Economic Report

SENATE ECONOMIC PLANNING OFFICE

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2014 Mid-Year Report

Economy slows down, growth target in limbo

The lingering impact of typhoon Yolanda on agricultural production coupled with weak public sector consumption has contributed much to the deceleration of economic growth for the first nine months of the year. Growing by an average of 5.8 percent for the first three quarters of the year, it is unlikely that actual growth in 2014 will hit the low-end target of 6.5 percent. Nonetheless, employment figures exhibited positive developments and business sentiment remained positive.

I. Introduction

The Philippines' gross domestic product (GDP) grew 5.3 percent in real terms during the third quarter of 2014, much slower than the 7.0 percent growth recorded in the same period in 2013. This brings the average GDP growth rate at a 5.8 percent for the first nine months of 2014. Full-year growth target is 6.5 to 7.5 percent.

The expansion of the country's domestic economy surpassed those of its neighbors in Southeast Asia (SEA) with the exception of Vietnam, which grew by 6.19 percent in the third quarter. The third quarter growth figure marked the economy's weakest phase in almost three years (eight consecutive quarters of above 6.0 percent growth in 2012 thru 2013).

Real GDP Growth in SEA countries, 3rd Quarter 2014

China	1.90
Indonesia	3. 16
Malaysia	0.90
Philippines	5.30
Singapore	3.10
Thailand	1.10
Vietnam	6.19

Source: http://www.tradingeconomics.com

The SEPO Economic Report, a semi-annual publication of the Senate Economic Planning Office, provides useful information on the current state of the economy to the Senators and Senate Officials. The SEPO Economic Report is also available at www.senate.gov.ph.

Growth in demand was fuelled by net exports which grew by 125.7 percent and contributed 2.1 percentage points (ppts) to economic growth in the third quarter. Household consumption grew by 5.2 percent year-on-year, decelerating from the 6.2 percent growth it registered during the same period last year. Investment slightly grew by 3.6 percent in the third quarter with fixed capital formation growing robustly for intellectual property products at 35.1 percent and private construction at 15.7 percent. Government consumption continued to act as a drag, posting a negative 2.6 percent growth rate. The slack in state spending is attributed to delays in the submission of reportorial requirements and adjustments to new spending protocols.

Growth in production was still mainly driven by the services sector which grew by 5.4 percent, and contributed 3.1 ppts to GDP growth. However, the expansion of services slowed down compared to the 7.7 percent growth it registered in the third quarter of 2013. Industry contributed 2.4 ppts to economic growth with the manufacturing sub-sector growing robustly by 7.2 percent. Food manufacturing, beverage industries, petroleum and other fuel products, fabricated metal products, as well as transport equipment, contributed to growth in manufacturing. Demand for these manufactures came from both domestic and external markets. The faster pace of growth of the mining and construction sub-sectors also supported the

GDP Growth Rates, 2013 and 2014 (At Constant 2000 Prices)

	2013				2014		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
GROSS NATIONAL INCOME	7.3	7.9	7.0	6.3	5.6	6.4	4.8
GROSS DOMESTIC PRODUCT	7.7	7.9	7.0	6.3	5.6	6.4	5.3
Agriculture, Hunting, Forestry and Fishing	3.2	-0.2	0.3	0.9	0.9	3.6	-2.7
Agriculture and Forestry	2.6	-0.9	0.3	2.3	1.7	4.6	-3.3
Fishing	5.8	3.3	0.5	-4.4	-3.1	-0.7	-0.4
Industry	11.3	10.5	7.7	7.6	5.3	7.8	7.6
Mining and Quarrying	2.1	0.3	5.0	-2.5	9.0	1.9	7.8
Manufacturing	9.5	10.3	8.9	12.0	6.9	10.8	7.2
Construction	31.1	16.6	3.4	-5.2	0.2	1.4	11.9
Electricity, Gas and Water Supply	0.6	7.0	8.4	3.0	1.0	2.8	3.3
Services	6.5	7.8	7.7	6.7	6.8	6.0	5.4
Transport, Storage and Communication	1.4	6.6	6.3	8.1	7.7	6.3	5.3
Trade and Repair of Motor Vehicles, Motorcycles, and Personal and Household Goods	4.2	6.3	5.6	6.4	6.0	6.6	6.1
Financial Intermediation	18.0	10.3	12.1	10.7	5.7	5.9	7.7
Real Estate, Renting and Business Activities	5.8	9.5	11.6	7.6	9.5	8.9	6.2
Public Administration and Defence; Compulsory Social Security	5.3	5.9	6.0	-2.3	6.3	1.2	-2.9
Other Services	7.6	8.3	6.3	6.4	5.5	4.1	5.2
Household Consumption Expenditure	5.5	5.1	6.2	5.9	5.9	5.3	5.2
Government Consumption Expenditure	10.0	12.1	7.0	-0.4	1.9	0.0	-2.6
Capital Formation	49.8	33.6	21.6	22.4	9.5	-2.4	3.6
Fixed Capital	17.3	13.6	9.5	8.0	11.0	4.0	10.1
Construction	33.9	16.5	3.9	-4.3	-1.3	5.1	12.3
Durable Equipment	10.4	13.2	15.4	23.2	22.7	2.3	8.1
Breeding Stock and Orchad Development	0.6	-1.0	-0.9	-12.1	-4.4	-2.0	-1.2
Intellectual Propery Products	7.4	13.8	13.1	28.3	-5.1	35.9	35.1
Exports	-10.6	-7.7	12.4	3.2	13.5	10.3	9.8
Export of Goods	-8.9	-8.8	13.7	6.2	14.2	10.0	9.8
Export of Services	-16.4	-3.2	6.4	-6.7	11.1	11.7	9.9
Less: Imports	2.8	-4.6	17.3	6.4	10.1	1.4	5.8
Import of Goods	2.1	-6.1	16.7	4.4	7.5	-3.9	3.4
Import of Services	5.3	3.1	19.9	12.8	19.2	26.2	15.9

Source: National Statistics Coordination Board (NCSB) growth of industry. On the other hand, the agriculture, fishery, and forestry sector registered a 2.7 percent fall in output on account of the disruption brought by typhoons Glenda and Luis on palay and poultry production. The scale insect infestation likewise adversely affected coconut farms in the Visayas.

Fiscal position posted a deficit amounting to PhP31.1 billion for the first three quarters of 2014, PhP204.4 billion lower than the programmed. The low deficit was mainly on account of sluggish state spending. Expenditures from January to September 2014 was PhP273.8 billion lower than programmed. Revenues on the other hand, grew by 12.5 percent during the same period. Tax collection by the Bureau of Customs, in particular, showed an 18.3 percent increase, which is attributed to an improvement in the valuation of goods following the appointment of a new commissioner. Likewise, the Treasury's interest income exceeded the programmed amount by PhP36.7 billion. Despite these gains however, actual total revenues fell short of the target by PhP69.4 billion.

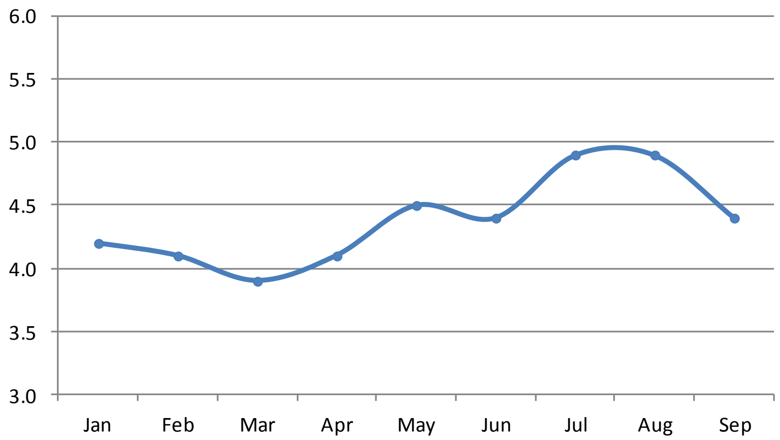
Fiscal Position (in PhP billion)

Particulars	Jan–Sept 2013	Jan–Sept 2014		Variance	Growth (%)
	Actual	Program	Actual		
REVENUES	1,266.6	1,494.4	1,425.0	(69.4)	12.5
Tax Revenues	1,134.1	1,391.1	1,273.8	(117.3)	12.3
Bureau of Internal	898.0	1,076.8	996.3	(80.4)	11.0
Bureau of Customs	224.6	302.0	265.8	(36.2)	18.3
Other Offices	11.5	12.3	11.6	(0.8)	0.8
Non-Tax Revenues	132.4	103.3	151.1	47.7	14.1
o/w Treasury Income	68.1	44.6	81.3	36.7	19.3
EXPENDITURES	1,367.4	1,729.8	1,456.1	(273.8)	6.5
SURPLUS/(DEFICIT)	**(100.8)**	**(235.5)**	**(31.1)**	**204.4**	**(69.2)**

Source: Bureau of Treasury (BTr)

Inflation continued its upward trend with headline inflation reaching 4.6 percent in the third quarter, higher than the 4.4 percent recorded in the previous quarter and the 2.4 percent in the third quarter of 2013. The upward trend is attributed to rising food prices due to tight supply conditions. Non-food inflation on the other hand, registered a decrease from 2.6 percent in the second quarter to 2.4 percent in the third quarter. Favorable US supply inventories have helped stabilize world oil prices, which in turn, slowed price increases for domestic electricity, gas, and other petroleum products. Inflation expectations are still broadly stable and will likely remain within target.

Headline Inflation, Jan–Sept 2014



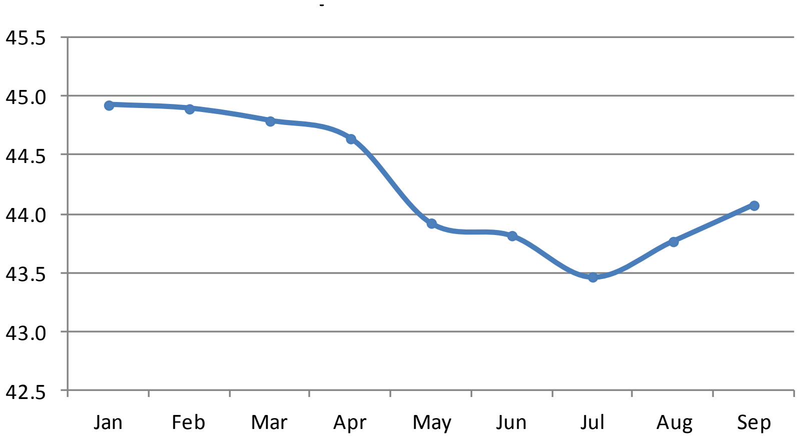
Source: BSP

Key policy rates were raised by 25 basis points last September 2014 on account of elevated inflation pressures. Overnight borrowing (RRP) and overnight lending (RP) went up to 4.0 percent and 6.0 percent, respectively. Reserve requirements however, were left unchanged. Inflation outlook is leaning on the upside given the uptick in food prices and the pending petitions for upward adjustment of utility rates. Thus, the Monetary Board deemed it prudent to rein in inflation expectations and preempt potential second-round effects.

Balance of payment position (BOP) for the first half of 2014 registered a deficit of US$4.1 billion, a reversal of the US$2.6 billion surplus it posted in the same period in 2013. Weaker balance of trade-in-goods and services led to the decline in the current account from US$4.4 billion in the first half of 2013 to US$3.9 billion in the same period in 2014. Likewise, a reversal in portfolio investments caused the significant outflow in the financial account from US$709 million in 2013 to US$4.6 billion in 2014. On the other hand, foreign direct investments continue to post net inflows for the 13th consecutive month in July 2014.

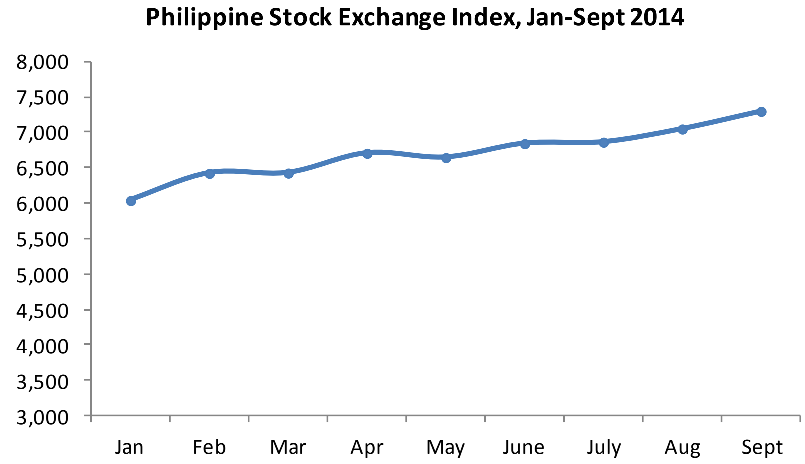
Philippine Peso-US Dollar exchange rate is expected to weaken in light of higher import demand. Economic managers adjusted import growth forecast from 6.0 percent to 9.0 percent in 2014. The depreciation of the peso is consistent with the movement of other regional currencies against the US dollar following the US Federal Reserve's (US Fed) higher rate projections for 2015. The target range for the peso-dollar exchange rate for 2014-2016 was adjusted from PhP41.00-PhP44.00 to PhP42.00-PhP45.00.

Peso per US Dollar Rate, Jan-Sept 2014



Source: BSP

Stock market performance was bullish as the Philippine Stock Exchange Index reached a record-breaking level of 7,414 points last September 2014. This came even after the US Fed announced tapering its quantitative easing program in 2013. Value traded increased by 23.7 percent in the first nine months of the year. Some repositioning is expected ahead of the release of third quarter earnings on the early part of the fourth quarter.



Source: PSE

Unemployment rate is at its lowest level in ten years with the October 2014 round of the Labor Force Survey (LFS) showing the jobless rate at 6.0 percent. Data for labor force participation rate from October 2013 to 2014 indicate that the labor market grew to around 41.3 million individuals, 925,000 of whom are new labor entrants. The number of employed increased by 2.8 percent year-on-year from 37.8 million to 38.8 million. The services sector continues to absorb the bulk of the employed, accounting for 53.7 percent of employed workers. However, underemployment rose to 18.7 percent with approximately 7.3 million workers wanting more work. This indicates that raising the quality of employment remains to be a challenge.

Labor Statistics, Oct 2013-Oct 2014

Period	Labor Force Participation Rate	Employment Rate	Unemployment Rate	Underemployment Rate
Oct 2013	63.9	93.5	6.5	17.9
Jan 2014	63.8	92.5	7.5	19.5
Apr 2014	65.2	93.0	7.0	18.2
Jul 2014	64.2	93.3	6.7	18.3
Oct 2014	64.3	94.0	6.0	18.7

Source: BLES

II. Outlook and Risks

The lingering impact of typhoon Yolanda on agricultural production coupled with weak public sector consumption has contributed much to the deceleration of economic growth for the first nine months of the year. The increase in the prices of basic commodities as well as the higher costs of raw materials and utilities have likewise resulted in lower consumer spending. Port congestion issues also contributed to a slowdown in business activities.

Growing by an average of 5.8 percent for the first three quarters of the year, it is unlikely that actual growth in 2014 will hit the low-end target of 6.5 percent. In its mid-year update, the Asian Development Bank revised its outlook for the Philippines from 6.4 percent to 6.2 percent. The World Bank also downgraded the country’s prospects from 6.6 percent to 6.4 percent.

Nonetheless, business sentiment remains optimistic, although less sanguine. A brisk business environment and an increase in consumer spending is expected in the fourth quarter, which is likewise expected to bring expansion in the retail, power and telecommunications sector. Recovery in global markets should bring higher export demand particularly for semiconductors, transport, garments and metal. Steady growth of overseas Filipino workers (OFW) remittances in addition to favorable macroeconomic conditions will continue to buttress economic growth.

The resolve to deal with domestic reform lags must be strengthened to sustain the growth momentum. For instance, the introduction of reforms in tax administration is critical if the government is bent on increasing public spending on infrastructure, health and education services. Likewise, measures that would improve the investment climate and revive manufacturing industries should be continued in an effort to accelerate job creation.

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This Economic Report was prepared by Macroeconomics Sector Head Maria Kathreena D. Tan and Myrna E. Diana under the supervision of the SEPO Directors and the overall guidance of its Director General.