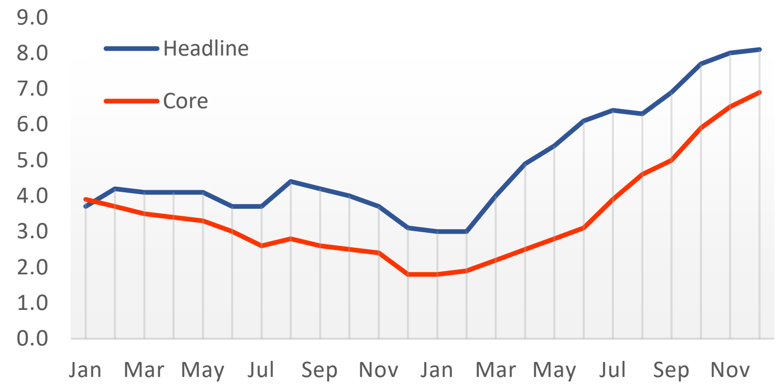
# Inflation in 2022
## *At A Glance*

**January 2023** **AAG-23-01**

*The average headline inflation for 2022 reached 5.8 percent, higher than the 3.9 percent posted in 2021 and well above the target range of 2.0 to 4.0 percent. Inflationary pressure mainly came from rising global oil prices, exacerbated by the simultaneous rise in commodity prices due to supply-side bottlenecks, coupled with the peso's depreciation. While the acceleration of inflation is evident across countries, the Philippines posted the highest inflation rate amongst the ASEAN member countries. This is expected to worsen the plight of low-income households and may have repercussions on the government's plan to reduce poverty. Inflation is expected to taper off in 2023 although upside risks remain. Likewise, monetary tightening that came as a response to curb inflation, is expected to drag economic growth.*

**Average headline inflation for 2022 reached 5.8 percent.** This is higher than the 3.9 percent inflation posted in 2021 and well above the Bangko Sentral ng Pilipinas (BSP) initial target range of 2.0 to 4.0 percent for 2022. The rapid acceleration of inflation in 2022 prompted the Monetary Board to adjust the inflation forecast thrice—from the original 2.0 to 4.0 percent in February to 5.0 percent in May and 5.4 percent in August and finally, to 5.8 percent in November.

Figure 1: Monthly Headline and Core Inflation (%)
January 2021 - December 2022




*Source: BSP*

**The inflation rate peaked in December 2022 at 8.1 percent, the highest since November 2008.** Inflationary pressure resulted from the increase in global oil prices, supply-side bottlenecks, as well as the peso's depreciation. Core inflation,[1] which excludes volatile energy and food prices, began rising in the latter half of the year, indicating second round effects.[2] It averaged at 3.9 percent, higher than the 3.0 percent in 2021. All in all, the purchasing power of the peso fell to PhP0.8674 in 2022. This means that products worth PhP100.00 in 2018 cost PhP113.26 in 2022.

**The increase in food prices accounted for more than a third of overall inflation.** The food index posted a year-on-year average inflation rate of 6.1 percent and contributed 2.1 percentage points to the 5.8 percent headline inflation. The heavily weighted cereal and cereal products which include rice, corn and flour were the foremost

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[1] Taking out the volatile items such as food and energy allows economists to see the broad underlying trend in consumer prices.

[2] Second round effects occur when inflation caused by supply-side factors persists, consequently prompting an increase in wages and transport fares.

inflation driver followed by meat and seafood prices. The prevalence of the African Swine Flu (ASF), the disruption in the global supply chain of feed wheat[3] as well as the fuel price hikes kept farmgate prices of pork elevated. Vegetable prices also surged upwards, particularly in the fourth quarter of 2022 when its inflation rate reached double-digits—from 3.5 percent in September to 32.4 percent in December. This is partly on account of the series of typhoons (e.g., Florita, Karding and Paeng) that hammered agricultural production. The accelerated rise in the price of red onion is noteworthy as its average retail price soared from PhP180.70 per kilo in December 2021 to PhP305.76 in December 2022, a 69 percent increase.[4] This stems largely from the insufficiency of supply as there was no importation of onion prior to the lean season when domestic production was at its lowest.

**Table 1: Average Inflation and Contribution to Inflation of Major Food Items, 2022**

| | Weights | Inflation | Contribution* |
|---|---|---|---|
| FOOD | 34.8 | 6.1 | 2.1 |
| Cereals and cereal products | 12.3 | 4.4 | 0.5 |
| Meat | 6.4 | 6.8 | 0.4 |
| Fish and other seafood | 5.7 | 6.7 | 0.4 |
| Milk, other dairy products, eggs | 2.9 | 4.5 | 0.1 |
| Vegetables, tubers, plantains, cooking bananas and pulses | 2.8 | 7.8 | 0.2 |
| Ready-made food, other food | 1.6 | 5.1 | 0.1 |
| Fruits and nuts | 1.5 | 0.7 | 0.0 |
| Sugar, confectionery, desserts | 1.0 | 18.9 | 0.2 |
| Oil and fats | 0.6 | 15.5 | 0.1 |

*Source: Philippine Statistics Authority (PSA)*
** SEPO Computation*

**More than half of overall inflation was driven by the non-food index.** The heavily weighted non-food consumer price index (CPI) contributed 3.4 ppt to the over-all inflation. Its housing and utilities[5] subcomponent accelerated by 6.4 percent, mainly due to upward adjustments in housing rental and electricity rates. Similarly, transport soared to a double-digit 12.9 percent inflation on the back of high global oil prices. Local transport groups petitioned for fare hikes which were eventually approved. The minimum base fare for traditional public utility jeepneys, for instance, was adjusted from PhP9.00 to PhP10.00 in June 2022, to PhP11.00 in July and finally to PhP12.00 in October. The rising prices of basic goods and services likewise prompted all 17 regional wage boards to approve the minimum wage hikes ranging from PhP30.00 to PhP110.00 in May and June. For the National Capital Region (NCR), the minimum daily wage was adjusted by PhP33.00 to PhP570.00. The biggest increment came from Region VI where daily wage was adjusted to PhP450.00, or an increase of PhP110.00. Core inflation hit 3.9 percent in July from 3.1 percent in June, a month after the wage hikes.

**Table 2: Average Inflation and Contribution to Inflation of Selected Non-Food Items, 2022**

| | Weights | Inflation | Contribution* |
|---|---|---|---|
| NON-FOOD | 60.1 | 5.7 | 3.4 |
| Actual rentals for housing | 12.8 | 2.4 | 0.3 |
| Electricity, Gas, Other Fuels | 6.7 | 15.8 | 1.1 |
| Electricity | 4.6 | 18.5 | 0.8 |
| Gas | 1.3 | 15.7 | 0.2 |
| Liquefied hydrocarbons | 1.3 | 15.7 | 0.2 |
| Operation of Personal Transport | 2.8 | 33.7 | 0.9 |
| Diesel | 0.6 | 65.4 | 0.4 |
| Gasoline | 1.8 | 31.2 | 0.6 |
| Passenger Transport Services | 4.5 | 5.5 | 0.2 |
| Passenger transport by road | 4.3 | 5.3 | 0.2 |
| Food and Beverage Services | 9.5 | 4.1 | 0.4 |

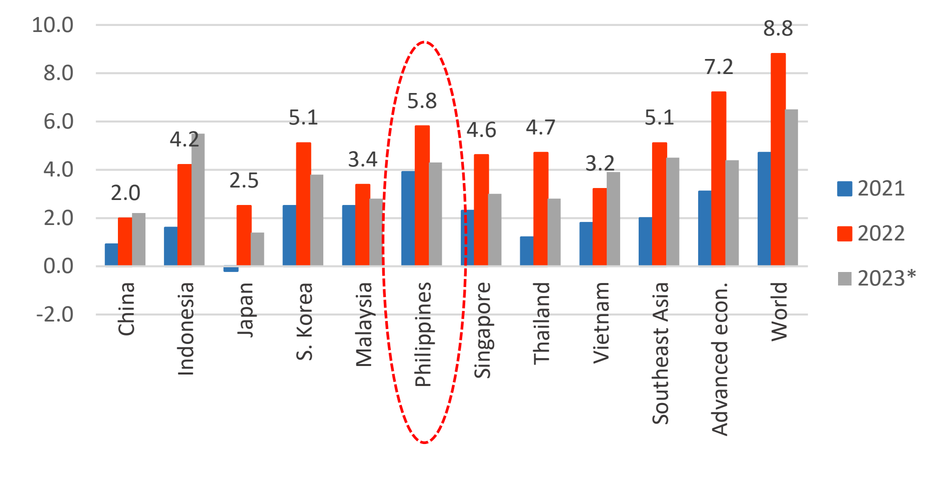
*Source: PSA*
** SEPO Computation*

[3] Both Russia and Ukraine are amongst the largest exporters of wheat globally.
[4] Data from PSA.
[5] This refers to the housing, water, electricity, gas and other fuels subcomponent and accounts for 21.4 percent of the CPI basket.

**The inflation for lower-income households increased to 5.3 percent in 2022 from 4.8 percent in 2021.** The inflation rate for the bottom 30% income group was slower compared to the 5.8 percent inflation experienced by the average household. This is partly due to the larger share of food to the total expenditure of poor families relative to non-food items.[6] Nonetheless, the acceleration of the inflation rate for the bottom 30% will exacerbate the plight of low-income households and undermine the government's goal of reducing poverty rates.

**While the issue of inflation is not unique to the Philippines, the country posted the highest inflation rate among the ASEAN economies.** Global inflation hit 8.8 percent in 2022 as countries emerged from lockdowns and face persistent supply chain disruptions, higher energy and food prices, and tight labor markets. Inflation was more pronounced among advanced economies particularly in the United States due to the large fiscal stimulus package it introduced to combat the impact of the pandemic. In Southeast Asia, inflation rose to 5.1 percent, more than double the 2.0 percent inflation registered in 2021. Among the ASEAN-6 countries, the Philippines' inflation rate was the highest.

Figure 2: Inflation rate, average consumer prices (%)




** Forecasts*
*Source: IMF*

**Inflation Outlook**

**For 2023, the Development Budget Coordination Committee (DBCC) expects inflation to gradually ease to 2.5 to 4.5 percent before returning to the target range of 2.0 to 4.0 percent in 2024.** This projection is aligned with the forecasts of multilateral agencies. Both the International Monetary Fund (IMF) and the Asian Development Bank (ADB) see the Philippine inflation rate hitting 4.3 percent this year. The BSP attributes the projected deceleration in inflation to three main factors—the expected easing in global oil and non-oil prices, the negative base effects from the transport fare adjustments in 2022, and the impact of BSP's cumulative policy rate adjustments. Note that the BSP's policy rate reached a 14-year high of 5.5 percent in 2022 after seven policy rate adjustments totaling to 3.5 percentage points. Analysts expect that this tightening cycle is likely to continue until at least the first half of 2023 as the BSP's rate decisions, like most central banks, are influenced to a certain extent by the action of the US Federal Reserve, which is likely to keep its policy rates elevated in the foreseeable future. BSP Governor Felipe Medalla has earlier expressed openness to pausing the current rate hike cycle by the second half of 2023 once the inflation moderates and the Philippine peso is stabilized.

**The weaker-than-expected global economic recovery may temper inflationary pressures but upside risks persist.** International development institutions have been sounding the alarm over the worsening external outlook. The World Bank has recently slashed its 2023 global economic growth forecast to 1.7 percent from its earlier projection of 3 percent. This would mark its third weakest growth profile since 2001, overshadowed

[6] The non-food index contributed 3.1 ppt to the over-all inflation while the food index contributed 2.1 ppt.

only by the recessions caused by the COVID-19 pandemic (2020) and the global financial crisis (2007-2008). The World Bank attributed the sluggish global growth to the "unexpectedly rapid and synchronous" monetary tightening around the world. The IMF has similarly warned that 2023 is going to be a tough year as most engines of global growth are experiencing weakening activity.

Nonetheless, upside risks to inflation remain. On the global front, these include continued supply chain challenges stemming from the continuing Russia-Ukraine conflict, droughts in parts of China and the US, as well as the pass-through from higher fertilizer prices. China's reopening of its economy, while good for growth may also stoke inflation. Demographic changes such as aging populations, re-shoring and friend shoring,[7] and *greenflation*[8] if kept unabated, may likewise provide unwelcome ballast to global inflationary pressures. Meanwhile, on the domestic front, the adverse effect of severe weather conditions, trade restrictions, the alleged presence of cartels, as well as pending petitions for transport fare and wage hikes, have been identified as upside risks to the inflation outlook.

**Inflation continues to be one of the biggest downside risks to Philippine economic growth in 2023.** The primary instrument by which the monetary authorities manage the inflation is through the interest rates. Higher interest rates encourage people to spend less and save more and in theory, this should reduce the demand for goods and services, and in turn, put downward pressure on prices. However, higher interest rate also means higher cost of borrowing which may slow the growth of consumption and investment, and ultimately, weaken the expansion of the domestic economy. For 2023, the DBCC is eyeing the gross domestic product (GDP) to grow between 6.0 to 7.0 percent, slightly lower than its 2022 target of 6.5 to 7.5 percent.

[7] While offshoring (manufacturing, logistics, distribution) was once seen as a way of reducing production costs, disruptions in global supply chains—caused by the lockdowns that came with the COVID-19 pandemic as well as trade tensions spurred by nationalism and protectionism—pushed nations to re-shore critical supply chains back to their home countries. However, not all supply chains can be re-shored mainly because some critical resources can only be found in one or two nations. Thus, the concept of friend shoring, which tries to fix supply chains by partnering with other nations and trusted suppliers, came about.

[8] Greenflation refers to the sharp rise in the prices of resources (particularly mineral resources) used in the production of renewable energy. In general, it is the price of the transition towards a more sustainable economy.