BANGKO SENTRAL NG PILIPINAS

HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 14 FEBRUARY 2024 [1]

I. Monetary Policy Decision

The Monetary Board decided to:

a) Maintain the current policy interest rate at 6.50 percent for the Target RRP Rate; and

b) Maintain the current interest rates on the overnight deposit facility at 6.00 percent and overnight lending facility at 7.00 percent.

II. Key Considerations in the Formulation of the Monetary Policy Stance

- Based on new information and its latest assessment of the impact of prior monetary policy adjustments, the Monetary Board decided to maintain the current monetary policy settings of the BSP. The Monetary Board deemed it appropriate to keep the BSP's monetary policy settings unchanged in the near term amid the improvement in inflation conditions while taking into consideration the prevailing risks to the inflation outlook.

- The Monetary Board noted that the outlook for inflation was broadly unchanged. The latest risk-adjusted inflation forecast for 2024 eased to 3.9 percent from 4.2 percent in the previous meeting in December. For 2025, the risk-adjusted inflation forecast is relatively steady at 3.5 percent from 3.4 percent. Equally important, the BSP's latest survey of external forecasters shows inflation expectations to be more firmly anchored, with mean forecasts remaining within the target range for both 2024 and 2025.

- Meanwhile, the risks to the inflation outlook have receded but remain tilted toward the upside. The upside risks to the inflation forecasts are linked mainly to higher transport charges, increased electricity rates, higher oil and domestic food prices, and the additional impact on food prices of a strong El Niño episode. On the other hand, the implementation of government measures to mitigate the impact of El Niño weather conditions is the primary downside risk to the outlook.

- Given the salience of rice prices to domestic inflation, the Monetary Board viewed the NG's recent agreement with Vietnam to secure rice supply over the next five years to be favorable. Moreover, the NG's efforts to increase

[1] The discussions herein reflect the assessment made by the Monetary Board based on macroeconomic and financial information available at the time of the monetary policy meeting. The next meeting of the Monetary Board on the monetary policy stance is scheduled on 4 April 2024.

productivity in the rice sector, including the distribution of drought-resistant seeds, are seen as a step in the right direction.

- On domestic economic activity, the Monetary Board noted the sustained expansion in output in Q4 2023 which reaffirmed the BSP's view that the country's growth momentum remains intact over the medium term. However, recent indicators also suggested that economic activity could moderate in the near term as the full impact of the BSP's prior monetary policy tightening continues to manifest.

- In consideration of the prevailing risks, the Monetary Board deems it appropriate to keep the BSP's monetary policy settings unchanged in the near term amid the improvement in inflation conditions. The BSP also continues to support the National Government's non-monetary measures to address supply-side pressures on prices and sustain the disinflation process. The Monetary Board stands ready to adjust monetary policy settings as necessary in keeping with its primary mandate to safeguard price stability.

III. Recent Developments and Inflation Outlook

In assessing the monetary policy stance, the Monetary Board considered the latest macroeconomic and financial developments as discussed below:

A. Domestic price conditions

- Headline inflation slowed further to 2.8 percent year-on-year (y-o-y) in January 2024 from 3.9 percent in December 2023. The downtrend in overall inflation was due mainly to the slower price increases in most food commodities. However, rice inflation increased further to 22.6 percent in January 2024 (from 19.6 percent in December 2023) due mainly to higher import prices and the El Niño impact on global and regional output. Non-food inflation also decelerated because of slower price increases of housing, water, electricity, gas and other fuels particularly, rent and power rates. Transport inflation also declined due to lower gasoline and diesel prices, along with easing inflation for sea fares. In addition, the official core inflation further slowed down to 3.8 percent in January 2024 from 4.4 percent in December 2023. Likewise, alternative measures of core inflation including trimmed mean and weighted median further moderated in January 2024.

B. Inflation expectations

- Results of the BSP's survey of external forecasters for February 2024 showed unchanged mean inflation forecast for 2024 at 3.9 percent as well as for 2026 at 3.4 percent relative to the forecasts in the January 2024 survey round. By contrast, the mean inflation forecast for 2025 rose to 3.5 percent from 3.4 percent. Analysts expected inflation to remain manageable in 2024 and settle within the target range. However, analysts also anticipate that the risks to the inflation outlook will continue to be dominated by upside pressures owing to supply-side shocks and second-round effects.

C. Inflation outlook

- The risks to the inflation outlook continue to be primarily skewed to the upside for 2024 to 2025, even as the risk-adjusted forecasts are now within the BSP's inflation target range. The upside risks to the inflation outlook could emanate from increased electricity rates; higher transport charges; higher global oil prices; higher prices of food commodities facing supply constraints; and higher rice prices owing to stronger El Niño and further weather disturbances as well as higher global prices. Meanwhile, successful implementation of government measures to mitigate the impact of El Niño weather conditions is the primary downside risk to the outlook.

- The latest staff risk-adjusted inflation forecast is estimated at 3.9 percent for 2024 (from 4.2 percent in the previous forecast round) and 3.5 percent in 2025 (from 3.4 percent). The downward revision in the risk-adjusted forecast for 2024 is attributed primarily to the decline in the estimated risks along with the decrease in the baseline forecast for the year. The lower estimated impact of risks emanated from the removal of the impact of higher transport fares from the jeepney modernization; the lower probability of fare hikes for traditional jeepneys; the lower impact of higher global oil prices; and the removal of the risk from the non-extension of Executive Order (E.O.) No. 10. Meanwhile, the risk-adjusted forecast for 2025 is higher due mainly to the shift in the assumed implementation of higher electricity rates.

D. Demand conditions

- The Philippine economy grew by 5.6 percent year-on-year in Q4 2023, slower than the 6.0 percent growth posted in the previous quarter and 7.1-percent growth in the same period a year ago. This brought the full year 2023 real GDP growth to 5.6 percent, which is below the government target of 6.0 to 7.0 percent GDP growth for the year. On a seasonally adjusted basis, quarter-on-quarter GDP growth slowed down to 2.1 percent in Q4 2023 from 3.8 percent in the previous quarter. GDP growth in Q4 2023 was mainly driven by strong household spending and investments but was tempered by slower government spending and weak external trade.

- The country's output growth prospects for 2024 and 2025 remain intact despite global headwinds and tighter financial conditions. Philippine GDP growth estimates by the BSP for 2024 and 2025 have been adjusted upwards from the previous forecast round due to the improved outlook in global economic activity and the decline in crude oil prices which offset the lower-than-expected GDP outturn in Q4 2023. However, domestic economic activity is seen to decelerate in the second semester of 2024, reflecting the impact of policy rate hikes, before picking up again in 2025.

E. Supply-side indicators

Developments in Agriculture

- Agriculture, Forestry, and Fishing (AFF) posted a growth of 1.4 percent in Q4 2023, faster than the 0.9-percent growth in Q3 2023, and a reversal of the 0.3 percent contraction in Q4 2022.68. Cumulative growth of the AFF sector was recorded at 1.2 percent for 2023, higher than the 2022 outturn of 0.5 percent. Higher AFF output in Q4 2023 was attributed mainly to the positive contribution of poultry, egg, livestock, other animal production, sugarcane, and support activities to AFF, which more than compensated for the lower output in fishing and aquaculture, corn, coconut, rubber, cassava, and other agricultural crops production.

- Nationwide average retail rice prices continued to increase in January 2024 after falling during the start of the peak harvest season in October 2023. Rice prices further increased in January as import prices remained high due to rice export bans and worries over potential impact of El Niño on global and regional output.

- Based on the assessment of weather conditions by the US Climate Prediction Center and International Research Institute for Climate and Society (CPC/IRI) as of 11 January 2024, prevailing El Niño conditions will likely continue in the coming months before transitioning to El Niño Southern Oscillation (ENSO)-neutral by April to June 2024. Similarly, according to PAGASA's climate outlook as of 24 January 2024, a strong and mature El Niño is present and is expected to gradually weaken in the coming months. In addition, most climate models predict that the current El Niño episode will likely persist until the March-April-May 2024 season. Nonetheless, El Niño increases the likelihood of way-below to below-normal rainfall conditions which could occur within the first semester of 2024.

Oil Price Developments

- The spot price of Dubai crude oil slightly increased in the first week of February 2024 compared to the full-month average price in January 2024. The rise in world oil prices was driven primarily by fears of possible supply disruptions due to the on-going geopolitical tensions in the Middle East; the continued disputes in the Red Sea; and Ukraine's attacks on Russian oil facilities. The uptick in oil prices was partly tempered by possible ceasefire between Israel and Hamas. On the demand side, the worsening real estate situation in China as well as the continued contraction in Chinese manufacturing activity in January 2024, and high global interest rate environment, also counterbalanced the increase in oil prices.

Developments in the Utilities Sector

- Retail electricity rates went up in February 2024 relative to January 2024 rates, reflecting increased generation charges due to higher power costs from Independent Power Producers (IPPs) and Power Supply Agreements (PSAs). Charges from IPPs rose due to higher fuel costs resulting from the increased use of imported liquefied natural gas (LNG), which was more expensive than Malampaya gas. Charges from PSAs also increased due to higher costs from Emergency Power Supply Agreements (EPSAs). Furthermore, the depreciation of the peso also contributed to higher charges from IPPs and PSAs.

F. Financial market developments

- The peso depreciated by 0.13 percent to an average of ₱56.09/US$1 for the period 1-12 February 2024 relative to the previous month's average. The weakening of the peso partly reflected US dollar strength amid expectations of delay in the US Fed's policy easing as well as lingering geopolitical tensions in Gaza and the Middle East. On the domestic front, dampened market sentiment amid elevated inflation outlook in Q2 2024, and lower Gross International Reserves (GIR) in January contributed to the depreciation of the peso. Nonetheless, these factors were partly offset by the following positive domestic developments: i) stronger-than-expected Q4 and full-year 2023 GDP growth; ii) hawkish statement from the central bank; iii) sustained growth in the country's manufacturing activity in January; iv) lower government debt-to-GDP ratio in 2023; and v) stronger net FDI inflows in November 2023.

- On a year-to-date basis, the peso closed at ₱56.01/US$1 on 12 February 2024, depreciating by 1.13 percent against the US dollar from the end-December 2023 closing rate of ₱55.37/US$.

G. Liquidity and credit conditions

- Preliminary data showed that outstanding loans of universal and commercial banks, net of RRP placements with the BSP increased by 7.0 percent y-o-y in December, the same rate of increase as in November. Bank lending activity has continued to grow at a single-digit rate, reflecting the impact of the BSP's tight monetary policy. Nonetheless, banks anticipate sustained demand for credit from both corporate and household sectors in the near term.

H. Fiscal developments

- National Government (NG) spending, which amounted to about ₱4.7 trillion in January-November 2023, increased to 89.4 percent of the full-year (FY) 2023 expenditure program from 81.1 percent share in January-October 2023. NG spending also expanded by 3.6 percent y-o-y in January-November 2023, buoyed by the higher NG disbursements for infrastructure and other capital outlays (IOCO); personnel services (PS); maintenance and other operating expenses (MOOE); and interest payments. Meanwhile, other expenditure items declined.

- As revenue growth outpaced the percentage increase in expenditures, the ₱1.1-trillion NG deficit in January-November 2023 is 10.1 percent narrower than the deficit in the same period in 2022 and is 74.1 percent of the FY 2023 deficit program. Netting out the interest payments in NG expenditures, the primary deficit amounted to ₱543.5 billion, 30.0 percent lower than the deficit recorded in 2022.

I. External developments

- Prospects for global economic growth improved as downside risks to economic activity recede. In the January 2024 World Economic Outlook (WEO), the International Monetary Fund (IMF) raised its 2024 global economic growth projection to 3.1 percent, reflecting the greater-than-expected resilience in the US and several large emerging market and developing economies (EMDEs), as well as fiscal support in China. Nonetheless, global economic expansion is expected to remain well below the annual average of 3.8 percent until at least 2025 with elevated central bank policy rates to fight inflation, a withdrawal of fiscal support and high debt weighing on economic activity, as well as low underlying productivity growth. With the likelihood of a hard landing receding as adverse supply shocks unwind, the risks to the global outlook are broadly balanced.

Additional details on the key factors behind the monetary policy decision of the BSP can be found in the February 2024 Monetary Policy Report (Link: [Bangko Sentral ng Pilipinas Price Stability (bsp.gov.ph)](bsp.gov.ph))
