

POLICY BRIEF

MONITORING THE PHILIPPINE ECONOMY

Volume VI No. 2, 2015

ISSN # 2094-3342



De La Salle University

AKI

Angelo King Institute
for Economic and Business Studies

MONITORING THE PHILIPPINE ECONOMY YEAR-END REPORT FOR 2014

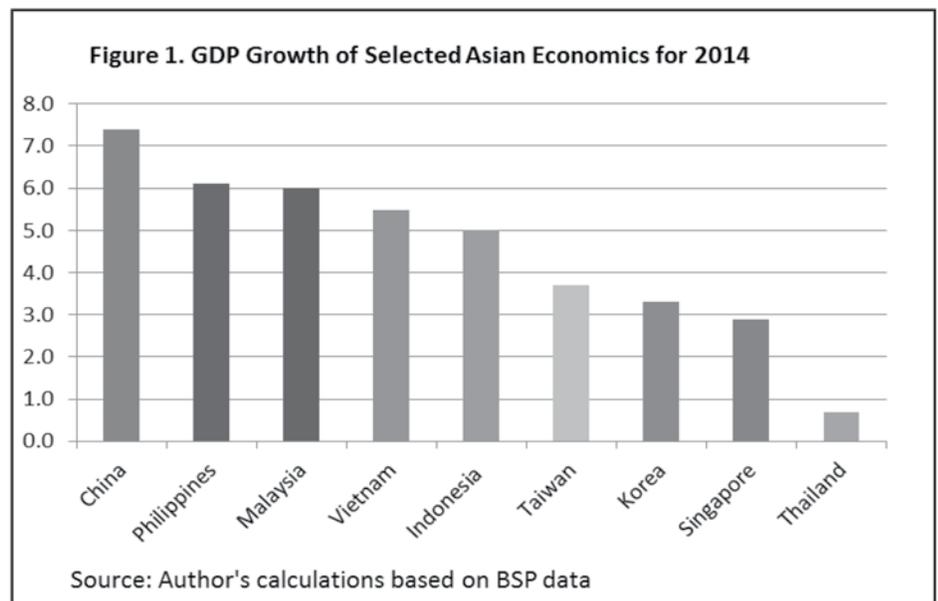
Despite doubts over growth prospects and challenges in the external market, the Philippine economy attained a solid 6.1 percent growth in 2014.

Economic performance: The upward trend in the demand side was driven by consumer spending and exports. The main growth factor for the supply side, on the other hand, was the service sector.

The Philippines maintains its growth momentum in 2014, besting other Asian economies. Favorable demand and supply side factors combined with improvements in the global market, particularly are covering US economy and intensifying demand in Asia, led to the 6.1 percent growth

in the country's Gross Domestic Product (GDP). A robust household consumption and strong construction subsector fueled the demand side. Moreover, external trade rallied owing to the deepening and strengthening of regional integration and a more stable US economy. Supply side factors include a dynamic service sector and a more resilient manufacturing sector. While domestic growth was lower than last year's 7.2 percent expansion rate, the country's performance bested most Asian economies (refer to Figure 1).

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¹Report is based on latest available data as of March 25, 2015. For comments and questions, please email mitzie.conchada@dlsu.edu.ph

MAJOR COMPONENTS OF AGGREGATE DEMAND

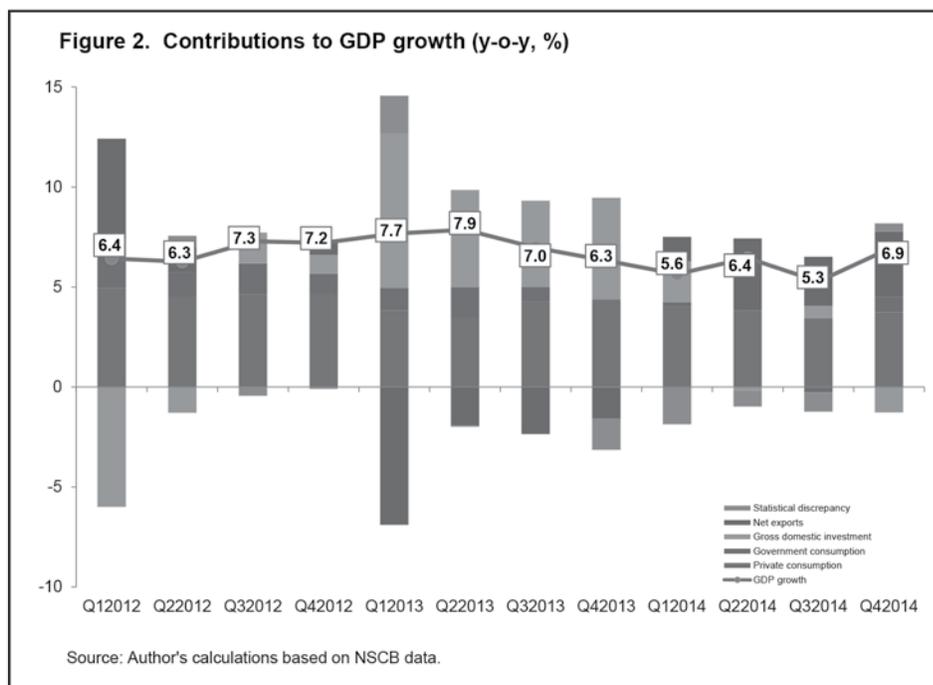
Private consumption slightly loses steam. Although household consumption still remains as the largest contributor to growth, the sector reported a slower expansion rate of 5.4 percent in 2014 – a tad below the previous year’s 5.7 percent. The top contributors to the growth of household consumption were food and non-alcoholic beverages (4.5 percent), utility expenses (5.4 percent), health expenses (10.5 percent), and transport related expenses (10 percent) (refer to Figure 2).

Domestic investment slows down due to weaker demand. Despite the notable performance of the construction and intellectual property subsectors, 10 percent and 10.1 percent in 2014, respectively, domestic investment dropped to a 1.1 percent growth from 2013’s 18.2 percent increase. The weak performance of the sector was accounted for by: the slowdown in durable equipment investments (8.7 percent growth relative to 2013’s 14.4 growth) and the contraction in miscellaneous equipment investments, particularly office machine and data processing (14.2 percent decline in the fourth quarter of 2014). Construction, however, rebounded as a result of a stronger private construction performance - 21.9 percent year-on-year (y-o-y) growth in the fourth quarter of 2014 (refer to Figure 2).

Solid fourth quarter performance yields lower deficit. The national government’s deficit was lower by 34.3 percent by the end of 2014. Government expenditure for the year increased to PhP1,981.7 billion. Revenues also rose to PhP1,908.5 billion, resulting in a reduction in the budget deficit from PhP111.5 billion in 2013 to PhP73.2 billion in 2014. The Bangko Sentral ng Pilipinas reported that the deficit was financed mainly from domestic sources.

Philippine exports remain strong; imports slow down. Export of goods grew by 15.9 percent in the fourth quarter of 2014- more than double that of 2013’s fourth quarter expansion rate of 6.2 percent. The main drivers of the upswing in exports were the rise in electric components (22.6 percent) and principal agricultural products (40.3 percent) foreign sales. Export of medical/industrial instrumentation (119 percent), control instrumentation (72 percent), office equipment (35 percent), and semiconductors (26.8 percent) topped the electronic components’ sales abroad. In addition, export of coconut oil, mango and

pineapple grew by 230, 138, and 24 percent, respectively. The export of fishery products such as shrimps and prawn and tuna, however, fell by 63.5 percent. Total export of goods for the fourth quarter, thus, amounted to PhP590 billion. Total import of goods went up by 3.6 percent; lower than 2013’s increase of 4.4 percent. The slower rate of imports is attributed to the contraction in the purchase of foreign-manufactured electronics (36.2 percent), ores and metal (98.5 percent), and transport equipment (36.9 percent). Net exports for the month of December were recorded at a deficit of USD68.4 million.



Philippines Economic Data												
Monthly Leading Indicators	Jan-14	Feb-14	Mar-14	Apr-14	May-14	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14
Industrial Production (y-o-y, %)	4.40	5.93	0.00	10.77	12.70	12.65	7.53	5.95	4.86	8.10	9.26	7.44
Consumer Price Index (y-o-y, %)	4.24	4.08	3.92	4.14	4.51	4.41	4.85	4.92	4.37	4.29	3.68	2.70
Exports (y-o-y, %)	9.18	24.49	21.95	1.32	6.85	21.31	12.92	19.49	15.68	2.47	19.73	-3.21
Imports (y-o-y, %)	24.66	1.70	10.62	3.82	-4.02	-1.41	0.16	0.84	-1.24	7.49	-10.79	-10.58
Trade Balance, US\$ million	-1,575.80	-131.00	-199.00	-784.00	423.00	626.00	-42.00	-137.00	201.00	-56.00	188.96	-68.39
Total Reserves (less gold), US\$ billion	71.63	72.21	71.64	71.83	72.45	72.45	72.63	72.82	71.99	72.10	71.45	72.06
Policy Rate	3.5	3.5	3.5	3.5	3.5	3.5	3.75	3.75	4	4	4	4
Fiscal Balance (million pesos)	-34,218	-9,718	-40,186	80,852	11,782	-62,486	-1,762	29,865	-5,198	-2,530	6,824	...
Quarterly/Annual Economic Indicators	2011	2012	2013	2014	1Q2013	2Q2013	3Q2013	4Q2013	1Q2014	2Q2014	3Q2014	4Q2014
Real GDP (y-o-y, %)	3.6	6.8	7.2	6.1	7.67	7.87	6.96	6.32	5.64	6.44	5.27	6.90
- Private Consumption	5.7	6.6	5.7	5.4	6.65	6.53	6.52	6.48	6.54	6.52	6.51	6.51
- Government Consumption	2.1	12.2	10.8	1.8	15.88	13.64	14.46	14.17	14.54	14.20	14.34	14.34
- Gross Capital Fixed Formation	2.0	-3.2	28.1	1.1	-5.55	-0.34	1.51	-0.08	-1.12	-0.01	0.08	0.08
Current Account (% of GDP)	2.3	2.8	4.2	4.4	5	3.8	5	5	2.3	4.4	4.8	5.9
Financial Account (US\$ million)	-5610	-6748	2230	10084	-655	835	1183	1585	4098	696	810	4,480
- Net Direct Investments, US\$ million	-1277	958	-90	789	-1336	502	-589	168	-487	-543	842	977
- Net Portfolio Investments, US\$ million	-4390	-3205	-1001	2460	-1697	-255	217	948	2811	-649	-903	1,202
Overall BOP position (US\$, million)	11400	9236	5085	-2858	1536	1041	1247	1260	-4475	330	712	574
Unemployment rate	7.4	7.0	7.1	6.8	7.1	7.5	7.3	6.5	7.5	7	6.7	6.0
Others	Jan-14	Feb-14	Mar-14	Apr-14	May-14	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14
Overseas Filipinos' Remittances (US\$, million)	1,804	1,800	1,888	1,918	1,984	2,054	2,068	2,057	2,110	2,228	2,122	2,317
... = not available												

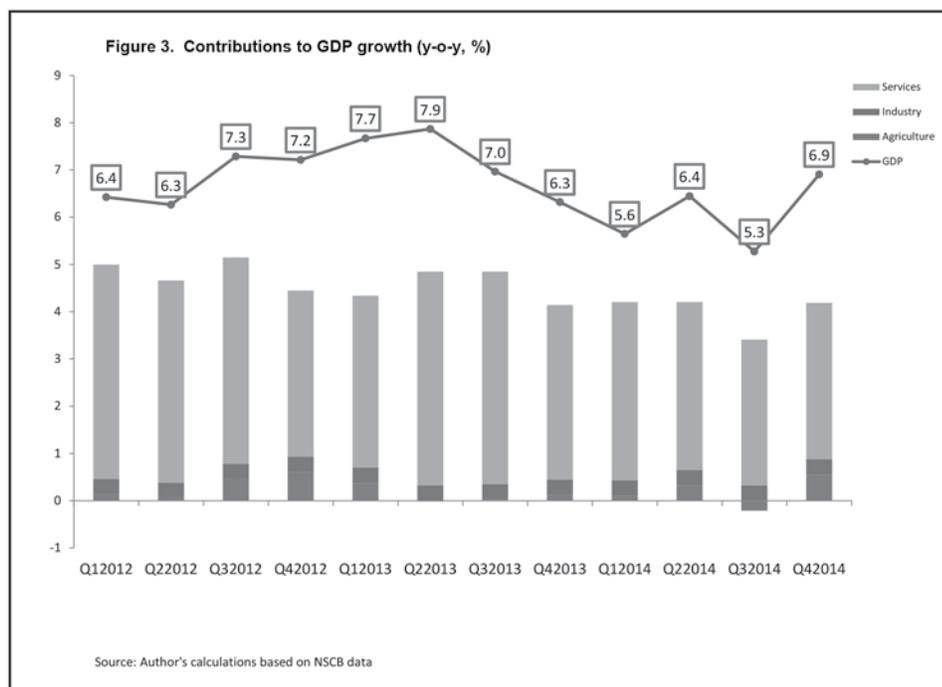
Source: Bangko Sentral ng Pilipinas, National Statistics Office, International Financial Statistics, IMF, Asian Development Bank.

MAJOR COMPONENTS OF AGGREGATE SUPPLY

Service sector remains as the main driver of supply-side growth. The service sector's contribution of 3.4 percent to the 2014 GDP growth was the highest among the components of aggregate supply. The sector's Gross Value Added (GVA) expansion rate, recorded at 6.0 percent, however, was lower than last year's 7.2 percent increase. The leading subsectors were public administration and defense (10.9 percent), real estate, renting and business activity (8.3 percent), and financial intermediation (6.6 percent).

Industry sector expansion powered by the manufacturing and construction subsectors. The industry sector remained strong with a 7.5 percent year-on-year growth, but weaker than 2013's 9.3 percent increase. The laudable performance of the sector was attributed to the upswing in the construction subsector, particularly private construction, which grew by 20.5 percent in the fourth quarter of 2014. The upsurge was fueled by higher demand in the local and international markets. Manufacturing GVA growth of 7.3 percent however, was lower than 2013's 12 percent growth owing to the slowdown in tobacco and wearing apparel manufactures.

Agriculture sector attains positive growth. The relatively robust performance of agriculture, hunting, forestry, and fishing industry by the end of 2014, 1.1 percent GVA growth, contributed 0.2 percent to the country's 6.1 percent GDP expansion. Despite unfavorable weather conditions throughout the year, the agriculture subsector managed to post a 2.3 percent growth at the end of 2014 with the help of higher productions of mango, cassava, and corn. Forestry GVA, however, contracted by 0.1 percent, a considerable drop from the previous year's growth of 37.3 percent.



Policy response

BSP Monetary Board (MB) makes adjustment on policy rates. After keeping key policy rates at 3.5 percent, the BSP Monetary Board decided during its July 31, 2014 meeting to increase the overnight RRP (borrowing) by 25 basis points to 3.75 percent. In September, the Monetary Board decided to again increase policy rates by 25 basis points to 4.00 percent. The MB assessed that the inflation environment has remained manageable despite the policy rates changes and predicted that the 2015 inflation rate would be lower at 3.7 percent.

Other economic news

Philippine remittances end strong in December. The Bangko Sentral ng Pilipinas (BSP) announced that cash remittances at the end of December 2014 amounted to USD24 billion, 5.4 percent higher than the same period last year. The boost in remittance was brought about by the increase in transfers from land-based workers employed in the United States, Saudi Arabia, and the United Arab Emirates. The proliferation of remittance centers and correspondent banks also contributed to the inflow of remittances.

Gross international reserves slacken by the end of December. A contraction in BSP's net foreign assets position resulted in a decline of 4.8 percent in the gross international reserves (less gold) at the end of December 2014; a significant change from the 3 percent growth in 2013.

Unemployment rate drops and improvements are seen in the labor market. The latest unemployment statistics revealed that the number of people who were unemployed in 2014 was lower than that of the previous year. The December 2014 Philippine Statistics Authority's Annual Labor and Employment report placed unemployment at 6.8 percent, less than last year's 7.2 percent. Per the Labor Force Survey, majority of the unemployed possessed the following characteristics: male (63.6%), high school graduate (33.2%), and between the ages of 15 to 24 years old (49.1%). Among the regions, the National Capital Region had the highest unemployment rate at 10.4%.

Inflation continues to stabilize because of lower petroleum prices. Average headline inflation for December 2014 was recorded at 2.7 percent, below last year's 4.1 percent. The deceleration in inflation rate was the effect of a drop in fuel prices. As of

December 14, the prevailing gasoline and diesel prices fell to PhP43.75 and PhP32.95, respectively, from an average of PhP49.25 and PhP37.45. An oversupply of oil pushed down world oil prices and slowed the rate of increase of basic commodities prices, especially in December.

Outlook on “hot money” inflow remains to be positive given a strong stock market performance. The bullish performance of the Philippine Stock market reached a new all-time high as the Philippine Stock Exchange index (PSEi) peaked at 7,230.57 by year-end December 29, 2014.

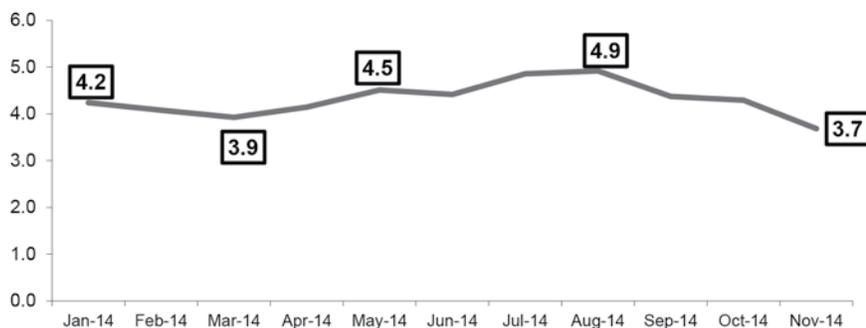
Domestic money supply maintains its positive growth. The Bangko Sentral ng Pilipinas (BSP) placed M3 growth at 9.6 percent in December 2014, higher than the previous month’s 9.2 percent expansion rate. Owing to the measures taken by the BSP to prevent excess liquidity in the financial system, the single digit growth, however, was lower as compared to that of the first half of the year.

Special report: Inflation reaches highest point at 4.9 percent

In July 2014, the change in Consumer Price Index reached a staggering 4.9 percent increase - the highest since October 2011 when inflation stood at 5.2 percent. Although the rise in the 2014 inflation rate was gradual (starting at 4.2 percent in January), it prompted the Bangko Sentral ng Pilipinas (BSP) to raise the overnight RRP (borrowing) rates to 4.00 percent in September for the purpose of controlling the rapid increases in prices. The sustained upward trend in headline inflation, according to the BSP, was primarily driven by the higher prices of food due to weather-related production disruptions and supply-side bottlenecks.

The escalation in prices was indeed halted by the end of 2014 with a recorded December inflation rate of 2.7 percent, the lowest since September 2013, via the tightening of policy rates and the sudden drop in petroleum prices.

Figure 4. Consumer price index (y-o-y, %)



.Source: Graph prepared by author based on NSCB data

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