing and service sectors, especially in the business process outsourcing industry. However, the issue on contractualization of workers should be resolved to alleviate the high underemployment rate in the country.

- **31st ASEAN Summit in the Philippines[16].** Last November 12-14, 2017, world leaders gathered to attend the 31st ASEAN Summit, with the theme "Partnering for Change, Engaging the World." This event was hosted by the Philippines, wherein related summits were held in the Philippine International Convention Center (PICC), Manila. At the main meeting, leaders of the ten ASEAN countries discussed and gave guidance to the various ASEAN sectoral bodies on the way forward in building a region of peace and progress for the mutual benefit of ASEAN citizens. The Philippines, as the host and

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[15] http://www.bsp.gov.ph/publications/media.asp?id=4550
[16] https://www.dfa.gov.ph/newsroom/dfa-releasesupdate/14628-significance-of-the-philippines-hosting-of-the-31st-asean-summit-and-related-summits

chair of ASEAN, was able to push for its own initiatives and play a vital role in finalizing the ASEAN Consensus on the Protection and Promotion of the Rights of Migrant Workers. Moreover, it showed leadership in various aspects of regional cooperation, increased connectivity, enhanced trade, while boosting local tourism and talents. Some of the significant accomplishments by the ASEAN leaders at the summit include: (1) Signing the ASEAN Consensus on the Protection and Promotion of the Rights of Migrant Workers—ten years after the ASEAN leaders signed the Cebu Declaration on the Protection and Promotion of the Rights of Migrant Workers in January 2007—to solidify social protection and access to justice and health services of the region's migrant workers, and ensure fair treatment. (2) Discussing ways to combat peace and order issues prevailing in the region. (3) Meeting US President Donald Trump, Chinese Premier Li Kequiang, UN Secretary-General Antonio Guterres, and the leaders of five other dialogue partners of ASEAN. An agreement between ASEAN member-countries and China on the drafting of a South China Sea code was also signed.

- **World Economic Forum's "Readiness for the Future of Production Assessment 2018" profiled the Philippines as a Legacy Country**[17]**.** The World Economic Forum evaluated the readiness of 100 countries and economies for the future of production on a scale of 0 (lowest) to 10 (highest). Two components of the assessment are Drivers of Production and Structure of Production. Then, countries are identified as one of the four archetypes (Leading/Legacy/High-Potential/Nascent) depending on their scores. The Philippines scored 6.12 (Rank 28) in Structure of Production and 4.51 (Rank 66) in Drivers of Production. Under the Structure of Production component, the Philippines scored the following: Complexity (Score: 5.91; Rank: 43) and Scale (Score: 6.44; Rank: 11). And, under the Drivers of Production component, the Philippines scored the following: Technology & Innovation (Score: 4.02; Rank: 59), Human Capital (Score: 4.59; Rank: 66), Global Trade & Investment (Score: 4.52; Rank: 69), Institutional Framework (Score: 4.35; Rank: 76), Sustainable Resources (Score: 5.45; Rank: 69), and Demand Environment (Score: 4.94; Rank: 45). Hungary, India, Lithuania, Mexico, Romania, Russian Federation, Slovak Republic, Thailand, and Turkey were profiled together with the Philippines under the Legacy archetype.

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[17] http://www3.weforum.org/docs/FOP_Readiness_Report_2018.pdf

Table 1. Philippine Economic Indicators

Philippines Economic Data												
Monthly Leading Indicators	**Jan-17**	**Feb-17**	**Mar-17**	**Apr-17**	**May-17**	**Jun-17**	**Jul-17**	**Aug-17**	**Sep-17**	**Oct-17**	**Nov-17**	**Dec-17**
Industrial Production (y-o-y, %)	14.9	9.8	12.3	0.1	2.1	-0.1	-5.1	0.3	-5.7	-6.5	-9.3	-4.8
Consumer Price Index (y-o-y, %)	2.5	3.1	3.1	3.2	2.9	2.5	2.4	2.6	3.0	3.1	3.0	2.9
Exports (y-o-y, %)	22.0	8.7	18.1	19.1	14.0	5.8	10.4	11.0	8.0	9.2	6.0	2.6
Imports (y-o-y, %)	12.2	15.2	18.0	-0.1	16.6	-1.3	-3.2	14.2	8.5	18.6	21.4	25.4
Trade Balance, US$ million	-2,469	-1,768	-2,297	-1,754	-2,737	-1,992	-1,646	-2,393	-2,077	-2,819	-3,845	-3,839
Total Reserves (less gold), US$ billion	73.73	73.58	73.01	74.08	74.18	73.49	73.06	73.29	72.90	72.35	72.26	73.23
Policy Rate	3	3	3	3	3	3	3	3	3	3	3	3
Fiscal Balance (million pesos)	2,222	-23,724	-61,471	52,797	-33,421	-90,873	-50,512	28,808	-36,892	-21,800	-8,623	-107,148
Quarterly/Annual Economic Indicators	**2012**	**2013**	**2014**	**2015**	**1Q2016**	**2Q2016**	**3Q2016**	**4Q2016**	**1Q2017**	**2Q2017**	**3Q2017**	**4Q2017**
Real GDP (y-o-y, %)	6.8	6.9	6.2	6.1	6.9	7.1	7.1	6.6	6.4	6.7	7.0	6.6
- Private Consumption	6.6	5.6	5.6	6.3	7.1	7.5	7.2	6.2	5.8	5.9	5.3	6.1
- Government Consumption	12.2	8.1	3.3	7.6	11.8	13.5	3.1	4.5	0.1	7.1	8.3	14.3
- Gross Capital Fixed Formation	-3.2	27.3	4.4	18.4	31.5	30.3	21.7	14.7	10.6	8.5	8.7	8.2
Current Account (% of GDP)	2.8	4.2	4.4	2.9	0.9	0.1	1.3	1.2	-0.7	-0.1	0.7	-3.8
Financial Account (US$ million)	-6,748	2,230	10,084	2,523	995	-1,039	308	54	328	-945	442	-2,033
- Net Direct Investments, US$ million	958	-90	789	-122	-1,119	-1,030	-498	-1,829	-1,480	-1,868	-2,117	-2,646
- Net Portfolio Investments, US$ million	-3,205	-1,001	2,460	4,757	1,573	787	-843	-309	3,258	-129	875	-114
Overall BOP position (US$, million)	9,236	5,085	-2,858	2,616	-210	843	1,014	-2,068	-994	289	-662	505
Unemployment rate	7.0	7.1	6.8	6	5.8	5.4	4.7	4.7	6.6	5.6	5.7	5
Others	**Jan-17**	**Feb-17**	**Mar-17**	**Apr-17**	**May-17**	**Jun-17**	**Jul-17**	**Aug-17**	**Sep-17**	**Oct-17**	**Nov-17**	**Dec-17**
Overseas Filipinos' Remittances (US$, million)	2,169	2,169	2,615	2,083	2,310	2,467	2,283	2,499	2,186	2,275	2,262	2,741
… = not available												
Source: Bangko Sentral ng Pilipinas, Philippine Statistics Authority, Asian Development Bank.												

Source: Bangko Sentral ng Pilipinas, National Statistics Office, Asian Development Bank

Table 2. Level of Philippine GDP, 2016– 2017

	Nominal GDP (million current pesos)		Real GDP (million constant 2000 pesos)	
	2016	2017	2016	2017
Agriculture and Forestry	1,212,872	1,329,426	587,579	616,780
Fishing	185,191	197,228	123,347	122,249
Mining and Quarrying	114,330	134,514	83,106	86,222
Manufacturing	2,847,597	3,074,575	1,885,514	2,043,118
Construction	1,034,279	1,116,365	512,113	539,267
Electricity Gas and Water Supply	455,901	487,946	269,301	278,497
Transport Communication and Storage	909,269	962,540	611,902	636,577
Trade and Repair of Motor Vehicles Motorcycles Personal	2,652,835	2,919,613	1,367,438	1,467,855
Financial Intermediation	1,168,611	1,297,428	590,112	635,064
Real Estate Renting & Bus. Actvt	1,898,993	2,084,798	930,685	999,493
Public Administration & Defense: Compulsory Social Security	575,043	648,404	318,540	343,251
Other Services	1,425,023	1,553,521	843,105	897,335
Sum = GDP	14,479,945	15,806,359	8,122,741	8,665,708

Source: Philippine Statistical Authority, 2017

Table 3. Industry Contributions to Philippine GDP Growth, 2017

	TRAD GDP Growth (percent)	PGE (percent)	PCE (percent)	GEN GDP Growth (percent)
		(1)	(2)	(1)+(2)
GDP Growth	**6.68**	**6.69**	**0.03**	**6.68**
Industry Growth Contribution				
Agriculture	**0.35**	**0.40**	**0.24**	**0.65**
Agriculture and Forestry	0.36	0.42	0.18	0.60
Fishing	-0.01	-0.01	0.06	0.05
Industry	**2.43**	**2.16**	**-0.42**	**1.74**
Mining and Quarrying	0.04	0.03	0.09	0.12
Manufacturing	1.94	1.64	-0.56	1.09
Construction	0.33	0.38	0.01	0.39
Electricity Gas and Water Supply	0.11	0.11	0.04	0.14
Services	**3.91**	**4.12**	**0.17**	**4.29**
Transport Communication and Storage	0.30	0.25	-0.04	0.22
Trade & Repair of Motor Veh., Cycles, Personal, & House. Goods	1.24	1.35	0.04	1.39
Financial Intermediation	0.55	0.61	0.07	0.69
Real Estate Renting & Bus. Actvt	0.85	0.97	-0.01	0.96
Public Administration & Defense: Compulsory Social Security	0.30	0.31	0.10	0.41
Other Services	0.67	0.63	0.01	0.64

Source: DLSU-AKI Philippine Economic Monitor calculations by applying the data in Table 2 to a "generalized" (GEN) exactly addtive decomposition of GDP growth into pure growth effect (PGE) and price change effect (PCE) as an alternative to the "traditional" (TRAD) GDP growth decomposition. The GEN formulas for PGE and PCE and the TRAD formula are given, respectively, by equations (12), (13), and (17) in Dumagan, Jesus C. (2016), "Effects of Relative Prices on Contributions to the Level and Growth of Real GDP," Working Paper Series No. 2016-036, Angelo King Institute for Economic and Business Studies, De La Salle University, Manila. Analytically, PGE is the result of real GDP or "quantity" growth holding real price constant and PCE is the result of relative price or "real price" growth holding quantity constant. This alternative framework follows from the decomposition of "aggregate labor productivity" (ALP) growth in Dumagan, Jesus C. (2013), "A Generalized Exactly Additive Decomposition of Aggregate Labor Productivity Growth," Review of Income and Wealth, 59 (Issue 1): 157-168, where ALP is the ratio of GDP to total labor employment. Thus, by removing the labor variable, the decomposition of ALP growth in the latter paper yields the decomposition of GDP growth into PGE and PCE which is implemented in this Table 32.