Q4 | INFLATION REPORT

2020
FOURTH QUARTER

Foreword

The primary objective of monetary policy is to promote a low and stable rate of inflation conducive to a balanced and sustainable economic growth. The adoption in January 2002 of the inflation targeting framework for monetary policy was aimed at helping to fulfill this objective.

One of the key features of inflation targeting is greater transparency, which means greater disclosure and communication by the BSP of its policy actions and decisions. This Inflation Report is published by the BSP as part of its transparency mechanisms under inflation targeting. The objectives of this Inflation Report are: (i) to identify the risks to price stability and discuss their implications for monetary policy; and (ii) to document the economic analysis behind the formulation of monetary policy and convey to the public the overall thinking behind the BSP's decisions on monetary policy. The broad aim is to make monetary policy easier for the public to understand and enable them to better monitor the BSP's commitment to the inflation target, thereby helping both in anchoring inflation expectations and encouraging informed debate on monetary policy issues.

The government's target for annual headline inflation under the inflation targeting framework has been set at 3.0 percent ± 1.0 percentage point (ppt) for 2020-2022 by the Development Budget Coordination Committee. This is consistent with the desired disinflation path over the medium term, favorable trends in inflation dynamics, and expected higher capacity of the economy for growth under a low inflation environment.

The report is published on a quarterly basis, presenting an analysis of the various factors affecting inflation. These include recent price and cost developments, inflation expectations, prospects for aggregate demand and output, labor market conditions, monetary and financial market conditions, fiscal developments, and the international environment. An entire section is devoted to a discussion of monetary policy developments in the most recent quarter, while a separate section provides a comprehensive analysis of the BSP's view of the inflation outlook for the policy horizon.

The Monetary Board approved this Inflation Report at its meeting on 14 January 2021.

BENJAMIN E. DIOKNO
Governor

The Monetary Policy of the Bangko Sentral ng Pilipinas

The BSP Mandate

The BSP's main responsibility is to formulate and implement policy in the areas of money, banking and credit, with the primary objective of maintaining stable prices conducive to a balanced and sustainable economic growth in the Philippines. The BSP also aims to promote and preserve monetary stability and the convertibility of the national currency.

Monetary Policy Instruments

The BSP's primary monetary policy instrument is its overnight reverse repurchase (RRP) or borrowing rate. Other instruments to implement the desired monetary policy stance to achieve the inflation target include (a) increasing/decreasing the reserve requirement (RR); (b) conducting auctions for the term deposit facility (TDF);[1] (c) adjusting the rediscount rate on loans extended to banking institutions on a short-term basis against eligible collateral of banks' borrowers; and (d) outright sales/purchases of the BSP's holdings of government securities.

Policy Target

The BSP's target for monetary policy uses the Consumer Price Index (CPI) or headline inflation rate, which is compiled and released to the public by the Philippine Statistics Authority (PSA). The policy target is set by the Development Budget Coordination Committee (DBCC)[2] in consultation with the BSP. The inflation target for 2020-2022 is 3.0 percent ± 1.0 ppt.[3]

BSP's Explanation Clauses

These are the predefined set of acceptable circumstances under which an inflation-targeting central bank may fail to achieve its inflation target. These clauses reflect the fact that there are limits to the effectiveness of monetary policy and that deviations from the inflation target may sometimes occur because of factors beyond the control of the central bank. Under the inflation targeting framework of the BSP, these exemptions include inflation pressures arising from: (a) volatility in the prices of agricultural products; (b) natural calamities or events that affect a major part of the economy; (c) volatility in the prices of oil products; and (d) significant government policy changes that directly affect prices such as changes in the tax structure, incentives, and subsidies.

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[1] The TDF was introduced under the interest rate corridor (IRC) system which was implemented on 3 June 2016.

[2] The DBCC, created under Executive Order No. 232 dated 14 May 1970, is an inter-agency committee tasked primarily to formulate the National Government's fiscal program. It is composed of the Office of the President (OP), Department of Budget and Management (DBM), National Economic and Development Authority (NEDA), and the Department of Finance (DOF). The BSP attends the Committee meetings as a resource agency.

[3] In a joint DBCC statement on 3 December 2020 on the Review of the Medium-Term Macroeconomic Assumptions and Fiscal Program for FY 2020 to 2022, the inflation target was kept at 3.0 percent ± 1.0 percentage point.

The Monetary Board

The powers and functions of the BSP, such as the conduct of monetary policy and the supervision over the banking system, are exercised by its Monetary Board (MB), which has seven members appointed by the President of the Philippines. The Monetary Board holds eight (8) monetary policy meetings in a year to review and decide on the stance of monetary policy.

Chairman & Governor
Benjamin E. Diokno

Members
Carlos G. Dominguez III
Felipe M. Medalla
Peter B. Favila
Antonio S. Abacan, Jr.
V. Bruce J. Tolentino
Anita Linda R. Aquino

The Advisory Committee

The Advisory Committee was established as an integral part of the institutional setting for inflation targeting. It is tasked to deliberate, discuss, and make recommendations on monetary policy to the Monetary Board. Like the Monetary Board, the Committee meets eight times a year but may also meet between regular meetings, whenever deemed necessary.

Chairman
Benjamin E. Diokno
Governor

Members
Francisco G. Dakila, Jr.
Deputy Governor
Monetary and Economics Sector

Ma. Cyd Tuaño-Amador
Deputy Governor
Corporate Services Sector

Chuchi G. Fonacier
Deputy Governor
Financial Supervision Sector

Ma. Ramona GDT Santiago
Senior Assistant Governor
Financial Market Operations Sub-Sector

Johnny Noe E. Ravalo
Assistant Governor
Office of Systemic Risk Management

Iluminada T. Sicat
Assistant Governor
Monetary Policy Sub-sector

2021 SCHEDULE OF MONETARY POLICY MEETINGS, INFLATION REPORT PRESS CONFERENCE AND PUBLICATION OF MB HIGHLIGHTS

2020	Advisory Committee (AC) Meeting	Monetary Board (MB) Meeting	MB Highlights Publication	Inflation Report (IR) Press Conference
Jan			14 (Thu) (17 Dec 2020 MB meeting)	21 (Thu) (Q4 2020 IR)
Feb	8 (Mon) (AC Meeting No. 1)	11 (Thu) (MB Meeting No. 1)		
Mar	22 (Mon) (AC Meeting No. 2)	25 (Thu) (MB Meeting No. 2)	4 (Thu) (11 Feb 2021 MB meeting)	
Apr			22 (Thu) (25 Mar 2021 MB meeting)	22 (Thu) (Q1 2021 IR)
May	10 (Mon) (AC Meeting No. 3)	13 (Thu) (MB Meeting No. 3)		
Jun	21 (Mon) (AC Meeting No. 4)	23 (Wed) (MB Meeting No. 4)	3 (Thu) (13 May 2021 MB meeting)	
Jul			22 (Thu) (23 Jun 2021 MB meeting)	22 (Thu) (Q2 2021 IR)
Aug	9 (Mon) (AC Meeting No. 5)	12 (Thu) (MB Meeting No. 5)		
Sep	20 (Mon) (AC Meeting No. 6)	23 (Thu) (MB Meeting No. 6)	2 (Thu) (12 Aug 2021 MB meeting)	
Oct			28 (Thu) (23 Sep 2021 MB meeting)	21 (Thu) (Q3 2021 IR)
Nov	8 (Mon) (AC Meeting No. 7)	11 (Thu) (MB Meeting No. 7)		
Dec	13 (Mon) (AC Meeting No. 8)	16 (Thu) (MB Meeting No. 8)	9 (Thu) (11 Nov 2021 MB meeting)	

List of Acronyms, Abbreviations, and Symbols

AONCR	Areas Outside the National Capital Region
ASEAN	Association of Southeast Asian Nations
ASF	African Swine Fever
BAP	Bankers Association of the Philippines
BES	Business Expectations Survey
BI	Bank Indonesia
BIR	Bureau of Internal Revenue
BNM	Bank Negara Malaysia
BOC	Bureau of Customs
BoP	Balance of Payments
bp	Basis Point
BSPB	Bangko Sentral ng Pilipinas Bills
BSP-SF	Bangko Sentral ng Pilipinas Securities Facility
BTr	Bureau of the Treasury
BvD	Bureau van Dijk
CALABARZON	Cavite, Laguna, Batangas, Rizal and Quezon
CAMPI	Chamber of Automative Manufacturers of the Philippines, Inc.
CAR	Capital Adequacy Ratio
CBD	Central Business District
CDS	Credit Default Swap
CES	Consumer Expectations Survey
CI	Confidence Index
CPI	Consumer Price Index
CREATE	Corporate Recovery and Tax Incentives for Enterprises
CREL	Commercial Real Estate Loan
DA	Department of Agriculture
DBCC	Development Budget Coordination Committee
DBM	Department of Budget and Management
DI	Diffusion Index
DND	Department of National Defense
DOE	Department of Energy
DOF	Department of Finance
EQQ	Enhanced Community Quarantine
EIA	Energy Information Administration
EMBIG	Emerging Market Bond Index Global
ERC	Energy Regulatory Commission
ESI	Economic Sentiment Indicator
FCD	Foreign Currency Deposit
FIST	Financial Institutions Strategic Transfer
GCQ	General Community Quarantine
GDP	Gross Domestic Product
GIR	Gross International Reserve
GNI	Gross National Income
GNPL	Gross Non-Performing Loan
GOUR	Generation Over/Under Recovery
GS	Government Securities
HCW	Health Care Worker
IMTS	International Merchandise Trade Statistics
IPP	Independent Power Producer
IRC	Interest Rate Corridor
kWh	Kilowatt Hour
LFPR	Labor Force Participation Rate
LFS	Labor Force Survey
LSOUR	Lifeline Subsidy Over/Under Recovery
MB	Monetary Board
mb/d	Million Barrels per Day
MECQ	Modified Enhanced Community Quarantine
MERALCO	Manila Electric Company
MGCQ	Modified General Community Quarantine
MISSI	Monthly Integrated Survey of Selected Industries
m-o-m	Month-on-Month
MOOE	Maintenance and Other Operating Expenses
mt	Metric Ton
MTP	Major Trading Partner
NAP	National Accounts of the Philippines
NBFIs	Non-Bank Financial Intermediaries
NBQBs	Non-Banks with Quasi-Banking Functions
NCR	National Capital Region
NEDA	National Economic and Development Authority
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NG	National Government
NGCP	National Grid Corporation of the Philippines
NNPL	Net Non-Performing Loans
NSFR	Net Stable Funding Ratio
ODF	Overnight Deposit Facility
OFW	Overseas Filipino Worker
OP	Office of the President
OPEC	Organization of the Petroleum Exporting Countries
OPR	Overnight Policy Rate
P/E	Price-Earning Ratio
PISM	Philippine Institute for Supply Management
PMI	Purchasing Managers' Index
PNP	Philippine National Police
Ppt	Percentage Point
PS	Personnel Services
PSA	Philippine Statistics Authority
PSEi	Philippine Stock Exchange Index
QBs	Quasi-Banks
q-o-q	Quarter-on-Quarter
RBA	Reserve Bank of Australia
RBs	Rural Banks
RCEF	Rice Competitiveness Enhancement Fund
REER	Real Effective Exchange Rate
RP	Repurchase
RR	Reserve Requirement
RREL	Residential Real Estate Loan
RREPI	Residential Real Estate Price Index
RRP	Reverse Repurchase
RRR	Reserve Requirement Ratio
SAP	Social Amelioration Program
SBL	Substandard or Below Loan
SDA	Special Deposit Account
SLOS	Senior Bank Loan Officers' Survey
SLOUR	System Loss Over/Under Recovery
TBs	Thrift Banks
TDF	Term Deposit Facility
TMA	Truck Manufacturers Association
TOUR	Transmission Over/Under Recovery
TPI	Trading Partner Index
TPI-A	Trading Partner Index in Advanced Countries
TPI-D	Trading Partner Index in Developing Countries
U/KBs	Universal and Commercial Banks
VaPI	Value of Production Index
VoPI	Volume of Production Index
WAIR	Weighted Average Interest Rate
WESM	Wholesale Electricity Spot Market
y-o-y	Year-on-Year
y-t-d	Year -to-Date

Contents

Overview

Headline inflation for Q4 2020 rises. Headline inflation increased to 3.1 percent year-on-year (y-o-y) in Q4 2020, higher than the year- and quarter-ago rates of 1.6 percent and 2.5 percent, respectively. The resulting average headline inflation for full year 2020 also increased slightly to 2.6 percent but remained well within the government's target range of 3.0 percent ± 1.0 percentage point (ppt) for the year. Food inflation was the main driver of the higher Q4 inflation as supply disruptions due to adverse weather conditions led to higher prices for agricultural products.

Average headline inflation for 2020 stays within 2-4 percent target range despite uptick in Q4

Core inflation, which measures underlying price pressures, remained steady at 3.2 percent y-o-y in Q4 2020 relative to the previous quarter. On the other hand, preliminary estimates of alternative core inflation measures showed mixed trends as the weighted median measure was unchanged while both trimmed mean and net of volatile items posted higher rates during the quarter. Meanwhile, the number of Consumer Price Index (CPI) items with inflation rates higher than the threshold of 4.0 percent declined further to 47 items from 51 items in the previous quarter. These items accounted for a higher portion of the CPI basket at around 20.1 percent.

Inflation expectations are higher but remain manageable. The results of the BSP's survey of private sector economists for December 2020 showed higher mean inflation forecasts for 2020 and 2021 to 2.6 percent from 2.5 percent, and 2.9 percent from 2.8 percent, respectively, compared to the survey in September 2020. Meanwhile, mean inflation forecast for 2022 was unchanged at 3.0 percent. Analysts expect inflation to remain benign in the near term, with risks to the inflation outlook tilted to the upside as the economy gradually reopens.

Domestic economy still in double-digit contraction. The Q3 2020 real gross domestic product (GDP) contracted by 11.5 percent y-o-y from -16.9 percent in Q2 2020 and 6.3 percent in Q3 2019. This brought the year-to-date (y-t-d) GDP to a 9.7-percent contraction. On the demand side, household consumption and investment improved slightly with the partial reopening of economic activity but remained in contraction at -9.3 percent and -41.6 percent, respectively. Meanwhile, government spending slowed markedly to 5.8 percent following the expiration of the fiscal stimulus Bayanihan Act 1 in June 2020 and the delay in Bayanihan Act 2. On the supply side, agriculture was the sole growth sector, expanding by 1.2 percent. Services and industry sectors continued to decline at -10.6 percent and -17.2 percent, respectively, although at rates slower than in the previous quarter.

Real GDP continues to contract in Q3 2020

Other demand indicators continued to reflect weakness. Property prices declined as vacancy rates in both office and residential spaces increased. Sales of new vehicles remained weak and energy consumption continued to contract. Similarly, leading indicators of economic activity remained frail. The composite Purchasing Managers' Index (PMI) as of November 2020 was below the 50-point expansion threshold. Capacity utilization continued to be below optimal while the volume and value of production orders in the manufacturing sector remained weak. On the other hand, business confidence improved, and consumer expectations were less pessimistic in Q4 2020.

Nevertheless, global economic activity shows modest growth. The JP Morgan Global All-Industry Output Index stood at 52.7 in December 2020. Five out of the six sub-sectors covered by the survey registered output expansions during the month, led by the financial services and intermediate goods sectors. In contrast, consumer services activity fell for the eleventh consecutive month. On the other hand, Q3 2020 real GDP of major economies, namely the US, euro area, Japan and India, showed single-digit contractions, an improvement from their double-digit declines in the previous quarter. Moreover, latest PMIs for these countries showed general optimism. On the other hand, China's Q3 GDP expanded, showing the country's recovery from the pandemic. The slow and uneven pace of global growth prompted surveyed central banks to maintain a supportive monetary policy stance during the quarter.

Philippine financial system continues to be stable amid supportive monetary settings and ample liquidity. The Philippine stock exchange index (PSEi) increased by 12.2 percent quarter-on-quarter (q-o-q) to average 6,721.75 index points in Q4 2020. Expectations of economic rebound in the near term, further monetary stimulus measures during the review period and the pick-up in consumer spending during the Christmas season lifted investor sentiment. In the government securities (GS) market, demand for Treasury papers remained robust amid ample liquidity in the financial system. The Bureau of the Treasury (BTr) also issued ₱6.6-billion worth of 1-year Premyo Bonds 2 in December. During the review quarter, GS yields continued to decline in both primary and secondary markets, in part due to the 25-bp cut in the BSP's policy rate as well as sustained market interest for safe assets. In the foreign exchange market, the peso remained strong, averaging ₱48.27/US$1 in Q4 2020, an appreciation by 1.39 percent from the Q3 2020 average of ₱48.94/US$1. The continued strength of the peso was due in part to the country's high level of international reserves as well as positive market sentiment over the progress in the vaccine against COVID-19. Finally, the banking system continued to be solid and stable, showing respectable growth in deposits and resources. Moreover, asset quality remained manageable while capital adequacy ratios stayed above international standards.

The BSP remains accommodative in Q4 2020. The BSP reduced the overnight reverse repurchase (RRP) rate by 25 basis points (bps) in its November policy meeting and maintained the accommodative monetary setting in its December policy meeting. The BSP's decision to remain accommodative was based on a benign inflation outlook over the policy horizon.

The BSP cuts key policy rate by 25 bps during the quarter

Latest baseline forecasts rose slightly following higher-than-expected food inflation, which reflects the impact of weather disturbances, however, these are seen to be largely transitory. Inflation is projected to remain relatively benign in 2021 and 2022 with inflation expectations well-anchored within the target range. The balance of risks to the inflation outlook also remains tilted to the downside over the policy horizon owing largely to potential disruptions to domestic and global economic activity amid the ongoing pandemic.

Given these considerations, the BSP is of the view that prevailing monetary policy settings remain sufficiently accommodative to help quicken the economy's transition toward a sustainable recovery. Continuing monetary policy support, together with sustained fiscal initiatives to ensure public welfare, should help mitigate strong headwinds to growth.

However, possible upside surprises to inflation may be linked to supply-side risks such as weather disturbances and rising global crude oil prices. Looking ahead, the BSP will continue to monitor these developments and their impact on domestic inflation. Moreover, the BSP remains committed to deploying its full range of monetary instruments and regulatory relief measures as needed in fulfillment of its mandate to promote non-inflationary and sustainable growth.

I. Inflation and Real Sector Developments

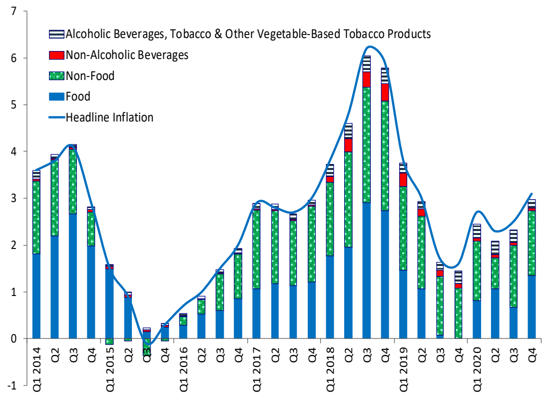
Prices

Headline inflation. Headline inflation rose to 3.1 percent y-o-y in Q4 2020, higher than the year- and quarter-ago rates of 1.6 percent and 2.5 percent, respectively. Despite the increase, Q4 2020 inflation remained within the 2-4 percent target range.

Average headline inflation stays within target in 2020 despite further rise in Q4 2020 inflation…

The resulting annual average headline inflation also increased slightly to 2.6 percent in 2020 from 2.5 percent in the previous year but remained well within the government's target range of 3.0 percent ± 1.0 ppt for the year.

Chart 1. Quarterly Headline Inflation (2012=100)
In percent



Source: Philipine Statistical Authority (PSA), BSP

Core Inflation. Meanwhile, core inflation, which excludes selected volatile food and energy items to measure underlying price pressures, remained steady at 3.2 percent y-o-y in Q4 2020 relative to the previous quarter.

… while official core inflation remains steady

On the other hand, preliminary estimates of alternative core inflation measures showed mixed trends in Q4 2020. Core inflation estimate based on weighted median was unchanged during the quarter while both trimmed mean and net of volatile items posted higher rates in Q4 2020.

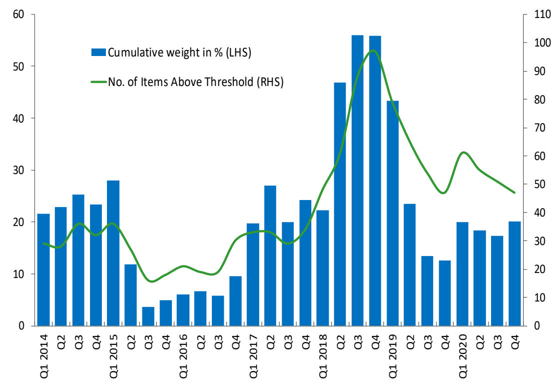
Table 1. Alternative Core Inflation Measure
Quarterly averages of year-on-year change

Quarter	Official Headline Inflation	Official Core Inflation	Trimmed Mean [1]	Weighted Median [2]	Net of Volatile Items [3]
2019					
Q1	3.8	3.9	3.8	3.4	3.7
Q2	3.0	3.4	2.9	3.0	3.0
Q3	1.7	2.9	1.9	2.8	3.3
Q4	1.6	2.7	1.7	2.6	3.3
2020					
Q1	2.7	3.2	2.2	2.6	3.8
Q2	2.3	2.9	2.1	2.3	3.5
Q3	2.5	3.2	2.0	2.2	3.0
Q4	**3.1**	**3.2**	**2.2**	**2.2**	**3.1**

[1] The trimmed mean represents the average inflation rate of the (weighted) middle 70 percent in a lowest-to-highest ranking of year-on-year inflation rates for all CPI components.
[2] The weighted median represents the middle inflation rate (corresponding to a cumulative CPI weight of 50 percent) in a lowest-to-highest ranking of year-on-year inflation rates.
[3] The net of volatile items method excludes the following items: bread and cereals, vegetables sugar, jam, honey, chocolate, and confectionery, electricity, gas, fuel and lubricants for personal transport equipment, and passenger transport by road, which represents 29.5 percent of all items.
Source: PSA, BSP estimates

The number of CPI items with inflation rates higher than the threshold declined further to 47 items in Q4 2020 from 51 items in the previous quarter but accounted for a higher portion of the CPI basket at around 20.1 percent in Q4 2020 from 17.4 percent in the previous quarter.

Chart 2. CPI Items with Inflation Rates Above Threshold (2012=100)



Source: PSA, BSP staff estimates

Food Inflation. Food inflation rose markedly in Q4 2020 to 3.8 percent y-o-y from 1.9 percent in the previous quarter due largely to higher price increases of selected agricultural products.

Tighter domestic supply pushes food inflation higher in Q4 2020

Vegetable inflation went up due to weather-related supply disruptions following the recent typhoons that visited the country. At the same time, adverse weather conditions limited the supply of fish, which also led to higher price increases for fish. Meat inflation also increased owing to some tightness in supply brought about by the African Swine Fever (ASF).

Table 2. Inflation Rates for Selected Food Items (2012=100)

Year-on-year, in percent

Commodity	2019	2020	
	Q4	Q3	Q4
Food and Non-Alcoholic Beverages	**0.3**	**1.9**	**3.7**
Food	0.0	1.9	3.8
Bread and Cereals	-5.5	-0.2	0.3
Rice	-8.3	-0.9	-0.2
Corn	-2.5	-0.4	-0.9
Meat	3.1	3.9	7.6
Fish	3.6	2.9	4.1
Milk, Cheese and Eggs	3.2	2.9	1.9
Oils and Fats	0.6	2.4	2.6
Fruit	8.5	7.2	5.5
Vegetables	2.7	-0.9	11.3
Sugar, Jam, Honey, Chocolate and Confectionery	-3.8	0.1	0.3
Food Products, N.E.C.	5.9	5.3	4.2
Non-Alcoholic Beverages	3.2	2.1	1.9
Alcoholic Beverages and Tobacco	17.5	16.5	12.0

Source of Basic Data: PSA, BSP

Non-food Inflation. Non-food inflation inched up to 2.3 percent y-o-y in Q4 2020 from 2.2 percent in the previous quarter and 1.8 percent in the same period a year ago.

… while non-food inflation inches up slightly during the quarter

Transport inflation continued to rise in Q4 2020 due to higher road transport fares (i.e., tricycle, pedicab, bus, and jeepney). The higher inflation for education at 1.1 percent y-o-y during the quarter also contributed to the increase in non-food inflation. Meanwhile, the slowdown in inflation of other major subcomponents such as housing, water, electricity, gas, and other fuels along with price declines in recreation and culture, slightly tempered the rise in non-food inflation.

Table 3. Inflation Rates for Selected Non-Food Items (2012=100)

Year-on-year, in percent

Commodity	2019	2020	
	Q4	Q3	Q4
Non-Food	**1.8**	**2.2**	**2.3**
Clothing and Footwear	2.7	2.0	1.6
Housing, Water, Electricity, Gas and Other Fuels	1.2	1.0	0.7
Furnishings, Household Equipment & Routine Household Maintenance	2.9	3.9	3.5
Health	3.0	2.8	2.6
Transport	-0.7	7.0	8.0
Communication	0.3	0.3	0.3
Recreation and Culture	1.4	0.2	-0.6
Education	4.6	0.6	1.1
Restaurant and Miscellaneous Goods and Services	2.8	2.3	2.4

Source of Basic Data: PSA, BSP

Private Sector Economists' Inflation Forecasts. The results of the BSP's survey of private sector economists for December 2020 showed higher mean inflation forecast for 2020 to 2.6 percent from 2.5 percent based on the September 2020 survey.[4]

Inflation expectations are higher for 2020 and 2021, and steady for 2022

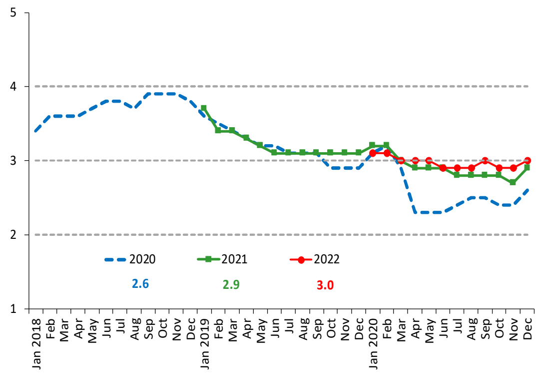
Similarly, mean inflation forecast for 2021 rose to 2.9 percent from 2.8 percent. Meanwhile, mean inflation forecast for 2022 was unchanged at 3.0 percent.

Chart 3. BSP Private Sector Economists' Survey*

Mean forecast for full year; in percent

January 2016 to February 2018 (2006=100)

March 2018 to December 2020 (2012=100)



*Based on forecasts provided by 24 respondents.

Source: BSP

[4] There were 24 respondents in the BSP's survey of private sector economists in December 2020. The survey was conducted from 4 to 12 December 2020.

Analysts expect inflation to remain benign in the near term, with risks to the inflation outlook tilted to the upside as the economy gradually reopens. The identified upside risks to inflation include: (a) food supply disruptions due to the recent typhoons and the likely occurrence of weather disturbances in the near term amid La Niña condition; (b) the rebound in oil prices on the possible recovery of demand; (c) higher consumer spending during the holiday season; and (d) the impact of the BSP's monetary policy actions.

Table 4. Private Sector Forecasts for Inflation

Annual percentage change; December 2020 (2012=100)

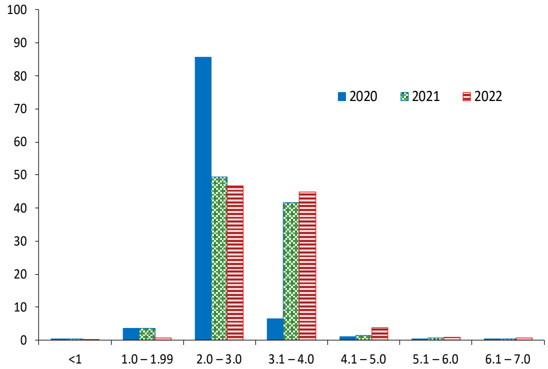
	2020	2021			2022
	FY	Q1	Q2	FY	FY
1) Al-Amanah Islamic Bank	3.00	3.00	3.50	3.50	3.50
2) Banco De Oro	2.56	2.90	3.67	3.41	3.17
3) Bangkok Bank	2.60	3.00	3.00	3.00	3.20
4) Bank of Commerce	2.57	-	-	-	-
5) Bank of China Ltd.	2.50	2.50	3.00	3.00	2.50
6) Chinabank	2.60	2.60	2.60	2.60	2.60
7) CTBC Bank	2.40	2.80	3.10	3.00	3.20
8) Deutsche Bank	2.50	-	-	2.90	3.00
9) Eastwest Bank	2.60	2.50	3.10	2.50	3.10
10) Global Source	2.60	2.90	3.30	3.00	2.90
11) Korea Exchange Bank	3.00	2.90	2.90	2.90	2.80
12) Land Bank of the Phils	2.50	2.80	2.90	2.80	2.90
13) Maybank	2.62	2.77	3.00	3.02	2.50
14) Maybank-ATR KimEng	2.60	2.70	3.10	2.80	2.50
15) Metrobank	2.40	-	-	2.60	-
16) Mizuho	2.50	2.70	2.90	3.10	3.20
17) Nomura	2.50	2.40	2.80	2.70	3.30
18) RCBC	2.50	2.20	3.00	2.60 - 3.10	3.00 - 3.50
19) Robinsons Bank	2.60	3.10	3.80	3.50	3.00
20) Philippine Equity Partners	2.60	3.10	3.80	3.50	3.30
21) Security Bank	2.50	2.90	3.00	3.00	3.30
22) Standard Chartered	2.40	2.20	3.00	2.90	3.00
23) Union Bank of the Phils.	2.60	2.00	2.60	2.50	3.00
24) UBS	2.40	2.20	-	2.50	-
Median Forecast	2.6	2.8	3.0	2.9	3.0
Mean Forecast	**2.6**	**2.7**	**3.1**	**2.9**	**3.0**
High	3.0	3.1	3.8	3.5	3.5
Low	2.4	2.0	2.6	2.5	2.5
Number of Observations	24	21	20	23	21
Government Target	**3.0±1.00**	**3.0±1.00**	**3.0±1.00**	**3.0±1.01**	**3.0±1.00**

Source: BSP

Downside risks to inflation are seen to emanate from (a) muted domestic demand as consumer confidence remains weak and low purchasing power amid high unemployment rate; (b) strong peso against the US dollar; and (c) soft global crude oil prices.

Based on the probability distribution of the forecasts provided by 20 out of 24 respondents, there is a 92.1-percent probability that average inflation for 2020 will settle between the 2-4 percent range, while there is a 4.0-percent chance that inflation will fall below 2.0 percent. Meanwhile, the probabilities that inflation will fall within the target band in 2021 and 2022 are seen at 91.0 percent and 91.5 percent, respectively.

Chart 4. Probability Distribution for Analysts' Inflation Forecasts* (2020-2022)



*Probability distributions were averages of those provided by 20 out of 24 respondents.
Source: December 2020 BSP Survey

Based on the Q4 2020 BSP Business Expectations Survey (BES), respondent firms expect inflation to increase in Q1 2021 and the next 12 months relative to their expectations during the Q3 2020 survey round.[5]

Firms and consumers expect inflation to remain within the government's target range

Relative to the previous survey, a higher number of respondents in Q4 2020 expect inflation to increase in the current quarter (i.e., the diffusion index (DI) increased slightly to 14.8 percent from 14.5 percent). Meanwhile, a lower number of respondents generally anticipate higher inflation in the next quarter (i.e., the DI declined to 18.7 percent from 22.4 percent). Nevertheless, businesses expect that the rate of increase in commodity prices will remain within the government's 2 to 4 percent inflation target range for 2020 and 2021. In particular, inflation is projected to settle below the midpoint of the target range to 2.5 percent for Q4 2020 and 2.6 percent for both Q1 2021 and the next 12 months (from 2.3 percent, 2.4 percent, and 2.5 percent, respectively in the Q3 2020 survey results).

The BSP Consumer Expectations Survey (CES) results for Q4 2020 also indicated that consumers expect inflation to remain within the government's

[5] The conduct of the Q2 2020 BES and CES in April 2020 was cancelled due to the implementation of the Enhanced Community Quarantine (ECQ) from 16 March to 31 May 2020. As such, no reports and statistics on the said surveys were published on 26 June 2020.

target range.[6] In particular, households generally anticipate inflation to fall below the midpoint of the target to 2.6 percent for Q4 2020, 2.7 percent for Q1 2021, and 2.9 percent for the next 12 months. Meanwhile, inflation is expected to decline for the following items: rice (3.5 percent); bread and cereals (3.5 percent); meat (5.0 percent); fish and seafood (5.6 percent); fruits (4.2 percent); vegetables (3.9 percent); milk, cheese, and eggs (4.1 percent); non-alcoholic beverages (3.2 percent); alcoholic beverages (6.3 percent); clothing (0.5 percent); house rent (1.6 percent); water (3.5 percent); light (5.9 percent); fuel (2.6 percent); medical care (2.7 percent); transportation (10.1 percent); communication (1.0 percent); education (1.2 percent); personal care (2.3 percent); and restaurants and cafes (1.5 percent).

Energy prices. The average price of Dubai crude oil increased by 4 percent q-o-q in Q4 2020, driven by optimism over global demand recovery following reports of the COVID-19 vaccine efficacy. The subsequent roll out of vaccine in different countries have also boosted market sentiment.

Rise in international oil price due to optimism over global demand recovery

At the same time, the Organization of the Petroleum Exporting Countries (OPEC) and other participating producers (OPEC+) have decided to increase production by 0.5 million barrels per day (mb/d) beginning in January 2021, which is lower than its initial plan of increasing output by 2 mb/d. This will bring the total production cuts at the start of 2021 to 7.2 mb/d.

The estimated futures prices of Dubai crude oil in December 2020,[7] which are based on movements in Brent crude oil futures, showed a much higher path for 2021 to 2023 compared to the estimates in September 2020.

In December 2020,[8] the US Energy Information Administration (EIA) revised downward its world oil consumption projection for 2021 by 0.6 mb/d compared to the previous month's report. At the same time, US EIA also reduced its world production forecast by 1.0 mb/d for 2021 compared to the November report, reflecting the OPEC+ decision during its 3 December 2020 meeting to lower the planned production increase for January 2021.

In the domestic market, on a y-t-d basis, there was a net price decrease for domestic petroleum products as of 29 December 2020 in Metro Manila. Domestic prices of gasoline, diesel, and kerosene declined by ₱8.49 per liter, ₱5.17 per liter, and ₱8.71 per liter, respectively, compared to end-2019 levels.[9]

Power. The overall electricity rate in the Meralco-serviced area fell slightly by around ₱0.03 per kilowatt hour (kWh) to about ₱8.51 per kWh (from ₱8.54 per kWh in Q3 2020) on the back of lower generation charge.

Retail electricity prices decline in Q4 2020

According to Meralco, the downward adjustment in the generation cost was due primarily to the improved supply conditions in the Luzon grid given lower electricity demand owing to weather disturbances and less generation capacity on outage, pushing cost of power from the Wholesale Electricity Spot Market (WESM) to decline. Contributing to the decline in generation charges during the review period was the cost of power from the Independent Power Producers (IPPs) which fell in November and December 2020. This was a result of lower Malampaya natural gas prices due to its quarterly repricing and improved average plant dispatch. At the same time, charges from the IPPs decreased as a result of the appreciation of the peso against the US dollar.

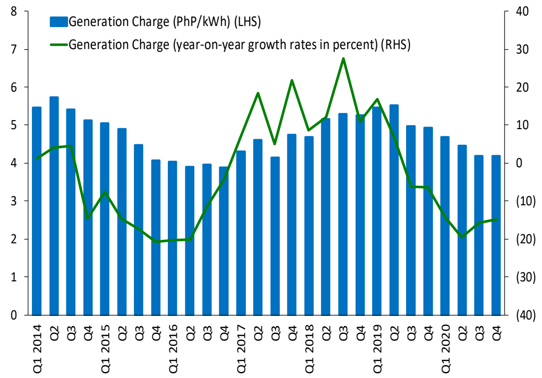
[6] Ibid.

[7] Based on BSP staff estimates of futures prices of Dubai crude oil as of 29 December 2020.

[8] Source: US EIA, December 2020 Short-Term Energy Outlook, https://www.eia.gov/

[9] Source: Department of Energy (DOE)

Chart 5. Meralco's Generation Charge
PhP/kWh; year-on-year growth rates in percent



Source: Meralco

There are potential sources of upside pressures on electricity charges which are mainly associated with still-pending petitions from previous years. Meralco has existing petitions for rate increases with the Energy Regulatory Commission (ERC) which include the petition to implement the Maximum Average Price for 2012, 2013, 2014, and 2015, amended application for a rate increase in the January 2014 billing (consisting of incremental fuel costs and deferred generation cost to be collected monthly for six months); and petitions for the refund of generation over/under recovery (GOUR), transmission over/under recovery (TOUR), system loss over/under recovery (SLOUR), and lifeline subsidy over/under recovery (LSOUR) for the period January-December 2011. Likewise, the National Grid Corporation of the Philippines (NGCP) also filed several petitions to recover connection charges and residual sub-transmission charges for 2011-2013 and the costs of repair on damages caused by force majeure events such as earthquake, flooding, landslides, and lightning incidents in 2011-2012.

Aggregate Demand and Supply[10]

The Q3 2020 real gross domestic product (GDP) contracted by 11.5 percent y-o-y from -16.9 percent in Q2 2020 and 6.3 percent in Q3 2019. On a seasonally-adjusted basis, q-o-q GDP grew by 8.0 percent in Q3 2020, higher than the 14.9-percent contraction in Q2 2020.

[10] Estimates on the second quarter 2020 National Accounts of the Philippines (NAP) are based on the 2018 base year following the recent revision and rebasing of the NAP series.

Real GDP remains in contraction in Q3 2020

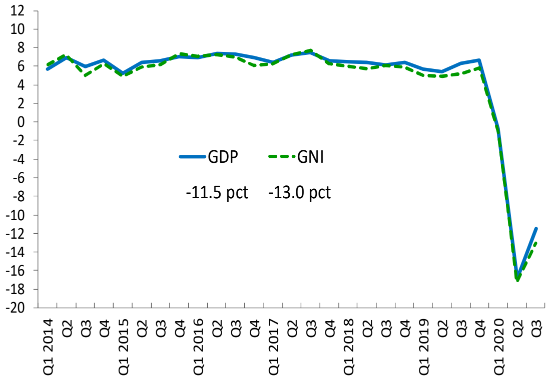
Gross national income (GNI) declined by 13.0 percent in Q3 2020, from the 5.2-percent growth registered in Q3 2019 but a smaller contraction compared to the 17.3-percent decline in Q2 2020. Net primary income went down further by 28.2 percent in Q3 2020, from -4.6 percent in Q3 2019 and -21.7 percent in Q2 2020.

On the demand side, consumer and investor sentiment improved in Q3 2020 following the gradual reopening of establishments and public transportation. Both household consumption (-9.3 percent in Q3 2020 from -15.3 percent in Q2 2020) and investments (-41.6 percent in Q3 2020 from -53.7 percent in Q2 2020) recovered, albeit still negative.

Meanwhile, government consumption slowed down markedly to 5.8 percent in Q3 2020 from 21.8 percent in Q2 2020. The combined effect of less negative private consumption and investments resulted in the smaller contraction of domestic demand. Moreover, total exports dropped at a slower pace (-14.7 percent in Q3 2020 from -35.8 percent in Q2 2020) while imports contracted less (-21.7 percent in Q3 2020 from -37.9 percent in Q2 2020), bringing net exports to decline by 43.5 percent in Q3 2020 from 44.3 percent in Q2 2020.

On the supply side, several industries posted slower contraction in Q3 2020 following the resumption of business operations as community quarantine measures were lifted. In particular, smaller decline in manufacturing (-9.7 percent in Q3 2020 from -20.7 percent in Q2 2020) contributed to the industry sector's recovery (-17.2 percent from -21.8 percent). The services sector—which accounts for over 60 percent of total GDP— continued to decline to 10.6 percent in Q3 2020 but less negative compared to the -17.0 percent in Q2 2020, supported by the less contraction in transport and storage as well as trade. Among the major industries, only the agriculture sector recorded an expansion of 1.2 percent y-o-y in Q3 2020, from the 1.6-percent growth in Q2 2020.

Chart 6. Gross Domestic Product (GDP) and Gross National Income (GNI)
At constant 2018 prices



Source: PSA

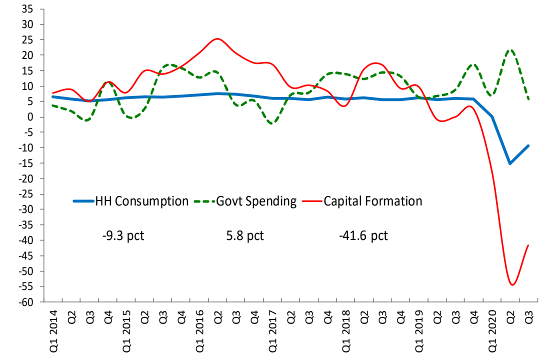
Aggregate Demand. Under the expenditure approach, household spending, government spending, net exports, and investments (or capital formation) contributed -6.6 ppt, 0.7 ppt, 4.4 ppts, -11.1 ppt, respectively, to total GDP growth in Q3 2020.

Household consumption and investments continue to weigh down aggregate demand

Household expenditures, which accounted for 73.2 percent of GDP in Q3 2020, contracted by 9.3 percent in Q3 2020, an improvement from the 15.3-percent decline in Q2 2020. This was attributed to the easing of quarantine measures as well as stable inflation environment and increased employment opportunities in Q3 2020.

Except for education, consumption for most household commodities posted smaller declines in Q3 2020 such as, transport and hotels and restaurants. By contrast, housing and utilities and communication eased in Q3 2020. Meanwhile, growth for food and non-alcoholic beverages was unchanged at 4.6 percent y-o-y in Q3 2020.

Chart 7. Gross Domestic Product by Expenditure Shares
At constant 2018 prices



Source: PSA

Government expenditures grew by 5.8 percent in Q3 2020, slower than the 8.8-percent and 21.8-percent increments in Q3 2019 and Q2 2020, respectively, following the expiration of the Bayanihan 1 in June and with Bayanihan 2 still in Congress for most of Q3 2020. Nevertheless, growth in maintenance and other operating expenses (MOOE) remained high at 56.1 percent in Q3 2020 from 120.8 percent in Q2 2020), with the continued implementation of various COVID-19 emergency measures pursuant to the Bayanihan to Heal as One Act (R.A. 11469). The growth in MOOE was driven by the hiring of health care workers (HCWs) due to COVID-19, and the delivery of learning modules and other materials in line with the opening of classes last October 2020.

Similarly, growth in expenditures for personnel services (PS) slowed down to 3.0 percent in Q3 2020 from 12.8 percent in Q2 2020 due to some base effects resulting from the one-off payment of the military and uniformed personnel's pension differential under the Department of National Defense (DND) in July 2019. Nonetheless, the recorded growth in PS spending was attributed to the implementation of the second tranche of the Salary Standardization Law of 2019 (R.A. 1146), payment for the retirement gratuity and terminal leave benefit claims, and creation or filing of positions in the Philippine National Police (PNP).

Table 5. Gross Domestic Product by Expenditure
At constant 2018 prices; growth rate in percent

BY EXPENDITURE ITEM	2019	2020	
	Q3	Q2	Q3
Household Consumption	6.0	-15.3	-9.3
Government Consumption	8.8	21.8	5.8
Capital Formation	-0.1	-53.7	-41.6
Fixed Capital Formation	5.9	-36.5	-37.1
Exports	1.8	-35.8	-14.7
Imports	-0.1	-37.9	-21.7

Source: PSA

Capital formation contracted at a slower pace to -41.6 percent in Q3 2020 from -53.7 percent in Q2 2020 primarily due to the decline in inventory drawdown. Meanwhile, total fixed capital investments dropped by 37.1 percent in Q3 2020 (from -36.5 percent in Q2 2020). This was due to the sluggish performance of the construction industry, particularly private and government construction, owing to the temporary suspension of construction activities following the re-imposition of a two-week modified enhanced community quarantine (MECQ) in August as well as the limited construction activities amid the implementation of health and safety protocols. Nevertheless, the overall decline in fixed capital formation was partly tempered by the slower reduction in durable equipment. In particular, investments in road transport, telecommunications and sound equipment, and miscellaneous equipment improved in Q3 2020.

Overall exports contracted by 14.7 percent in Q3 2020, an improvement from the 35.8-percent decline posted in Q2 2020. This was due to the registered recovery in merchandise exports (-2.2 percent from -30.8 percent) particularly in semiconductors and other exports of goods. Additionally, the economic recovery in the country's top export destinations such as, the US, China, and Japan and to a lesser extent, Germany, Singapore, Malaysia, and Netherlands likely contributed to the smaller decline in merchandise exports. Meanwhile, exports of services also contracted at a weaker pace in Q3 2020 as business and manufacturing services registered upturns.

Overall imports continued to contract by 21.7 percent in Q3 2020, from the 37.9-percent decline in Q2 2020. This slower decline was due to the improved performance of merchandise imports (-19.7 percent in Q3 2020 from -39.8 percent in Q2 2020), particularly mineral fuels, lubricants and related materials, electronic products, transport equipment, and base metal.

Other Demand Indicators.[11] Other demand indicators continued to reflect weakness in economic activity. Real estate values declined as vacancy rates in both office and residential spaces increased. Sales of new vehicles remained slow and energy consumption as reported by Meralco continued to contract. Similarly, leading indicators of economic activity continued to be frail. The composite Purchasing Managers' Index (PMI) as of November 2020 was below the 50-point expansion threshold. Capacity utilization was still below optimal while the volume and value of production orders in the manufacturing sector continued to be weak. On the other hand, business confidence improved, and consumer expectations were less pessimistic in Q4 2020.

Property Prices

Capital Values, Metro Manila. Average capital values[12] for office buildings in Metro Manila[13] in Q3 2020 declined to ₱179,627/sq.m., lower by 9.2 percent and 0.9 percent compared to the year- and quarter-ago levels, respectively. The decline was due mainly to the decrease in capital values for office buildings in major business hubs in Metro Manila such as Makati Central Business District (CBD), Ortigas Center, Fort Bonifacio, and Manila Bay Area.

Capital values decline for office buildings but increase y-o-y for residential spaces

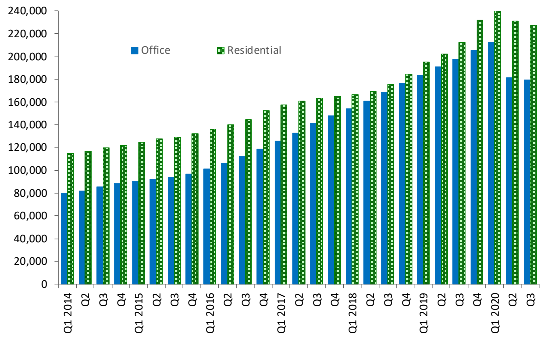
Meanwhile, average capital values for luxury residential buildings[14] in Metro Manila[15] in Q3 2020 reached ₱227,500 sq.m., higher by 7.2 percent y-o-y but lower by 1.5 percent q-o-q. In terms of location, three-bedroom luxury residential condominium units in Makati CBD, Fort

[11] There were no surveys conducted for Q2 2020 BES and CES.
[12] Probable price that the property would have fetched if sold on the date of the valuation. The valuation includes imputed land and building value.
[13] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, Alabang, and Manila Bay Area.
[14] In terms of location, luxury residential units are located within the CBD core and have quality access to/from and have superior visibility from the main avenue. Meanwhile, in terms of general finish, luxury residential units have premium presentation and maintenance.
[15] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, and Rockwell.

Bonifacio, and Ortigas Center recorded increases in capital values compared to the same period last year.

Chart 8. Capital Values, Metro Manila

Price per square meter



Source: Colliers International Philippines

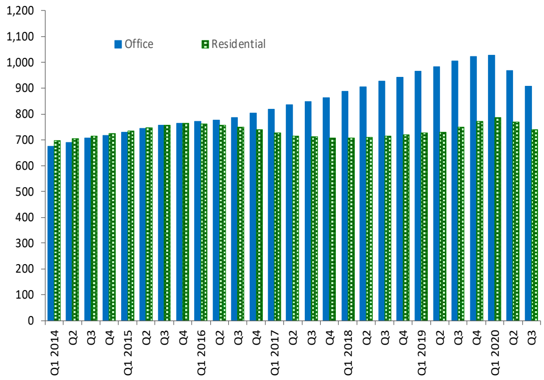
Rental Values, Metro Manila.[16] Average monthly office rents in Metro Manila reached ₱907/sq.m. in Q3 2020, which decreased by 6.3 percent from the previous quarter. This was also lower by 9.8 percent relative to Q3 2019. The depreciation in office rental rates was due to the reduced demand from offshore gaming, outsourcing, and traditional firms amid the pandemic. Per Colliers, landlords have become more flexible in accommodating tenant's requests to lower lease rates.

Rental values for office and residential spaces decline

According to market analysts, office leasing recovery will primarily hinge on recovery of general business sentiment which should entice local businesses to re-open; and recovery of global economies that outsource services from the Philippines. Key segments such as telecommunications, medical coding, health information management, and e-commerce should help lift leasing and hence, rental growth recovery in the second half of 2021.

Chart 9. Rental Values, Metro Manila

Price per square meter



Source: Colliers International Philippines

Average monthly rents for luxury three-bedroom condominium units in Metro Manila was recorded at ₱740/sq.m. in Q3 2020, lower by 3.9 percent and 1.3 percent compared to the previous quarter and year-ago levels, respectively. The slowdown in rents in Metro Manila in Q3 2020 relative to the previous quarter could be attributed to the lesser demand from foreign and local employees, especially in business districts. Residential leasing was adversely affected by a lackluster office market. Specifically, condominium segment was reeling from subdued business and consumer confidence.

Vacancy Rates, Metro Manila. The office vacancy rate in Metro Manila rose to 7.1 percent in Q3 2020 from 4.9 percent in the Q2 2020 due mainly to slower leasing from all segments and a rise in vacated spaces. In terms of location, the office vacancy rates in Makati CBD (3.0 percent from 1.8 percent), Fort Bonifacio (4.9 percent from 3.9 percent), Ortigas Center (11.7 percent from 5.3 percent), and Manila Bay Area (5.0 percent from 4.8 percent) increased in Q3 2020 compared to the previous quarter.

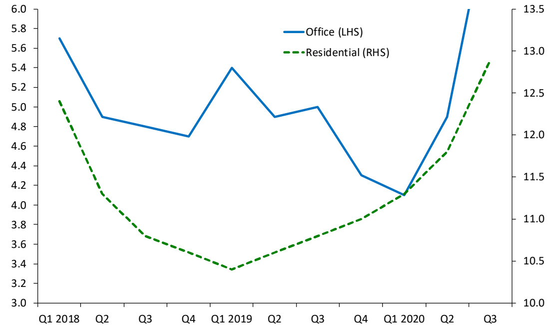
Vacancy rates for offices and residences continue to increase

Following the adverse impact of the pandemic and community quarantine, according to Colliers, higher office vacancy rate is expected in the remainder of 2020 due mainly to slowdown in leasing activities, weak demand, and a cautious market.

[16] Rental values discussed in this section pertain to high-end rented properties, which may be considered as indicators of wealth and demand.

Chart 10. Vacancy Rates

In percent



Source: Colliers International Philippines

Similarly, the overall residential vacancy rate in Metro Manila increased to 12.9 percent in Q3 2020 from 11.8 percent in Q2 2020 due to the slower take-up of units in areas near the core business districts. In particular, residential vacancy rates were higher in Makati CBD (12.1 percent from 11.4 percent), Fort Bonifacio (16.8 percent from 15.8 percent), Rockwell Center (10.9 percent from 10.4 percent), Ortigas Center (5.5 percent from 4.9 percent), Eastwood City (5.4 percent from 4.6 percent), and Manila Bay area (17.1 percent from 14.1 percent).

The rental market continues to face headwinds. Colliers sees vacancy rate approaching 13 percent due to softer sales and leasing in the secondary market. Nonetheless, Colliers projects vacancy to start improving in the second half of 2021 as consumer and business confidence rebound.

BSP Residential Real Estate Price Index (RREPI).[17] Residential real estate prices of various types of housing units nationwide declined by 0.4 percent y-o-y in Q3 2020 based on the RREPI. This is the first time that the RREPI posted negative y-o-y growth since the start of the series in Q1 2016.

Residential real estate price index records a slight decline

The decline in the RREPI may be attributed to the weak consumer demand for house and lot, which was consistent with the outcome of the Q3 2020 Consumer Expectations Survey. The said survey observed the low preference of consumers to buy real estate property amid the pandemic and economic uncertainty.

By area, residential property prices contracted y-o-y in the National Capital Region (NCR), but expanded in the Areas Outside NCR (AONCR). Residential property prices in NCR declined by 12.2 percent relative to a year ago, while prices in AONCR rose by 6.4 percent. In NCR, the decrease in prices of condominium units and duplexes outweighed the increase in prices of single detached/attached houses and townhouses. Meanwhile, prices in AONCR rose across all types of housing units, except for the prices of duplexes in the same period.

Table 6. Residential Real Estate Price Index[1] by Area

Q1 2014=100; growth rate in percent

Quarter	Residential Real Estate Price Index [1] (By Area)		
	Overall	NCR	AONCR
2018 Q1	118.8	123.1	115.9
Q2	119.7	127.2	115.4
Q3	119.3	128.0	113.8
Q4	120.7	131.4	113.5
2019 Q1	122.6	133.5	116.5
Q2	120.7	134.5	114.3
Q3	131.7	156.4	119.4
Q4	133.3	151.2	122.9
2020 Q1	138.0	158.7	126.4
Q2	152.8	180.6	134.7
Q3	131.2	137.3	127.1
Year-on-Year Growth Rates			
2018 Q1	1.8	2.8	0.8
Q2	4.5	4.3	4.2
Q3	4.5	7.0	2.2
Q4	0.5	1.7	-0.8
2019 Q1	3.2	8.4	0.5
Q2	0.8	5.7	-1.0
Q3	10.4	22.2	4.9
Q4	10.4	15.1	8.3
2020 Q1	12.6	18.9	8.5
Q2	26.6	34.3	17.8
Q3	-0.4	-12.2	6.4
Quarter-on-Quarter Growth Rates			
2018 Q1	-1.1	-4.7	1.3
Q2	0.8	3.3	-0.4
Q3	-0.3	0.6	-1.4
Q4	1.2	2.7	-0.3
2019 Q1	1.6	1.6	2.6
Q2	-1.5	0.7	-1.9
Q3	9.1	16.3	4.5
Q4	1.2	-3.3	2.9
2020 Q1	3.5	5.0	2.8
Q2	10.7	13.8	6.6
Q3	-14.1	-24.0	-5.6

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015.

Source: BSP

[17] The RREPI measures the average changes in prices of different types of housing units over a period of time across different geographical regions where the growth rate of the index measures house inflation. It is computed as a weighted chain-linked index based on the average appraised value per square meter weighted by the share of floor area of new housing units. The RREPI was computed based on data from housing loans granted by universal, commercial, and thrift banks.

In Q3 2020, the purchase of new housing units accounted for 74.9 percent of residential real estate loans (RRELs). Meanwhile, by type of housing units, most of the residential property loans were used for the acquisition of condominium units (48.7 percent), followed by single detached/attached houses (43 percent), and townhouses (7.9 percent).

By area, most of the RRELs granted in NCR were for the purchase of condominium units, while RRELs granted in AONCR were for the purchase of single detached/attached houses. By region, 46.5 percent of the total number of RRELs granted were accounted in NCR, while the rest were distributed in CALABARZON (26.5 percent), Central Luzon (7.7 percent), Western Visayas (5.1 percent), Central Visayas (4.9 percent), Davao Region (2.8 percent), and Northern Mindanao (2 percent). These regions combined accounted for 95.5 percent of total housing loans granted by banks.

Table 7. Residential Real Estate Price Index[1] by Housing Type

Q1 2014=100; growth rate in percent

Quarter	Residential Real Estate Price Index [1] (By Housing Type)				
	Overall [2]	Single Detached/ Attached	Duplex [3]	Townhouse	Condominium Unit
2018 Q1	118.8	109.6	131.5	125.2	133.3
Q2	119.7	107.3	99.0	131.3	141.0
Q3	119.3	105.8	115.5	130.6	141.0
Q4	120.7	104.7	98.8	132.9	146.8
2019 Q1	122.6	107.5	121.0	137.4	147.8
Q2	120.7	103.3	111.4	137.0	154.5
Q3	131.7	108.3	144.2	138.5	182.1
Q4	133.3	110.8	148.6	146.2	174.6
2020 Q1	138.0	115.4	167.3	145.1	182.7
Q2	152.8	127.5	112.3	151.8	201.0
Q3	131.2	116.3	131.5	155.1	154.7
Year-on-Year Growth Rates					
2018 Q1	1.8	-0.5	44.2	13.7	2.1
Q2	4.5	1.5	-4.4	13.8	7.1
Q3	4.5	0.2	30.7	18.5	5.8
Q4	0.5	-1.9	-3.7	11.5	0.7
2019 Q1	3.2	-1.9	-8.0	9.7	10.9
Q2	0.8	-3.7	12.5	4.3	9.6
Q3	10.4	2.4	24.8	6.0	29.1
Q4	10.4	5.8	50.4	10.0	18.9
2020 Q1	12.6	7.3	38.3	5.6	23.6
Q2	26.6	23.4	0.8	10.8	30.1
Q3	-0.4	7.4	-8.8	12.0	-15.0
Quarter-on-Quarter Growth Rates					
2018 Q1	-1.1	2.7	28.2	5.0	-8.6
Q2	0.8	-2.1	-24.7	4.9	5.8
Q3	-0.3	-1.4	16.7	-0.5	0.0
Q4	1.2	-1.0	-14.5	1.8	4.1
2019 Q1	1.6	2.7	22.5	3.4	0.7
Q2	-1.5	-3.9	-7.9	-0.3	4.5
Q3	9.1	4.8	29.4	1.1	17.9
Q4	1.2	2.3	3.1	5.6	-4.1
2020 Q1	3.5	4.2	12.6	-0.8	4.6
Q2	10.7	10.5	-32.9	4.6	10.0
Q3	-14.1	-8.8	17.1	2.2	-23.0

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015.
[2] No index generated for apartments due to very few observations.
[3] Indices for duplex exhibit more volatility due to relatively small number of reported real estate loans.
Source: BSP

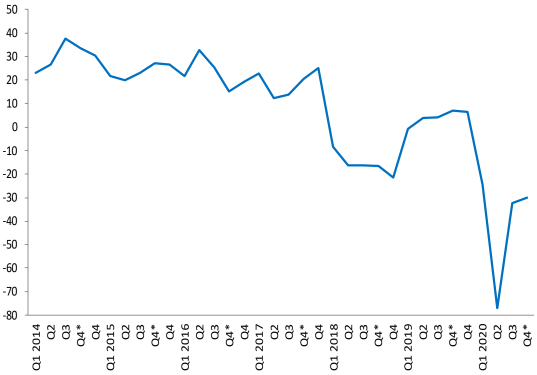
Vehicle Sales. The sales of new vehicles from CAMPI-TMA[18] members dropped by 30.0 percent y-o-y for the period October-November 2020, a turnaround from the 6.9-percent expansion recorded in the same period in 2019. The decline was due mainly to lower sales of passenger and commercial vehicles amid consecutive typhoons that affected most of Luzon during the period.

New vehicle sales remain weak

Commercial vehicle sales, which account for about 65.2 percent of total vehicle sales, went down by 36.2 percent y-o-y for the period October-November 2020 from the 7.6-percent increase in the same period in 2019. Commercial vehicles sold during the period reached 31,407 units from 49,228 units in the same period a year ago.

Chart 11. Vehicle Sales

Growth rate in percent



* October to November
Source: Chamber of Automotive Manufacturers of the Philippines, Inc. (CAMPI)

Similarly, passenger car sales decreased by 14.5 percent y-o-y for the period October-November 2020, a reversal from the 5.3-percent growth in the same period in 2019. New passenger car sales accrued to a total of 16,778 units for the period October-November 2020 from 19,634 units in the same period a year ago.

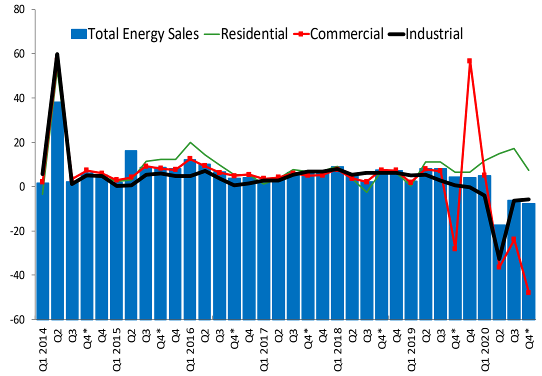
[18] Vehicle sales data is gathered on a monthly basis by the Chamber of Automotive Manufacturers of the Philippines (CAMPI) and the Truck Manufacturers Association (TMA). CAMPI represents the local assemblers and manufacturers of vehicle units in the Philippine automotive industry. The following are the active members of CAMPI: (1) Asian Carmakers Corp., (2) CATS Motors, Inc., (3) Columbian Autocar Corp., (4) Honda Cars Philippines, Inc., (5) Isuzu Philippines Corp., (6) Mitsubishi Motors Philippines Corp., (7) Nissan Motor Philippines Corp., (8) Suzuki Philippines Inc., (9) Toyota Motor Philippines Corp. and (10) Universal Motors Corp.

Energy Sales. Energy sales of Meralco contracted by 7.7 percent y-o-y in Q4 2020 (October – November), a reversal from the 4.2-percent growth in the same period a year ago.

Energy sales remain in contraction

The contraction in Q4 2020 continues to reflect the impact of the implementation of the quarantine protocols implemented in Meralco's service area. Energy sales from the residential sector increased by 7.5 percent, while energy sales from the commercial and industrial sectors contracted by 22.8 percent and 5.8 percent.

Chart 12. Energy Sales
Year-on-year growth in percent



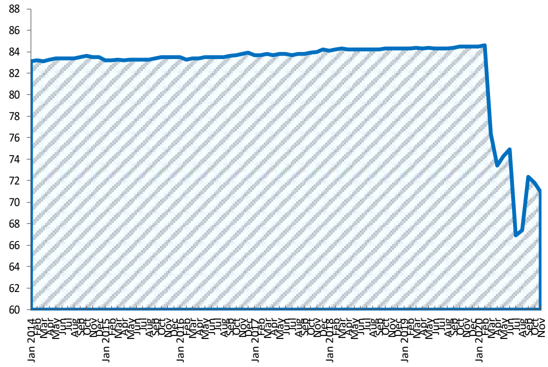
* October to November
Source: Meralco, BSP calculations

Capacity Utilization. The average capacity utilization rate of the manufacturing sector stood at 70.9 percent in November 2020, lower than the month-ago level of 71.8 percent (revised) based on the Philippine Statistics Authority's Monthly Integrated Survey of Selected Industries (MISSI). Of the 410 respondent-establishments, only 42.0 percent operated at a capacity of at least 80.0 percent in November 2020.

Utilization rate in November 2020 remains below optimal capacity

The 410 respondents are significantly lower than the October level at 572 firms (revised), and only takes account for about 45.9 percent of the 893 sample establishments.

Chart 13. Monthly Average of Capacity Utilization for Manufacturing
In percent



Source: PSA

The decrease in average capacity utilization in November was in line with the contractions of both volume and value indices. Only six (out of the 20) major industries in the sector operated at least at the 80.0-percent capacity level that include: machinery except electrical (91.7 percent), electrical machinery (85.4 percent), furniture and fixtures (84.4 percent), textiles (83.1 percent), rubber and plastic products (82.3 percent), and footwear and wearing apparel (81.6 percent). Eight major industries operated at the 70 to 79 percent capacity range namely, non-metallic mineral products (79.7 percent), leather products (78.3 percent), paper and paper products (78.3 percent), wood and wood products (78.2 percent), printing (75.0 percent), food manufacturing (72.4 percent), transport equipment (71.5 percent), and miscellaneous manufactures (70.8 percent).

Volume and Value of Production. The preliminary MISSI data for November 2020 contracted for the ninth consecutive month in both volume and value indices despite the relaxation of quarantine measures. Firms' average capacity utilization also dipped, as the number of establishments operating below 80 percent remained higher since the enforcement of lockdown restrictions in March 2020.

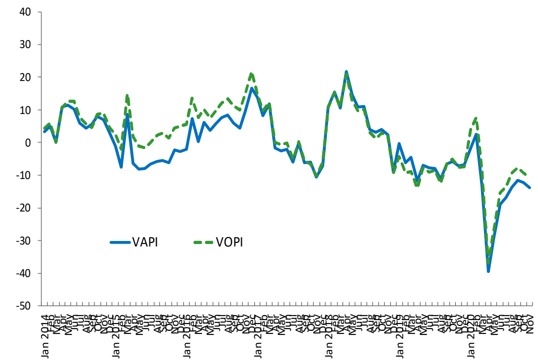
Preliminary results of the MISSI showed that volume of production index (VoPI) decelerated by 10.8 percent y-o-y in November 2020, faster than the contraction of 9.3 percent (revised) in October.

Manufacturing output continues to deteriorate

Of the 20 major industries, 16 sub-sectors posted negative growth rates: petroleum products (-61.9 percent), tobacco products (-58.6 percent), printing (-51.5 percent), leather products (-43.5 percent), furniture and fixtures (-41.1 percent), footwear and wearing apparel (-32.9 percent), machinery except electrical (-30.0 percent), fabricated metal products (-30.0 percent), non-metallic mineral products (-29.1 percent), textiles (-20.8 percent), beverages (-20.7 percent), transport equipment (-17.7 percent), rubber and plastic products (-11.9 percent), food manufacturing (-1.3 percent), electrical machinery (-0.7 percent), and paper and paper products (-0.3 percent).

Chart 14. Volume and Value Indices of Manufacturing Production

Year-on-year in percent



Source: PSA

Likewise, the value of production index (VaPI) declined faster by 13.8 percent in November 2020 from a 12.3-percent (revised) slump in the previous month. This was attributed to the contraction of 17 out of 20 sub-sectors: petroleum products (-66.0 percent), tobacco products (-56.9 percent), printing (-50.8 percent), leather products (-43.4 percent), machinery except electrical (-34.0 percent), footwear and wearing apparel (-33.9 percent), non-metallic mineral products (-30.4 percent), furniture and fixtures (-30.4 percent), fabricated metal products (-29.2 percent), transport equipment (-23.2 percent), textiles (-20.8 percent), beverages (-16.6 percent), rubber and plastic products (-15.0 percent), paper and paper products (-10.4 percent), electrical machinery (-3.3 percent), wood and wood products (-1.7 percent), and food manufacturing (-0.4 percent).

Business Expectations. Business confidence on the economy improved for Q4 2020 as the overall confidence index (CI)[19] of the Business Expectations Survey (BES)[20] reverted to the positive territory at 10.6 percent from -5.3 percent in Q3 2020. The positive reading indicates that respondents with optimistic views increased and outnumbered those with pessimistic views.

Business confidence improves in Q4 2020

The respondents' optimism for Q4 2020 was attributed to the reopening of businesses and adapting to the *new normal*; easing of community quarantines nationwide; seasonal factors such as uptick in demand during the holiday season and start of milling season; and increase in volume of sales and orders.

The sentiment of businesses in the Philippines mirrored the business outlook in Australia and Chile, which turned optimistic. Further, business confidence in Brazil, Canada, and US was more buoyant, while that of Bulgaria and Germany was less favorable. However, the sentiment of businesses in Croatia, Denmark, Euro Area, France, Greece, Hong Kong, Hungary, Israel, Mexico, Netherlands, New Zealand, South Korea, and Thailand was pessimistic, while that of the UK was neutral.

[19] The CI is computed as the percentage of firms that answered in the affirmative less the percentage of firms that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.

[20] The Q4 2020 BES was conducted during the period 6 October-24 November 2020. There were 1,513 firms surveyed nationwide. Samples were drawn from the Top 7,000 Corporations ranked based on total assets in 2016 from the Bureau van Dijk (BvD) database, consisting of 586 companies in NCR and 928 firms in AONCR, covering all 16 regions nationwide.

Table 8. Business Expectations Survey Current Quarter Next Quarter

BUSINESS OUTLOOK INDEX		Current Quarter	Next Quarter	Next 12 Months
2017	Q1	39.4	47.2	-
	Q2	43.0	42.7	-
	Q3	37.9	51.3	-
	Q4	43.3	39.7	-
2018	Q1	39.5	47.8	-
	Q2	39.3	40.4	-
	Q3	30.1	42.6	-
	Q4	27.2	29.4	-
2019	Q1	35.2	52.0	-
	Q2	40.5	47.6	-
	Q3	37.3	56.1	-
	Q4	40.2	40.3	59.6
2020	Q1	22.3	42.3	55.8
	Q2	-	-	-
	Q3	-5.3	16.8	37.5
	Q4	10.6	37.4	57.7

Source: BSP

For the quarter ahead (Q1 2021), improved business sentiment persisted, with the next quarter CI rising to 37.4 percent from the previous quarter's survey result of 16.8 percent. Respondents' more buoyant outlook for Q1 2021 was associated mainly with expectations of reopening of firms and adapting to the new normal; gradual recovery from the COVID-19 pandemic, particularly with the anticipated availability of the vaccine; relaxing the quarantine restrictions; and rise in sales and orders. Similarly, the business outlook on the country's economy was more optimistic for the next 12 months as the CI rose to 57.7 percent from the Q3 2020 survey result of 37.5 percent due to the aforementioned reasons.

Consumer Expectations.[21] Based on the Q4 2020 Consumer Expectations Survey (CES), the country's consumer outlook was less pessimistic for Q4 2020 as the overall CI[22] increased to -47.9 percent from -54.5 percent in Q3 2020. The improved CI, albeit remaining negative, indicates that the number of households with optimistic views increased, but was still lower than those with pessimistic views.

[21] The CES is a quarterly survey of a random sample of more than 5,500 households in the Philippines. The Q4 2020 CES was conducted during the period 1- 13 October 2020.

[22] The CI is computed as the percentage of households that answered in the affirmative less the percentage of households that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.

Consumer outlook is less pessimistic in Q4 2020

According to respondents, their improved outlook during the current quarter was brought about by their expectations of availability of more jobs and permanent employment; additional and high income; effective government policies and programs such as the Social Amelioration Program (SAP) and the Plant, Plant, Plant Program; and less community restrictions, reopening of businesses, and end to COVID-19 pandemic.

Table 9. Consumer Expectations Survey Current Quarter Next Quarter Next 12 Months

CONSUMER OUTLOOK INDEX		Current Quarter	Next 3 Months	Next 12 Months
2017	Q1	8.7	16.5	31.7
	Q2	13.1	13.6	34.3
	Q3	10.2	17.8	33.7
	Q4	9.5	17.5	32.0
2018	Q1	1.7	8.8	24.0
	Q2	3.8	8.7	23.1
	Q3	-7.1	3.8	13.0
	Q4	-22.5	-0.8	10.7
2019	Q1	-0.5	10.7	28.4
	Q2	-1.3	9.7	25.2
	Q3	4.6	15.8	29.8
	Q4	1.3	15.7	26.4
2020	Q1	1.3	9.2	19.9
	Q2	-	-	-
	Q3	-54.5	-4.1	25.5
	Q4	-47.9	4.3	23.6

Source: BSP

The sentiment of consumers in the Philippines was comparable to the less pessimistic outlook of consumers in Japan, South Korea, and Thailand for Q4 2020. Meanwhile, consumer outlook in Czech Republic, Euro Area, France, Indonesia, Poland, Switzerland, Taiwan, UK, and US were more pessimistic.

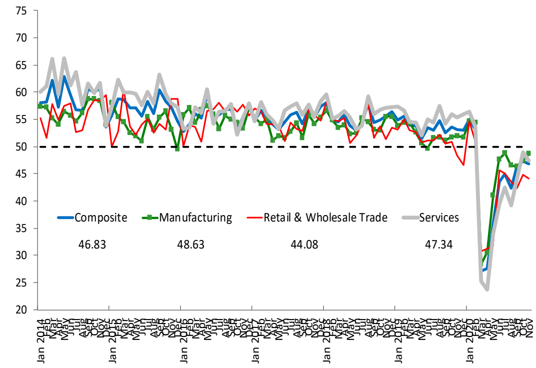
For the next quarter (Q1 2021), the CI reverted to positive territory at 4.3 percent from the Q3 2020 survey result of -4.1 percent for Q4 2020. Consumers cited their anticipation of availability of more jobs and more working family members; additional and high income; an end in the COVID-19 pandemic as well as the discovery of COVID-19 vaccine; and reopening of businesses as reasons behind their optimism for the said period. Meanwhile, consumer's outlook for the next 12 months remained optimistic as the CI was at 23.6 percent, although slightly lower than the previous quarter's survey result of 25.5 percent.

Purchasing Managers' Index.[23] The composite PMI in November 2020 remained below the 50-point expansion threshold[24] at 46.8, lower by 0.4 index point than the October PMI of 47.2. Despite the slower contraction of the manufacturing index, the composite PMI dipped anew as the services and retail and wholesale sectors contracted faster in November. The tepid recovery of demand and limited mobility options continued to temper economic activities, but respondent-firms are optimistic that the business environment will improve in December.

Composite PMI remains below the expansion threshold

The manufacturing PMI increased by 1.6 index points to 48.9 in November 2020 from 47.3 in October, in line with business managers' expectations of an uptick. The sector improved in November month-on-month (m-o-m) as the government eased the protracted lockdown measures implemented within economy's key regions. The New Orders Index (at a PMI of 48.9) and Employment Index (47.2) increased, while the Production Index (46.7) and Inventories Index (45.3) worsened as volatile demand conditions and the fulfillment of new orders depleted the existing stocks of raw materials and finished goods. The Supplier Deliveries Index likewise increased by 3.1 index points to a PMI of 55.4, indicative of a longer delivery lead time, despite the implementation of looser quarantine restrictions as the average utilization rate of factories remains low to observe social distancing measures through skeletal workforces. Meanwhile, firms with export volume of up to 25 percent and more than 50 percent of total revenues breached the 50-point expansion threshold with PMIs of 50.4 and 55.2, respectively. By contrast, non-exporting firms and those whose export volume account for 26-50 percent of total revenues remained below the threshold at 45.8 and 44.6, respectively. On a per sector basis, eight out of twelve subsectors reported expansions namely, fabricated metals (at a PMI of 54.5), food and beverages (53.9), motor vehicles (53.2), fuel (52.2), communication and medical equipment (51.3), publishing and printing (51.1), paper and paper products (50.4), and rubber and plastics (50.2). By contrast, four sectors posted contractions: non-metallic minerals, basic metals, textiles, and machinery. Prospects are assessed to be favorable for the sector in December.

Chart 15. Purchasing Managers' Index



Source: Philippine Institute of Supply Management (PISM)

Meanwhile, the retail and wholesale PMI decelerated slightly by 0.7 index point to 44.1 in November from 44.8 a month ago. The faster contraction of the Purchases Index as well as the slower expansion of the Supplier Deliveries Index were partly offset by the increases of Sales Revenues, Employment, and Inventories as transport operations resume, albeit at a slower pace to facilitate mobility of goods within vital areas of commerce. Lead time and purchases indices decreased the most, losing as much as 4.6 index points and 4.1 index points, respectively. The notable decline in lead time is indicative of the ongoing normalization of operations as supply chains recover from the disruptions of strict quarantine measures and limited factory operations. On a per sector basis, the PMI of the retail subsector dipped by 2.0 index points to 43.23 in November from 45.20 in October due to the continued contraction of Purchases, Sales Revenues, Employment, and Inventories. Likewise, the PMI of the wholesale subsector decelerated due to the notable declines of Purchases, Sales Revenues, Employment, and Inventories, while the Supplier Deliveries Index remained in expansion mode. Managers are anticipating an improvement for the retail and wholesale sector in December.

The services PMI also decreased by 1.6 index points to 47.3 from the previous month's 48.9. All the indices contracted faster, except for Employment. In particular, Average Price Charge,

[23] Data based on the monthly purchasing managers' index report of the Philippine Institute for Supply Management (PISM).

[24] The actual formula used to calculate the PMI assigns weights to each common element and then multiplies them by 1.0 for improvement, 0.5 for no change, and 0 for deterioration. As a result, an index above 50 indicates economic expansion, and an index below 50 implies a contraction. PMI surveys are conducted on the last week of the month.

Outstanding Business, and Business Activity lost as much as 5.2, 4.3, and 2.1 index points, respectively. The special work arrangements necessary for the observance of social distancing and other health protocols contributed to the declines in the performance of the services sector as operations remained limited. On a per sector basis, seven out of fourteen subsectors reported expansion namely, banking and financials (at a PMI of 56.8), provident/insurance (59.8), construction (52.0), hotels and restaurants (53.4), transportation including travel agency (52.0), utilities (54.8), and miscellaneous business (52.5). By contrast, seven sectors posted contractions: real estate, renting of goods, business/knowledge processing, health and social work, education, postal and telecommunications, as well as recreational, cultural, and sports-related activities. Despite the sector's sluggish performance in November as most indices faltered, services managers are expecting business activities to improve in December.

External Demand[25]

Exports. Exports of goods declined by 6.5 percent y-o-y in Q3 2020, an improvement from the 29.2-percent contraction in Q2 2020 but still a reversal from the 2.2-percent expansion in Q3 2019.

Exports of goods improve but remain in the negative in Q3 2020

The lower outbound shipments of coconut products, fruits and vegetables, other agro-based products, forest products, petroleum products, and manufactures outpaced the growth in exports of sugar products and mineral products in Q3 2020.

Table 10. Export of Goods
Growth rate in percent, year-on-year

COMMODITY GROUP	2019	2020	
	Q3	Q2	Q3
Coconut Products	-9.9	-28.4	-3.4
Sugar and Products	-89.0	-60.0	1,370.5
Fruits and Vegetables	41.8	-15.7	-20.2
Other Agro-Based Products	-5.9	-14.2	-13.6
Forest Products	48.5	-44.9	-14.1
Mineral Products	9.0	-9.7	10.0
Petroleum Products	-66.2	713.1	-98.4
Manufactures	1.5	-31.6	-6.2
Special Transactions	-2.6	-46.8	-27.9
Total Exports	**2.2**	**-29.2**	**-6.5**

Source: BSP staff computations based on the Foreign Trade Statistics of the PSA

Imports. Imports of goods fell by 20.2 percent y-o-y in Q3 2020, an improvement from the 43.4-percent drop in Q2 2020, but lower than the 4.0-percent contraction in Q3 2019.

Similarly, decline in imports of goods continue albeit slower

The decline in inward shipments during the period was due largely to lower imports of capital goods, raw materials and intermediate goods, minerals and lubricant, and consumer goods.

Table 11. Import of Goods
Growth rate in percent, year-on-year

COMMODITY GROUP	2019	2020	
	Q3	Q2	Q3
Capital Goods	4.6	-41.2	-24.6
Raw Materials and Intermediate Goods	-13.3	-33.3	-8.8
Mineral Fuels and Lubricants	-9.7	-74.8	-42.3
Consumer Goods	5.2	-46.1	-20.9
Special Transactions	41.5	-38.6	5.7
Total Imports	**-4.0**	**-43.4**	**-20.2**

Source: BSP staff computations based on the Foreign Trade Statistics of the PSA

[25] International Merchandise Trade Statistics (IMTS) concept

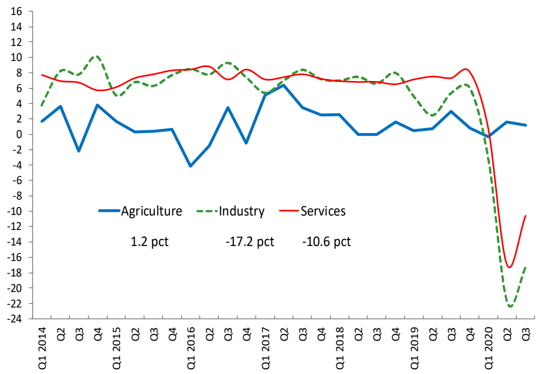
Aggregate Supply

On the production side of the economy, agriculture was the sole sector which recorded growth, contributing 0.1 ppt. Meanwhile, the industry and services sectors contributed -4.9 ppts and -6.7 ppts, respectively, to total GDP growth in Q3 2020.

Services and industry sectors contract supply-side activity

The agriculture sector grew by 1.2 percent in Q3 2020, slower than the 3.0-percent and 1.6-percent increments in Q3 2019 and Q2 2020, respectively. This was due to the lower production of sugarcane (4.9 percent in Q3 2020 from 72.6 percent in Q2 2020), corn (4.1 percent from 15.6 percent), and pineapple (-5.4 percent from 5.3 percent), as well as lower output for support activities to agriculture, forestry and fishing (2.7 percent from 7.8 percent).

Chart 16. Gross Domestic Product by Industrial Origin
At constant 2018 prices



Source: PSA

The growth in agricultural output was primarily on account of increased production in the crops particularly *palay* (15.4 percent in Q3 2020 from 7.2 percent in Q2 2020), and fisheries subsectors (2.1 percent in Q3 2020 from 1.0 percent in Q2 2020). The double-digit expansion rate in *palay* production was attributed to the slightly higher yield prospects of 4.12 metric tons (MT) in Q3 2020 from 4.11 MT in Q2 2020, as well as the implementation of the Plant, Plant, Plant Program and the Rice Competitiveness Enhancement Fund (RCEF) of the Department of Agriculture (DA). Meanwhile, the improvement in fishing and aquaculture was due to output increments for bigeye tuna, *Bali sardinella*, and blue crab.

Table 12. Gross Domestic Product by Industrial Origin
At constant 2018 prices; growth rate in percent

BY INDUSTRIAL ORIGIN	2019 Q3	2020 Q2	2020 Q3
Agri., Hunting, Forestry and Fishing	3.0	1.6	1.2
Industry Sector	5.4	-21.8	-17.2
Mining and Quarrying	-3.5	-22.8	-15.6
Manufacturing	0.9	-20.7	-9.7
Electricity, Gas and Water Supply			
Construction	15.3	-30.4	-39.8
Service Sector	7.3	-17.0	-10.6
Wholesale and Retail Trade and Repair of Motor Vehicles and Motorcycles	8.3	-13.9	-5.4
Transportation and Storage	7.9	-58.5	-28.1
Accomodation and Food Service Activities	6.0	-67.2	-52.7
Information and Communcation	5.5	9.4	0.8
Financial and Insurance Activities	12.8	5.4	6.2
Real Estate and Ownership of Dwellings	6.2	-29.7	-22.5
Professional and Business Services	2.7	-15.9	-9.4
Public Administration and Defense; Compulsory Social Security	8.7	7.1	4.5
Education	2.1	-15.0	-21.4
Human Heath and Social Work Activities	5.8	-15.1	-4.0
Other Services	5.2	-63.0	-53.4

Source: PSA

The industry sector declined by 17.2 percent in Q3 2020, a reversal of the 5.4-percent growth in Q3 2019 but less negative than the 21.8-percent contraction in Q2 2020. The slower decline was attributed to the smaller contractions in the performance of the manufacturing, and mining and quarrying subsectors, as well as the positive growth of the electricity, steam, water and waste management subsector.

Manufacturing sector contracted by -9.7 percent in Q3 2020, although slower than the -20.7 percent slump in Q2 2020 as most of the subsectors such as export-oriented manufactures and essential items posted moderate declines in Q3 2020 compared to the previous quarter. Moreover, the manufacturing PMI of the Philippines marginally improved to 50.1 in September 2020, from 48.4 in July and 47.3 in August. Based on the MISSI, VoPI for the entire manufacturing sector also fell by 10.3 percent in Q3 2020, albeit at a slower pace than the 26.6-percent decline in Q2 2020.

Mining and quarrying sector sustained its contraction at -15.6 percent in Q3 2020, although an improvement from the -22.8-percent growth in Q2 2020 largely due to the moderate declines in crude petroleum and natural gas, stone quarrying and other mining and quarrying, nickel ores, and gold and other precious metal ores.

Electricity, steam, water and waste management sector expanded by 0.2 percent in Q3 2020, a reversal from the 6.4-percent contraction in Q2 2020. The growth was brought about by notable improvements in electricity, water supply, waste management, and steam. The NGCP reported a slower decline in transmission energy sales7, while Meralco recorded an increase in energy sales for the residential segment owing to the start of online classes and the continuation of work-from-home arrangements. Energy sales in commercial and industrial segments also went up following the lifting of operational restrictions among businesses.

The services sector declined by 10.6 percent in Q3 2020, albeit less than the 17.0-percent contraction posted in Q2 2020. This was primarily due to the slower declines in all subsectors particularly transportation and storage, wholesale and retail trade, as well as financial and insurance activities. Trade and repair of motor vehicles, motorcycles, personal and household goods sector continued to contract albeit at a slower pace to -5.4 percent in Q3 2020 from -13.9 percent in Q2 2020, as performance of all subsectors improved particularly, for retail trade, sale and repair of motor vehicles, and wholesale trade.

Performance of the transport and storage sector fell by 28.1 percent in Q3 2020 from -58.5 percent in Q2 2020. Postal and courier activities recovered, while the rest of the subsectors such as land, air, and water transport, as well as warehousing and storage, still contracted in Q3 2020 although at lesser degree compared to the previous quarter. Public transportation continued to operate at lowered capacity with the imposition of quarantine measures. Meanwhile, the air transport sector remained sluggish, as the number of international and domestic passengers continued to drop in Q3 2020.

Accommodation and food service activities declined by 52.7 percent in Q3 2020, from the 67.2-percent drop in Q2 2020. Food and beverage service activities gradually recovered following the extended operating hours and reopening of dine-in services in areas under General Community Quarantine (GCQ) and Modified General Community Quarantine (MGCQ). For accommodation, the contraction was attributed to the limited services provided by hotels and other accommodation establishments, which only catered to service frontliners, stranded Filipinos and foreign nationals, returning overseas Filipino workers (OFWs), non-OFWs, and locally stranded individuals under mandated quarantine.

Financial and insurance activities rose to 6.2 percent in Q3 2020 from 5.4 percent in Q2 2020 due to the improvements on the non-bank financial intermediation and insurance which offset the slowdown in banking institution and activities auxiliary to financial intermediation. o Real estate and ownership dwellings continued to decline to 22.5 percent in Q3 2020 from -29.7 percent in Q2 2020. In particular, shopping center revenues dropped by 51 percent due to mall closures, rent concessions, and lower foot traffic despite the resumption of mall operations. Likewise, property development revenues decreased by 57 percent due to limited selling and construction activities.

Growth in the professional and business service activities sector improved at -9.4 percent in Q3 2020 from -15.9 percent in Q2 2020. This was attributed to the less stringent quarantine measures implemented in most areas of the country which allowed subsectors to operate from 50 to 100 percent capacity, except for travel agencies, tour operators, reservation service and related activities.

Health and social work sector continued to plunge to -4.0 percent in Q3 2020 from -15.1 percent in Q2 2020. The smaller contraction was due to the growth performance in private health in Q3 2020, which offset the contraction in public health and social work.

The contraction in other services remained in double-digits, albeit at a lesser degree at -53.4 percent in Q3 2020 from -63.0 percent in Q2 2020. This was largely due to slower declines noted for arts, entertainment and recreation, and other services activities brought about by the easing of community quarantine restrictions in most areas during Q3 2020.

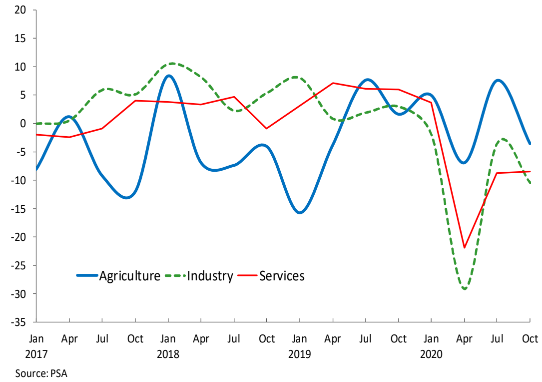
Labor Market Conditions

The Philippine labor market further improved in the fourth quarter of 2020 based on the October 2020 round of the Labor Force Survey (LFS). Compared to the previous quarter, employment rate inched up to 91.3 percent (from 90.0 percent), unemployment rate declined to 8.7 percent (from 10.0 percent), underemployment rate decreased to 14.4 percent (from 17.3 percent), and youth unemployment rate dropped to 19.4 percent (from 22.4 percent). While these employment indicators are still a deterioration compared to their rates in October 2019[26], the resulting full year unemployment rate at 10.4 percent is still better than the 11.0-13.0 percent unemployment rate projection of the government for 2020.[27]

Employment conditions improve in Q4 2020

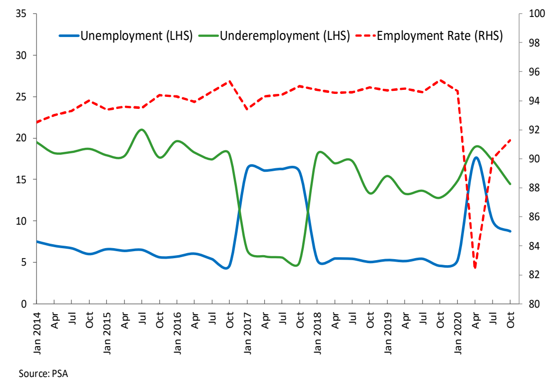
The employment rate in October 2020 was equivalent to 39.8 million employed individuals, 6.3 percent lower compared to 42.5 million employed persons in the same period a year ago. The 2.7 million employment loss mainly came from the services sector, which contracted by 7.9 percent primarily due to lower employment in accommodation and food service activities as well as transportation and storage subsectors. Employment in the industry sector also declined by 10.2 percent largely on account of weaker employment in manufacturing and construction subsectors. However, these were partly offset by employment gains in the agriculture sector, which posted a 0.7 percent growth due to higher employment in fishing and aquaculture. Compared to July 2020, the country recorded an employment loss of 1.5 million as typhoons hit the agriculture sector while inter-province transport restrictions affected the industry sector.[28] The lower employment was also due to reduced labor force participation rate (LFPR) (58.7 percent in October 2020 from 61.9 percent in July 2020), which can be attributed to a number of factors such as higher overseas Filipinos remittances and the need for parents to accompany their children in blended learning from home.

Chart 17. Employment by Sector
in percent



The unemployment rate in October 2020 translated to 3.8 million unemployed individuals or 1.8 million additional workers who lost their jobs from the same period a year ago. Relative to the previous quarter, the number of unemployed declined by 0.8 million, although this was also partly attributed to lower LFPR during the quarter. In terms of educational attainment, majority of the unemployed were junior high school graduates (26.4 percent) and college graduates (23.9 percent share). In terms of age, majority of unemployed was the 15-24 age group or the youth (34.7 percent), followed by the 25-34-year-old age group (32.8 percent). The number of unemployed youth increased by 38.3 percent during the period.

Chart 18. Unemployment, Underemployment and Employment Rate
in percent



[26] In October 2019, employment rate was 95.4 percent while unemployment, underemployment, and youth unemployment rates were at their lowest levels at 4.6 percent, 12.8 percent, and 12.9 percent, respectively.
[27] Development Budget Coordination Committee (2020), "Table A.1. Macroeconomic Parameters, 2019-2022," Budget of Expenditures and Sources of Financing FY 2021.
[28] NEDA (2020), "'PH Labor Market Shows Further Signs of Recovery," 3 December.

Similar with underemployment rate, other aspects of employment quality worsened in the last quarter of 2020 compared to a year ago levels, but improved relative to the previous quarter. The share of remunerative work or wage and salary workers declined to 62.5 percent in October 2020 from 64.7 percent a year ago, but higher than 60.4 percent in July 2020. The overall mean hours of work also fell to 40.8 in October 2020 from 42.0 in October 2019, although an increase from 38.2 in July 2020. Nonetheless, the government intends to manage risks more and further open the economy safely to restore jobs and economic activities in 2021.

II. Monetary and Financial Market Conditions

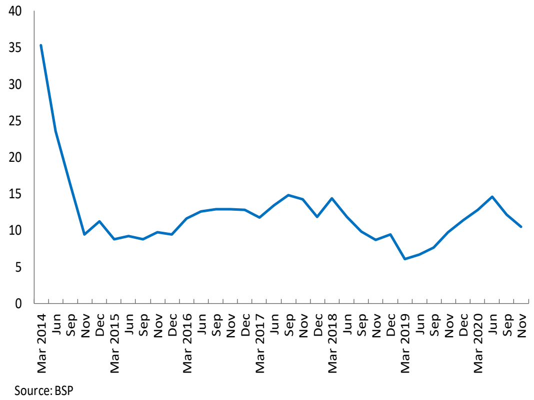
Domestic Liquidity

Domestic liquidity (M3) expanded by 10.5 percent y-o-y in November 2020 to ₱13.7 trillion, slower than the 12.2-percent (revised) expansion as of end-Q2 2020.

Domestic liquidity growth eases in November

Domestic claims grew by 6.7 percent in November from 8.1 percent as of end-Q2 2020 as bank lending remained weak. Meanwhile, net claims on the central government expanded by 40.7 percent in November from the 45.9-percent growth as of end-Q2 2020. The expansion reflects partly the sustained borrowings by the National Government (NG).

Chart 19. Domestic Liquidity
Year-on-year growth rates in percent



Net foreign assets (NFA) in peso terms grew by 22.9 percent y-o-y in November from a growth of 20.5 percent in end-Q2 2020. The expansion in the BSP's NFA position reflected the increase in gross international reserves during the month. Meanwhile, the growth in the NFA of banks increased as banks' foreign liabilities contracted mainly on account of foreign bills payables.

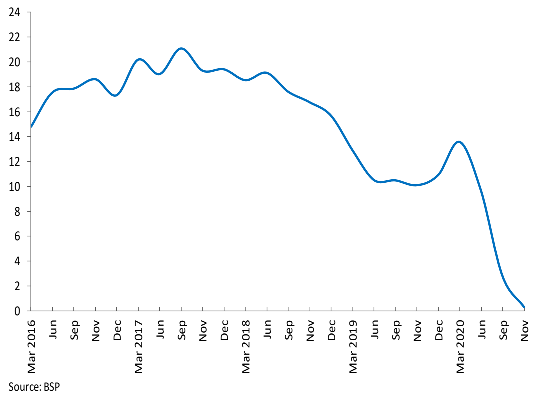
Bank Lending

Outstanding loans of commercial banks, net of RRP placements with the BSP, grew by 0.3 percent y-o-y in November 2020, slower than the 2.6-percent growth rate posted at end-Q3 2020 and the 10.9-percent growth rate reported in end-Q4 2019. Bank lending growth waned in November as the COVID-19 crisis continued to dampen consumer spending and business activity.

Lending growth eases anew amid dampened consumer spending and business activities

Loans for production activities grew by 0.5 percent y-o-y in November 2020 from 2.3 percent in end-Q3 2020 and 9.1 percent in end-Q4 2019. Outstanding loans to key industries declined further, particularly wholesale and retail trade and repair of motor vehicles and motorcycles and manufacturing.

Chart 20. Loans Outstanding of Commercial Banks
Year-on-year growth rates in percent



Similarly, growth in consumer loans declined to 7.1 percent in November 2020 from 9.8 percent in end-Q3 2020 and 27.5 percent in end-Q4 2019, due largely to the slowdown in credit card loans and the continued contraction in motor vehicle loans during the month.

Monetary Operations

As of end-Q4 2020, total outstanding amount absorbed in the BSP liquidity facilities stood at ₱2.0 trillion. Bulk of the BSP's liquidity-absorbing monetary operations had been through the overnight deposit facility (ODF), comprising about 57.0 percent of the combined outstanding amount of liquidity absorbed through the BSP liquidity facilities. Meanwhile, placements in the term deposit facility (TDF), reverse repurchase agreement (RRP) facility, BSP Securities facility (BSP-SF) made up 16.3 percent, 15.5 percent, and 11.2 percent, respectively.

The average weekly total offer volume in the TDF auctions was higher at about ₱489.2 billion in Q4 2020 relative to ₱310.8 billion average weekly volume offered in the previous quarter. The average bid-to-cover ratios for the 7-, 14-, and 28-day tenors were recorded at 1.1, 1.3, and 1.8. There was only one 28-day TDF auction during the quarter as the BSP started migrating funds from the 28-day TDF to 28-day BSP Securities starting with the 16 October 2020 auction. Meanwhile, the average bid-to-cover ratio for the daily RRP offerings was at around 4.0 during the quarter from 4.1 in Q3 2020.

Since the maiden auction of BSP Securities on 18 September 2020, market reception has been positive on the issuance of BSP Securities particularly the 28-day BSP Bills (BSPB). Thus far, the results of the weekly auctions of BSP Securities reflected sustained strong demand amid ample liquidity in the financial system. In Q4 2020, total subscription amounted to around ₱1.420 trillion or about 1.7 times the ₱840.0-billion aggregated offer amount.

Credit Conditions

Credit Standards. Results of the Q4 2020 Senior Bank Loan Officers' Survey (SLOS)[29] showed that majority of respondent banks maintained their overall credit standards for loans to both enterprises and households during the quarter based on the modal approach.[30] The latest survey results reflected a slight improvement compared to the Q3 2020 survey where almost half of the respondent banks stated that they tightened credit standards amid the continued economic and business disruptions caused by the ongoing COVID-19 pandemic.

Meanwhile, results based on the diffusion index (DI) approach,[31,32] continued to indicate a net tightening of overall credit standards for both loans to enterprises and households in Q4 2020 similar to the results in Q3 2020.

Credit standards indicate net tightening among respondents

It is important to note that the Q4 2020 survey was conducted within the government's extension of GCQ measures in Metro Manila and various AONCR. Responses from bank respondents for the SLOS were consolidated between 25 November 2020 and 11 January 2021.

Lending to Enterprises. More than half of the respondent banks (63.4 percent) indicated unchanged overall credit standards for loans to enterprises during the quarter using the modal approach. The DI-based results, however, pointed to a net tightening of lending standards across all

[29] The survey consists of questions on loan officers' perceptions relating to the overall credit standards of universal/commercial banks (U/KBs) and selected large thrift banks (TBs) in the Philippines, as well as to factors affecting the supply of and demand for loans by both enterprises and households. Survey questionnaires were sent to 64 U/KBs and TBs, of which, 45 banks responded to the current survey representing a response rate of 70.3 percent.
[30] In the modal approach, the results of the survey are analyzed by looking at the option with the highest share of responses.
[31] In the DI approach, a positive DI for credit standards indicates that the proportion of respondent banks that have tightened their credit standards exceeds those that eased ("net tightening"), whereas a negative DI for credit standards indicates that more respondent banks have eased their credit standards compared to those that tightened ("net easing").
[32] During the Q1 2010 to Q4 2012 survey rounds, the BSP used the DI approach in the analysis of survey results. Beginning in Q1 2013, the BSP used both the modal and DI approaches in assessing the results of the survey.

borrower firm sizes, specifically, top corporations, large middle-market enterprises, small and medium enterprises, and micro enterprises.

Table 13. General Credit Standards for Loans to Enterprises (Overall)

	2019				2020			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Tightened Considerably	2.1	4.8	4.1	0.0	2.8	20.4	20.5	14,6
Tightened Somewhat	22.9	11.9	12.2	15.2	30.6	49.0	27.3	17.1
Remained Basically Unchanged	**72.9**	**81.0**	**81.6**	**84.8**	**66.7**	**24.5**	**45.5**	**63.4**
Eased Somewhat	0.0	0.0	0.0	0.0	0.0	6.1	6.8	4.9
Eased Considerably	2.1	2.4	2.0	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Diffusion Index for Credit Standards	**22.9**	**14.3**	**14.3**	**15.2**	**33.3**	**63.3**	**40.9**	**26.8**
Number of Banks Responding	**48**	**42**	**49**	**46**	**36**	**49**	**44**	**41**

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").
Source: BSP

As indicated by respondent banks, the observed tightening of overall credit standards was largely due to less favorable economic outlook, deterioration in the profitability of bank's portfolio and profiles of borrowers, and reduced tolerance for risk, among other factors. On specific credit standards, the net tightening of overall credit standards was reflected in terms of reduced credit line sizes; stricter collateral requirements and loan covenants; and increased use of interest rate floors[33]. Meanwhile, some form of easing was revealed in terms of narrower loan margins and longer loan maturities.

In the next quarter, while majority of the respondent banks expect unchanged overall credit standards for loans to enterprises, DI-based results showed that banks continue to expect tighter standards due to a more uncertain economic outlook along with expected deterioration in borrowers' profiles and profitability of banks' portfolios, including banks' lower tolerance for risk.

Lending to Households. Most of the respondent banks (77.8 percent) maintained their overall credit standards for loans extended to households during the quarter. Meanwhile, the DI-based results manifested a net tightening of overall credit standards for household loans particularly for housing and personal/salary loans. Respondent banks cited more uncertain economic outlook, a deterioration in borrowers' profile, and reduced tolerance for risk as the main reasons that contributed to the overall tightening of credit standards for loans to households. By contrast, results based on the DI-approach reflected unchanged credit standards for credit card and auto loans given equal portions of respondent banks reporting that they tightened or eased their overall standards for said types of loans in Q4 2020.

Table 14. General Credit Standards for Loans to Households (Overall)

	2019				2020			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Tightened Considerably	3.3	4.0	3.1	0.0	0.0	39.4	16.7	3.7
Tightened Somewhat	16.7	8.0	6.3	6.9	21.7	21.2	30.0	11.1
Remained Basically Unchanged	**73.3**	**88.0**	**81.3**	**89.7**	**69.6**	**33.3**	**50.0**	**77.8**
Eased Somewhat	3.3	0.0	9.4	3.4	8.7	6.1	3.3	7.4
Eased Considerably	3.3	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Diffusion Index for Credit Standards	**13.3**	**12.0**	**0.0**	**3.4**	**13.0**	**54.5**	**43.3**	**7.4**
Number of Banks Responding	**30**	**25**	**32**	**29**	**23**	**33**	**30**	**27**

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").
Source: BSP

In terms of specific credit standards, the overall net tightening of credit standards for loans to households was revealed in reduced credit line sizes and stricter loan covenants. Meanwhile, some easing of credit standards for loans to households was also observed in terms of narrower loan margins, less restrictive collateral requirements, longer loan maturities, and decreased use of interest rate floors.

Over the next quarter, majority of respondent banks expect to retain their overall credit standards based on the modal approach. Meanwhile, DI-based results showed respondent banks' anticipation of tighter overall credit standards for household loans due to less favorable economic outlook, expected deterioration in borrowers' profile, and reduced tolerance for risk.

Loan demand. Latest survey results indicated that most of the respondent banks observed an unchanged overall loan demand from enterprises during the last quarter. On the other hand, banks' responses to household loan demand varied widely. At the same time, DI-based results generated mixed results in Q4 2020 as the overall loan demand for businesses pointed to a net increase (specifically for top corporations) while loan demand from households conveyed a net decline across all types of consumer loans.

The overall net increase in loan demand from businesses was attributed by respondent banks to

[33] Interest rate floor refers to the minimum interest rate set by banks for loans. Increased use of interest rate floors implies generally tighter credit conditions. Amid the continuing impact of the health crisis, banks appeared to have increased the use of interest floors for loans, despite the generally sustained decline in market interest rates in Q4 2020, as a safeguard or a precautionary measure against market uncertainty.

higher customers' requirements for inventory financing as businesses reopen,[34] as well as to higher accounts receivable financing needs amidst a decline in corporate clients' internally-generated funds. Meanwhile, respondent banks cited lower household consumption and housing investment as the key factors that contributed to the observed decline in household loan demand.

Loan demand increases for enterprises, declines for households

Over the next quarter, most of the respondent banks anticipate broadly unchanged overall loan demand from both enterprises and households indicating an increase in confidence of firms and consumers amid the gradual rise of economic activities. DI-based results suggested expectations of a further net increase in overall loan demand from enterprises associated largely with corporate clients' higher inventory financing and accounts receivable financing needs, improved economic outlook, and lack of other sources of funds. Similarly, the DI-approach pointed to banks' expectations of a net increase in overall loan demand from households (specifically personal/salary loans) due largely to higher household consumption, lower income prospects, and lack of other sources of funds.

Real Estate Loans. The Q4 2020 survey results also showed that most of the respondent banks reported broadly unchanged overall credit standards for commercial real estate loans (CRELs). Meanwhile, DI-based results continued to indicate a net tightening of overall credit standards for CRELs for the 20th consecutive quarter. Respondent banks pointed to a less favorable economic outlook, a lower tolerance for risk, as well as deterioration in borrowers' profile as the main contributors to the tightening of overall credit standards for CRELs. On specific credit standards, the net tightening of overall credit standards for CRELs continued to reflect wider loan margins, reduced credit line sizes, stricter collateral requirements and loan covenants, increased use of interest rate floors, and shortened loan maturities. Over the next quarter, banks' responses point to expectations of net tighter credit standards for CRELs based on the DI-approach.

Credit standards for real estate loans remain tight

More than half of respondents reported unchanged demand for CRELs in Q4 2020, while DI-based results continued to indicate a net decline in loan demand reflecting a deterioration in customers' economic outlook. In the following quarter, results based on the modal approach pointed to anticipation of a generally unchanged loan demand for commercial real estate loans while the DI-based results showed a net decline in demand for CRELs amid a deterioration in customers' economic outlook.

For housing loans extended to households, most of the respondent banks (65.4 percent) reported unchanged credit standards while DI-based results pointed to a net tightening in Q4 2020. Over the next quarter, DI-based results likewise indicated expectation of net tighter overall credit standards for housing loans amid more uncertain economic prospects, deterioration in borrowers' profile and profitability of bank's portfolio, and lower risk tolerance of banks.

Meanwhile, two-thirds of the respondent banks saw either a decrease or unchanged overall loan demand for housing loans in Q4 2020. DI-based results, however, pointed to a net decline in loan demand for housing loans during the quarter which was expected to persist until Q1 2021, reflecting largely the consumers' reduced appetite for housing investment.

Interest Rates

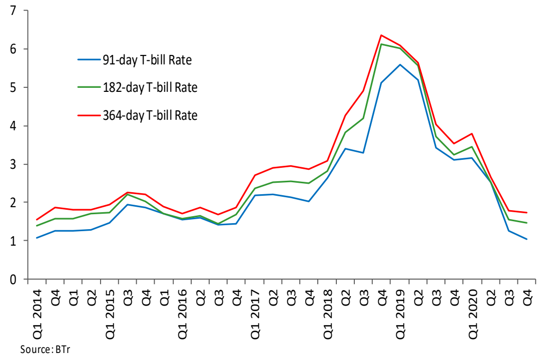
Primary Interest Rates. The weighted average interest rates (WAIRs) for the 91-, 182- and 364-day T-bills in the primary market continued to fall to 1.046 percent, 1.481 percent, and 1.745 percent in Q4 2020 from 1.264 percent, 1.548 percent, and 1.788 percent, respectively, in the previous quarter.

[34] The latest Business Expectations Survey (BES) reflected improved business confidence for Q4 2020 due to the (a) reopening of businesses and adapting to the "new normal", (b) easing of community quarantines nationwide, (c) seasonal factors such as uptick in demand during the holiday season and start of milling season, and (d) increase in volume of sales and orders. The renewed optimism among firms may have contributed to the increase in loan demand due to corporate clients' higher inventory needs.

Treasury bill rates are lower

Amid ample liquidity in the financial system, the results of the auctions during the quarter reflected sustained demand for government securities on market players' expectation of a manageable inflation over the policy horizon.

Chart 21. Treasury Bill Rates
In percent

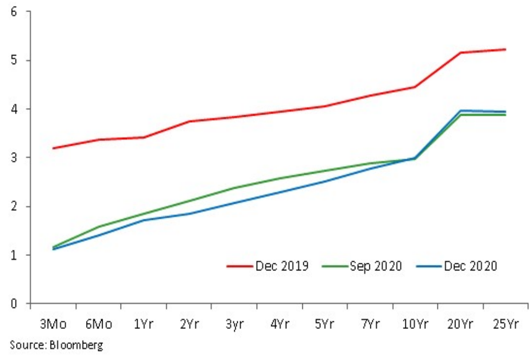


Yield Curve.[35] As of end-December 2020, the secondary market yield for government securities (GS) for all maturities (except for the 10-year, 20-year and 25-year tenors) declined relative to the end-September 2020 levels.

GS yields decline in Q4 2020

Debt paper yields were lower by a range of 4.8 bps for the 3-month GS to 29.3 bps for the 3-year GS compared to end-September 2020 levels. Meanwhile, yields for the 10-year, 20-year and 25-year GS were higher by 1.6 bps, 8.9 bps and 7.4 bps, respectively.

Chart 22. Yields of Government Securities in the Secondary Market
In percent



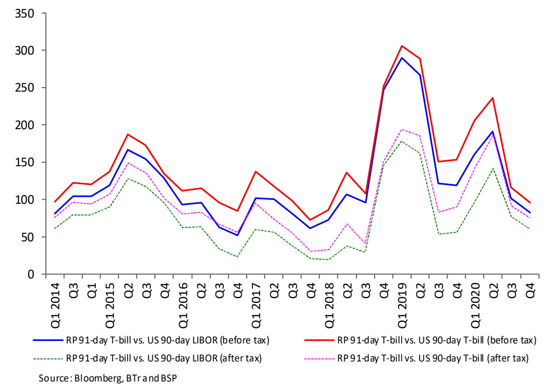
Relative to year-ago levels, the secondary market yields for GS for all maturities decreased by a range of 119.4 bps (for the 20-year GS) to 208.7 bps (for the 3-month GS).

Interest Rate Differentials. The average differentials between domestic and US interest rates, gross and net of tax, narrowed in Q4 2020 relative to the previous quarter.

Interest rate differentials narrow in Q4 2020

The average 91-day RP T-bill rate declined q-o-q by 22.9 bps to 1.043 percent in Q4 2020 from 1.272 percent in Q3 2020. Likewise, the average US 90-day LIBOR and the US 90-day T-bill rate both declined by 2.5 bps, to 0.225 percent and 0.083 percent in Q4 2020. These developments led to narrower positive gross and net of tax differentials between the 91-day RP T-bill rate and US interest rates.

Chart 23. Interest Rate Differentials
Quarterly averages; in basis points



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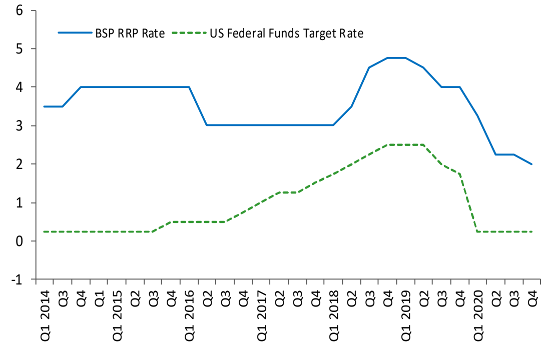
[35] On 29 October 2018, the Bankers Association of the Philippines (BAP) replaced the PDST Reference Rates and launched the PHP BVAL Reference Rates which will be used as the Philippine Peso GS benchmark. The PHP BVAL Reference Rates are calculated by Bloomberg Finance Singapore L.P. and/or its affiliates in an agreement with the BAP.

The positive differential between the BSP's overnight borrowing or RRP rate and the US Fed funds target rate narrowed to a range of 175-200 bps in Q4 2020 from 200-225 bps in Q3 2020, reflecting the impact of the 25-bp decline in the BSP's overnight RRP rate to 2.00 percent on 20 November 2020.

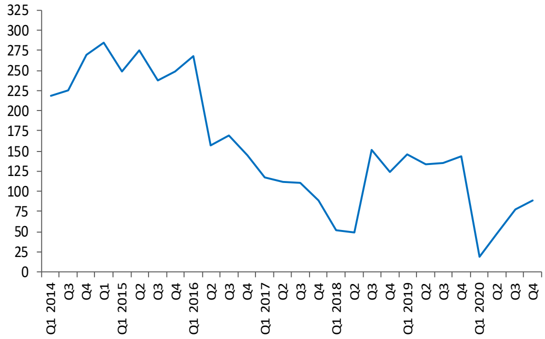
Chart 24. BSP RRP Rate and US Federal Funds Target Rate
In percent



Source: Bloomberg and BSP

Meanwhile, the interest rate differential between the BSP's overnight RRP rate and the US Fed funds target rate adjusted for risk[36] widened further to 89 bps as of end-December 2020 from 78 bps in end-September 2020.

Chart 25. Risk-Adjusted Differentials
In basis points



Source: Bloomberg and BSP

This development could be traced to the 36-bp decline in the country risk premium and the 25-bp decline in the interest rate differential between the BSP's overnight RRP rate and the US federal funds rate.

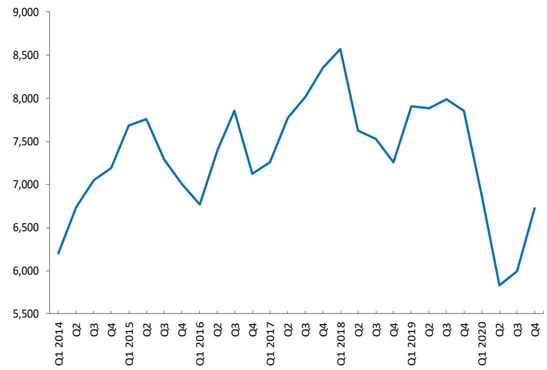
[36] The difference between the 10-year ROP note and the 10-year US Treasury note is used as proxy for the risk premium.

Financial Market Conditions

Financial conditions remained stable in Q4 2020 amid supportive monetary settings and ample financial liquidity. The Philippine stock market continued to improve on expectations of economic rebound while participation in the government bond market remained strong as market participants continued to invest their funds in safe assets. The country's debt spreads continued to narrow as lockdown restrictions eased. Moreover, the banking system continued to exhibit stability during the review quarter.

Stock Market. In Q4 2020, the Philippine Stock Exchange index (PSEi) increased by 12.2 percent q-o-q to average 6,721.75 index points. Expectation of an economic rebound in the near term, further monetary stimulus measures during the review period and the pick-up in consumer spending during the Christmas season lifted investor sentiment. Comparing the end-quarter levels of the PSEi between the third and fourth quarter, the main index surged by 21.8 percent from 5,864.23 index points in end- September to 7,139.71 index points in end-December.

Chart 26. Quarterly Average PSEi
In index points



Source: Philippine Stock Exchange, BSP

The Philippine stock market rallied amidst expectation of an economic rebound in the near term following the easing of quantitative restrictions to reopen the economy, the decline in new daily coronavirus cases in the country, the marked improvement in the earnings performance of companies in the third quarter and increased hopes of an end to the pandemic that followed the announcement of viable COVID-19 vaccines. The BSP's implementation of further monetary stimulus measures (e.g., the ₱540-billion provisional advance to the National Government in October and the 25-bp cut in policy rates in

November) to boost pandemic relief funds also lifted investor sentiment.

The following positive economic developments also helped sustain investors' buying momentum: continued benign inflation that supported policy easing; higher export data in September; the easing of the country's unemployment rate to 8.7 percent in October; improvement in the IHS Markit Philippines Manufacturing PMI to 49.9 in November from 48.5 in October; higher cash remittances from Filipinos abroad in September and October; the y-t-d BOP surplus of US$11.79 billion posted in November; the higher GIR level at US$104.82 billion in end-November; the signing of the ₱4.5-trillion 2021 national budget in December; and the improvement in the Q4 consumer and business confidence.[37] The rally was partly tempered by, among others, concerns over the continued surge in Covid-19 cases overseas and the recent discovery of a new COVID-19 strain in the United Kingdom.[38] This kept the main index lower y-t-d by 4.4 percent.

Other stock market indicators mirrored the general uptrend in the benchmark index during the review period. Total market capitalization rose by 21.4 percent from ₱13.09 trillion in end-September to reach ₱15.89 trillion as of end-December. The price-earnings ratio of listed firms in the PSE also improved from 23.4x to 28.5x during the same period. However, foreign investors continued to withdraw from the local bourse, posting net sales of ₱24.7 billion in Q4, albeit much lower than the ₱35.6-billion net sales recorded in Q3.

In the near term, the PSEi may continue to rise amid expectations of economic recovery due to continued improvement in demand. Although the decline in household income amid the pandemic has forced consumers to tighten their spending, e-commerce and the widespread use of delivery services can help offset the decline in consumer spending. The availability of a vaccine in the second half of 2021 and the low interest rate environment may also further accelerate the recovery of the Philippine economy. Lower corporate income taxes due to the Corporate Recovery and Tax Incentives for Enterprises (CREATE) bill could also potentially boost corporate earnings and lift the benchmark index further.

Government Securities. Results of the T-bill auctions conducted in October - December 2020 continued to show market players' robust demand for government securities with total subscription for the quarter amounting to around ₱918.6 billion or about 4.2 times the ₱220.0-billion aggregated original amounts on offer. Total oversubscription for the T-bill auctions in Q4 2020 reached ₱698.6 billion, higher than the ₱680.5 billion total oversubscription recorded in the previous quarter.

Demand for T-bills continues to be strong

Amid the healthy demand for T-bills, the BTr awarded in full the offered amounts in all the auctions during the quarter. Moreover, the strong demand has allowed the BTr to increase the amount awarded for non-competitive bids for the T-bill auctions on 5 October, 9 November, and 16 November, resulting in higher total accepted amounts than the original weekly offered amount. Meanwhile, the BTr did not offer the 35-day T-bills during the quarter, which was offered twice and six times in Q3 and Q2 2020, respectively.

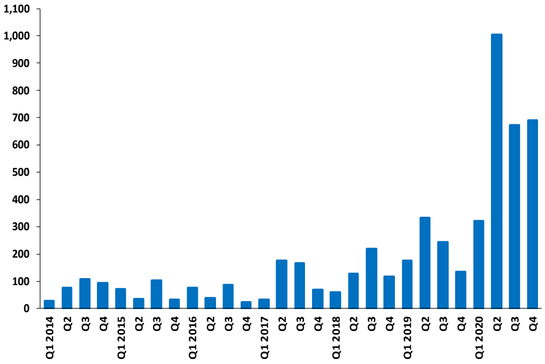
The BTr also offered Premyo Bonds during the quarter. The BTr sold about ₱6.6 billion (around 2.2 times the initial planned issuance of ₱3.0 billion) worth of 1-year Premyo Bonds on the back of strong demand from the public.[39] Similarly, results of the T-bond auctions during the quarter showed sustained strong demand for longer-term GS amid the ample liquidity in the financial system and expectations of a manageable inflation environment over the policy horizon.

[37] On 11 December, the BSP released its latest quarterly Business Expectations Survey, which showed that consumer sentiment improved to -47.9 percent in the current quarter against -54.5 percent in the third quarter due to hopes of a nearing end of the COVID-19 pandemic resulting from vaccine availability, additional employment, and higher income.

[38] In mid-December, the discovery of a new COVID-19 strain in the United Kingdom saw the Philippines join a growing list of countries that have imposed travel restrictions on the European country in efforts to block the entry of the new strain. The UK travel ban, originally imposed starting December 24 until December 31 was subsequently extended by the Philippine President for another two weeks.

[39] The public offer period for the 1-year Premyo Bonds was scheduled on 11 November -11 December 2020 while the settlement date was set on 16 December 2020.

Chart 27. Total Oversubscription of T-bill Auctions
in billion pesos



Source: Bureau of the Treasury

Sovereign Bond and Credit Default Swap (CDS) Spreads. In October, debt spreads narrowed due to improved market optimism as the economy adjusted to the new normal.

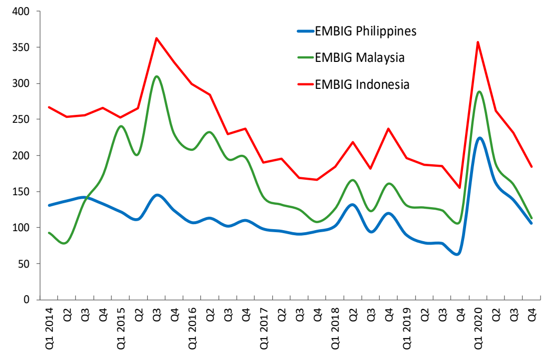
Debt spreads narrow on optimism over response to pandemic

In November, debt spreads continued to tighten as lockdown restrictions eased, enabling some businesses to operate nearer its full capacity.

Debt spreads narrowed further in December, reflecting some recovery of business activities and improved investor sentiment over positive developments on the availability of coronavirus vaccines.

As of 29 December 2020, the extra yield investors demanded to own Philippine sovereign debt over US Treasuries (or the Emerging Market Bond Index Global (EMBIG) Philippines spread) stood at 106 bps from the end-September level of 138 bps.

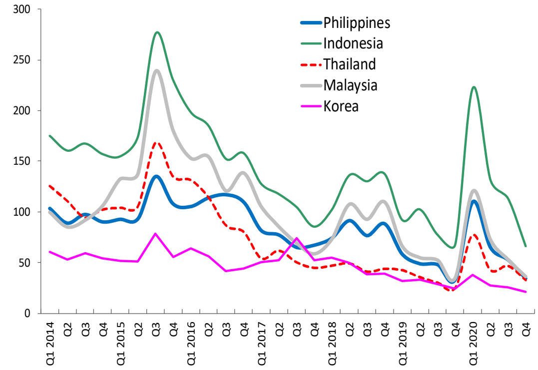
Chart 28. EMBIG Spreads of Selected ASEAN Countries
In basis points



Source: Bloomberg

Similarly, the country's 5-year sovereign CDS decreased to 34 bps from its end-September level of 53 bps. Against other neighboring economies, the Philippine CDS traded narrower than Malaysia's 36 bps and Indonesia's 66 bps but wider than Thailand's 33 bps and Korea's 21 bps spreads.

Chart 29. Five-Year CDS Spreads of Selected ASEAN Countries
In basis points



Source: Bloomberg

Banking System

The Philippine banking system showed resilience and stability in Q4 2020 as the country's economic activities and financial transactions continued to improve following the disruption caused by the pandemic and quarantine measures.

Banking system assets and deposits show moderate growth

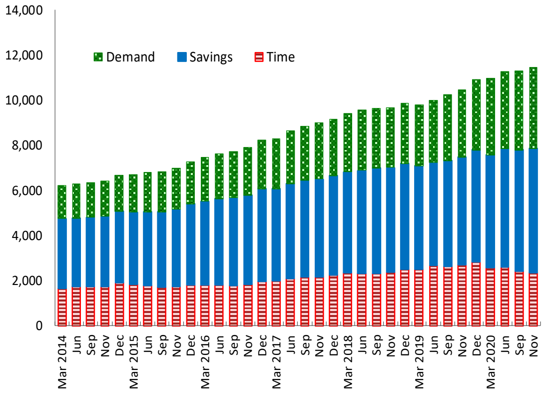
During the review period, banks' balance sheets sustained annual growth in assets and deposits. At the same time, asset quality remained steady while capital adequacy ratios stayed above international standards.[40] Banks maintained

[40] Beginning 1 July 2018, covered institutions (universal banks [UBs], commercial banks [KBs] and their subsidiary banks and quasi-banks [QBs]) must maintain a leverage ratio of no lower than five (5) percent. The leverage ratio is a non-risk based measure, which serves as a backstop to the Capital Adequacy Ratio. It is designed to constrain the potential build-up of leverage in the banking industry and to promote stability of the financial system. Also, the BSP sets an observation period of six months (from 1 July 2018 to 31 December 2018) for the Net Stable Funding Ratio (NSFR). This is to ensure a smooth transition to the new prudential standard and to allow prompt assessment and calibration of the components of the NSFR. Beginning 1 January 2019, however, the covered institutions (U/KBs) shall maintain an NSFR of 100.0 percent on both solo and consolidated bases.

dominance in the financial sector, with U/KBs accounting for about 92 percent of total banks' resources. In terms of the number of head offices and branches/agencies, non-bank financial intermediaries (NBFIs) have the widest physical network, consisting mainly of pawnshops.

Savings Mobilization. Savings deposits remained the primary source of funds for the banking system. Banks' total deposits as of end-November 2020 amounted to ₱11.4 trillion, 9.1 percent and 1.3 percent higher than the levels in end-November 2019 and end-September 2020, respectively.[41]

Chart 30. Deposit Liabilities of Banks
In billion pesos



Source: BSP

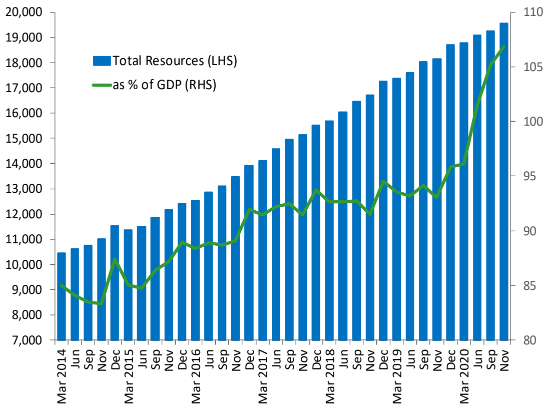
Meanwhile, foreign currency deposits owned by residents (FCD-Residents) reached ₱2.0 trillion as of end-November 2020, 3.6 percent higher than the level a year ago.[42]

Institutional Developments. The total resources of the banking system grew by 7.8 percent to reach ₱19.6 trillion as of end-November 2020 from ₱18.2 trillion a year ago. Relative to the end-September 2020 level, total resources of the banking system likewise increased by 1.6 percent. As a percent of GDP, total resources stood at 106.8 percent.[43]

Total resources of the banking system sustain growth

[41] This refers to the total peso-denominated deposits of the banking system.
[42] FCD-Residents, along with M3, forms part of a money supply measure called M4. Meanwhile, M3 consists of savings deposits, time deposits, demand deposits, currency in circulation, and deposit substitutes.
[43] GDP as of end-September 2020.

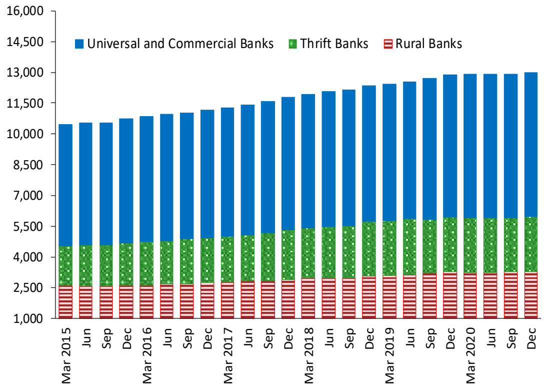
Chart 31. Total Resources of the Banking System
Levels in billion pesos; share in percent



Source: BSP

The number of banking institutions (head offices) as of end-December 2020 declined slightly to 535 offices from its end-September 2020 level of 537 offices. The banks' head offices are comprised of 46 U/KBs, 48 TBs, and 441 rural banks (RBs). During the same period, the operating network (head offices and branches/agencies) of the banking system increased to 12,985 offices from 12,927 offices in end-September 2020.

Chart 32. Number of Banking Institutions

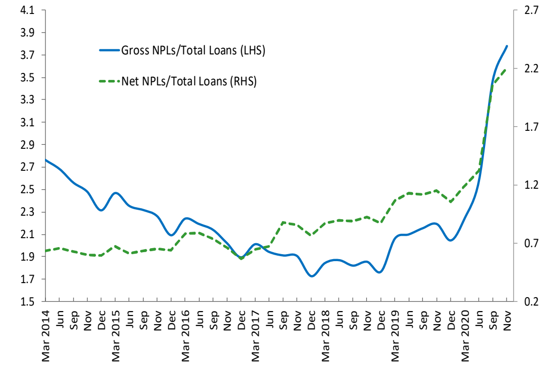


Source: BSP

In terms of asset quality, the Philippine banking system's gross non-performing loans (GNPL) ratio rose to 3.8 percent as of end-November 2020 relative to the 2.2 percent posted a year ago and 3.5 percent posted in end-September 2020.

NPLs rose but remain manageable

Chart 33. Ratios of Gross Non-Performing Loans and Net Non-Performing Loans to Total Loans
In percent



Source: BSP

Similarly, the net non-performing loans (NNPL) ratio increased to 2.2 percent as of end-November 2020 relative to the 1.2 percent and 2.1 percent posted a year- and a quarter- ago.

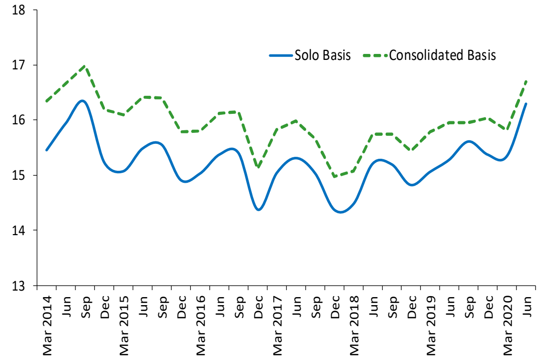
Compared with regional counterparts, the Philippine banking system's GNPL ratio of 3.8 percent was higher with respect to those of South Korea (0.7 percent), Malaysia (1.0 percent), Indonesia (2.9 percent) and Thailand (3.0 percent).[44]

Loan exposures of banks remained adequately covered with the banking system's NPL coverage ratio at 87.2 percent as of end-November 2020, albeit slightly lower than the previous year's and previous month's ratio of 91.5 percent and 88.0 percent, respectively.

U/KBs' CAR remains well above international and regulatory standards

The capital adequacy ratio (CAR) of U/KBs at end-June 2020, on solo basis, increased to 16.3 percent from 15.3 percent as of end-March 2020. On a consolidated basis, CAR of U/KBs likewise increased to 16.7 percent from 15.8 percent during the same period. These figures remained well above the BSP's regulatory threshold of 10.0 percent and international standard of 8.0 percent.

Chart 34. Capital Adequacy Ratio of Universal and Commercial Banks
In percent



Source: BSP

The CAR of Philippine U/KBs, on consolidated basis, was higher than that of South Korea (16.0 percent) but lower than those of Malaysia (18.5 percent), Thailand (20.2 percent) and Indonesia (23.4 percent).[45]

Exchange Rate

The peso averaged ₱48.27/US$1 in Q4 2020, appreciating by 1.39 percent from the Q3 2020 average of ₱48.94/US$1.

Peso appreciates on positive sentiment over vaccine news

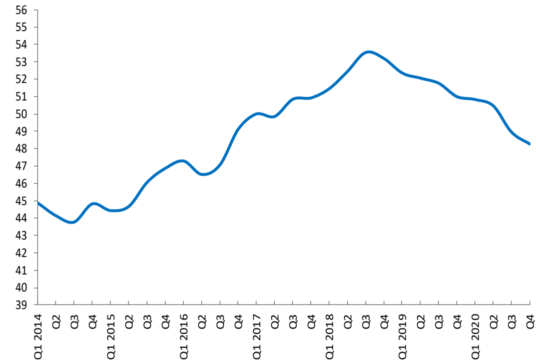
The appreciation of the peso during the review quarter partly reflected positive market sentiment over progress in the development of a vaccine against COVID-19. The country's macroeconomic fundamentals, characterized by a manageable inflation environment, strong and resilient banking system, prudent fiscal position, and a high level of international reserve buffer likewise continued to provide support to the peso. On a y-o-y basis, the peso likewise appreciated by 5.66 percent relative to the ₱51.00/US$1 average in Q4 2019.[46]

[44] Sources: Malaysia (Banking System's Ratio of net impaired loans to net total loans, November 2020); South Korea (Domestic Banks' Substandard or Below Loans [SBLs] ratio, September 2020); Indonesia (Commercial Banks' Nonperforming Loans to Gross Loans Ratio, September 2020); and Thailand (Total Commercial Banks' Gross NPL ratio, December 2019).

[45] Sources: South Korea (Domestic Banks' Total Capital Ratio, September 2020); Malaysia (Banking System's Total Capital Ratio, November 2020); Thailand (Commercial Banks' Capital Funds Percentage of Risk Assets, November 2020); and Indonesia (Commercial Banks' Regulatory Capital to Risk-Weighted Assets Ratio, September 2020).

[46] Dollar rates (per peso) or the reciprocal of the peso-dollar rates were used to compute for the percentage change.

Chart 35. Quarterly Peso-Dollar Rate
PHP/US$; average per quarter



Source: Reference Exchange Rate Bulletin, Treasury Department, BSP

In October, the peso breached the ₱48:US$1 territory as it averaged ₱48.48/US$1 during the month, 0.05 percent higher than the average in September. The peso appreciated amid positive market sentiment over (i) the progress in the 2021 national budget deliberations (which would give an assurance of economic stability amid the pandemic) ; (ii) the continued decline in daily COVID-19 cases in the country; (iii) news of the US President's support for a fresh economic stimulus fund; (iv) the country's balance of payment (BoP) position which remained at a surplus for the eighth consecutive month in September 2020; and (v) news that the clinical trials of coronavirus vaccines from drug company AstraZeneca Plc and University of Oxford yielded positive results.

The peso continued to appreciate in November. The peso averaged ₱48.25/US$1 during the month, 0.48 percent higher than the previous month's average. The peso appreciated on the back of: (i) market expectation of a slower contraction in the country's Q3 2020 GDP; (ii) the release of data which showed a narrowing of the country's trade deficit in September 2020; (iii) news of progress in the coronavirus vaccine being developed by Moderna, Inc., among others; (iv) the release of slower-than-expected inflation data in the US for the month of October 2020, providing latitude for the US Federal Reserve to remain accommodative; and (v) the BSP's decision on 19 November 2020 to cut its interest rate by 25 bps to 2.0 percent to help support economic recovery.

In December 2020, the peso appreciated to an average of ₱48.06/US$1, 0.39 percent higher than the ₱48.25/US$1 average during the previous month. The peso appreciated on market optimism over: (i) market optimism over news of progress in the development of a vaccine COVID-19;
(ii) renewed prospects of stimulus in the US;
(iii) the release of lower-than-expected local unemployment data for October 2020;
(iv) the seasonal increase in overseas Filipino remittances amid the holiday season; and
(v) the release of stronger domestic data on the BoP, Gross International Reserve (GIR) and foreign portfolio investments for October 2020, suggesting signs of economic recovery.

On a y-t-d basis, the peso appreciated against the US dollar by 5.44 percent to close at ₱48.02/US$1 on 29 December 2020 from the end-December 2019 closing rate of ₱50.64/US$1.[47]

Meanwhile, the volatility of the peso's daily closing rates (as measured by the coefficient of variation) stood at 0.07 percent in Q4 2020, lower than the 0.86 percent registered in the previous quarter.[48] The volatility of the peso in the review quarter was also lower than the volatility of most currencies in the region.

On a real trade-weighted basis, the peso lost external price competitiveness in Q4 2020 against the basket of currencies of all trading partners (TPI) and trading partners in advanced (TPI-A) countries relative to Q3 2020. This was indicated by the increase in the real effective exchange rate (REER) index of the peso by 0.03 percent and 0.86 percent, against the TPI and TPI-A baskets, respectively. Meanwhile, against the basket of currencies of trading partners in developing (TPI-D) countries, the peso gained external price competitiveness as shown by the decline in the REER index of the peso by 0.44 percent during the review quarter.

[47] Based on the last done deal transaction in the afternoon.
[48] The coefficient of variation is computed as the standard deviation of the daily closing exchange rate divided by the average exchange rates for the period.

Relative to Q4 2019, the peso meanwhile lost external price competitiveness across currency baskets during the review period. This developed following the nominal appreciation of the peso and the widening of inflation differentials vis-à-vis trading partners resulting in the increase in the REER index of the peso by 5.32 percent, 4.90 percent and 5.56 percent against the TPI, TPI-A and TPI-D baskets, respectively.[49,50]

[49] The TPI measures the nominal and real effective exchange rates of the peso across the currencies of 14 major trading partners (MTP:s) of the Philippines, which include US, Euro Area, Japan, Australia, China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand. The TPI-A measures the effective exchange rates of the peso across currencies of trading partners in advanced countries comprising of the US, Japan, Euro Area, and Australia. The TPI-D measures the effective exchange rates of the peso across 10 currencies of partner developing countries which include China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.

[50] The REER index represents the Nominal Effective Exchange Rate (NEER) index of the peso, adjusted for inflation rate differentials with the countries whose currencies comprise the NEER index basket. A decrease in the REER index indicates some gain in the external price competitiveness of the peso, while a significant increase indicates the opposite. The NEER index, meanwhile, represents the weighted average exchange rate of the peso vis-à-vis a basket of foreign currencies.

III. Fiscal Developments

The NG recorded a ₱1,068.9-billion deficit for January - November 2020, much higher than the previous year's budget gap.

Fiscal deficit widens for January to November 2020

Netting out the interest payments in NG expenditures, the primary deficit amounted to ₱713.8 billion, more than nine-fold of the amount recorded in the previous year.

Table 15. National Government Fiscal Performance
In billion pesos

	2019		2020		Growth Rate (in percent)	
	Nov	Jan-Nov	Nov	Jan-Nov	Nov	Jan-Nov
Surplus/(Deficit)	-60.9	-409.1	-128.3	-1,068.9	110.7	161.3
Revenues	304.7	2,894.2	245.8	2,617.4	-19.4	-9.6
Expenditures	365.6	3,303.3	374.1	3,686.3	2.3	11.6

* Totals may not add up due to rounding
Source: Bureau of the Treasury (BTr)

Revenues decreased by 9.6 percent to ₱2,617.4 billion in January-November 2020 compared to ₱2,894.2 billion in the same period last year. The Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) contributed ₱1,787.7 billion and ₱492.3 billion, respectively. Revenue collections by the BIR and BOC were lower by 11.2 percent and 14.8 percent, respectively. The lower collections of both agencies' was attributed to the economic restrictions brought about by the COVID-19 pandemic. Meanwhile, the BTr recorded an income of ₱211.3 billion, 56.9 percent higher than the income recorded last year on account of higher dividends.

Expenditures for the period in review amounted to ₱3,686.3 billion, 11.6 percent higher than the expenditures in January-November 2019. Excluding interest payments, expenditures went up by 12.1 percent to ₱3,331.2 billion. Meanwhile, interest payment was 7.0 percent higher compared to its year-ago level, reaching ₱355.1 billion in January-November 2020.

IV. External Developments

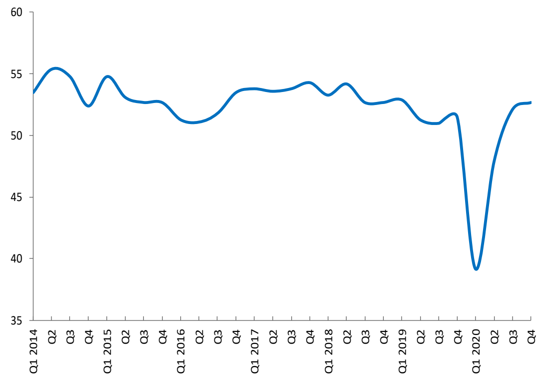
The JP Morgan Global All-Industry Output Index eased to 52.7 in December from 53.1 in November as new business intakes in both manufacturing and service sectors rose albeit at reduced rates. Five out of the six sub-sectors covered by the survey registered output expansions during the month, led by the financial services and intermediate goods sectors. In contrast, consumer services activity fell for the eleventh consecutive month.

Global economic output registers slower rate of expansion

All-industry output expanded in the US, China, Germany, India, the United Kingdom, Brazil, Australia, and Ireland. Contractions were seen in the euro area, Japan, and Russia.[51]

Chart 36. JP Morgan Global All-Industry Output Index

Index points



Source: Markit Economics

US. On a seasonally adjusted q-o-q basis, real GDP expanded by 33.4 percent in Q3 2020 following a 31.4-percent contraction in Q2 2020. On a y-o-y basis, real output decreased by 2.8 percent following a 9.0-percent decline in the previous quarter.

US manufacturing activity expands at a faster pace

[51] JP Morgan Global Composite PMI, http://www.markiteconomics.com/

The expansion in real GDP in the third quarter reflected increases in personal consumption expenditures, private inventory investment, exports, nonresidential fixed investment, and residential fixed investment. These movements were partly offset by decreases in state and local government spending as well as federal government spending.[52]

The US manufacturing PMI rose to 60.7 percent in December from 57.5 percent in November due to higher indices for production and new orders, reflecting continued expansion in demand.[53]

The unemployment rate was at 6.7 percent in December, unchanged from the record in November and reflecting the continued resumption of economic activity that had been curtailed due to the COVID-19 pandemic and efforts to contain it. Total nonfarm payroll employment declined by 140,000 during the month, as notable employment losses in leisure and hospitality and in private education which were partially offset by gains in professional and business services, retail trade, and construction. Meanwhile, on a y-o-y basis, inflation rose to 1.4 percent in December from 1.2 percent in the previous month due to higher inflation for food and new vehicles.

The Conference Board Consumer Confidence Index decreased to 88.6 in December from 92.9 in November as consumers' assessment of current business and labor market conditions became less favorable. By contrast, the preliminary Thomson-Reuters/University of Michigan Index of Consumer Sentiment rose to 80.7 in December from 76.9 in November, reflecting the large and rapid partisan shift, with Democrats becoming more positive and Republicans turning more negative.[54]

Euro Area. On a q-o-q basis, real GDP in the euro area increased by 12.5 percent in Q3 2020 after an 11.7-percent contraction in Q2 2020. On a y-o-y basis, real GDP contracted by 4.3 percent in

[52] US Bureau of Economic Analysis, "Gross Domestic Product: Third Quarter 2020 (Third Estimate)," news release, 22 December 2020. https://www.bea.gov/sites/default/files/2020-12/gdp3q20_3rd_0.pdf
[53] Institute for Supply Management, https://www.instituteforsupplymanagement.org
[54] University of Michigan Survey of Consumers, http://www.sca.isr.umich.edu/

Q3 2020 following a 14.7-percent decline in the previous quarter.[55] Meanwhile, the composite PMI for the euro area remained in contraction territory at 49.1 in December from 45.3 in November, driven by the continued decline in services activity due to weak incoming new business as social distancing measures and restrictions dampen demand.[56]

Economic activity in the euro area contracts

Preliminary figures show inflation in the euro area was unchanged at negative 0.3 percent in December from the same rate in November, driven by lower prices of energy and non-energy industrial goods.[57] Meanwhile, the seasonally adjusted unemployment rate declined to 8.3 percent in November from 8.4 percent in October.

The European Commission's Economic Sentiment Indicator (ESI) in the euro area rose to 90.4 in December from 87.7 in November, reflecting the stronger confidence in industry and construction sectors as well as among consumers.

Japan. On a q-o-q seasonally adjusted basis, real GDP expanded by 5.3 percent in Q3 2020 after an 8.3-percent contraction in Q2 2020. On a y-o-y basis, real GDP declined by 5.7 percent in Q3 2020 following a contraction of 10.3 percent in the previous quarter due mainly to weak domestic private demand.[58]

Manufacturing output in Japan stabilizes

The seasonally adjusted manufacturing PMI rose to the 50.0 no-change threshold in December from 49.0 in November, reflecting the stabilization in output levels during the month amid increased orders for manufactured goods.[59]

Inflation fell to -0.9 percent in November from -0.4 percent in October due to the decline in food; fuel, light, and water charges; transportation and communication; education; and culture and recreation. Meanwhile, the seasonally adjusted unemployment rate eased to 2.9 percent in November from 3.1 percent in October.

China. Real GDP in China expanded by 4.9 percent y-o-y in Q3 2020 from 3.2 percent in the previous quarter, reflecting the recent rebound in consumer spending amid the economy's recovery from the impact of the COVID-19 pandemic.

Chinese manufacturing activity expands at a slower pace

Meanwhile, China's seasonally adjusted manufacturing PMI declines to 53.0 in December from 54.9 in November due to a slower increase in production and overall new orders.[60]

Inflation rose to 0.2 percent in December following a 0.5-percent decline in November due to higher food inflation during the month.

India. Real GDP in India contracted by 7.5 percent in Q3 2020 following a 23.9-percent decline in the previous quarter due to sustained contraction in mining and quarrying; construction; trade, hotels, transport, communication and services related to broadcasting; financial, real estate and professional services; and public administration, defense and other services.

Economic activity in India eases

Meanwhile, the composite PMI fell to 54.9 in December from 56.3 in November as new orders expanded at weaker rates in both manufacturing and service sectors.

Inflation in India fell to 4.6 percent in December from 6.9 percent in November due mainly to lower inflation for food and beverages.

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[55] Eurostat news release 178/2020 dated 8 December 2020
[56] Markit Eurozone PMI, http://www.markiteconomics.com/
[57] Flash estimate. Eurostat news release 02/2021 dated 7 January 2021
[58] Second Preliminary Estimate. Department of National Accounts, Economic and Social Research Institute, Cabinet Office. http://www/esri.cao.go.jp/
[59] Jibun Bank Japan Manufacturing PMI, http://www.markiteconomics .com/
[60] Caixin China General Manufacturing PMI, http://www.markiteconomics.com/

ASEAN Region. The Nikkei ASEAN Manufacturing PMI rose to 50.8 in December from 50.0 in November, supported by the strongest upturn in new orders since August 2018.

Output indicators in the ASEAN region improves

Across the seven monitored countries, Singapore, Indonesia, Thailand, and Vietnam, exhibited improvements in manufacturing operations. Meanwhile, the Philippines, Malaysia, and Myanmar registered contractions in their respective manufacturing conditions.[61]

Policy Actions by Other Central Banks.
On 3 November 2020, the Reserve Bank of Australia (RBA) cut the cash rate by 15 bps to 0.10 percent to stimulate job creation and further support the recovery of the economy from the COVID-19 pandemic.

Policy stance of other central banks remain accommodative

On 19 November 2020, Bank Indonesia (BI) decided to cut its seven-day reverse repurchase rate by 25 bps to 3.75 percent to support the recovery of the Indonesian economy through injection of additional liquidity. BI estimates that it had pumped approximately US$48.12 billion into the banking system this year.

[61] Nikkei ASEAN Manufacturing PMI, http://www.markiteconomics.com/

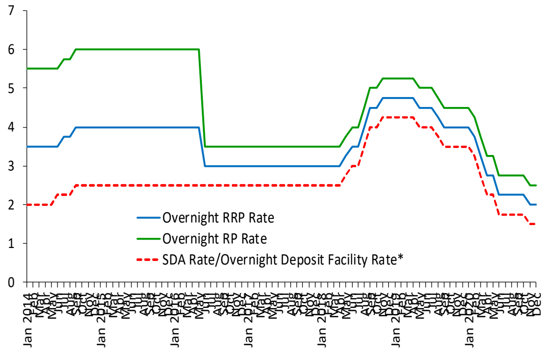
V. Monetary Policy Developments

At its policy meeting on 19 November 2020, the BSP decided to cut the interest rate on the overnight RRP facility by 25 bps to 2.0 percent. The interest rates on the overnight deposit and lending facilities were likewise reduced to 1.5 percent and 2.5 percent, respectively.

BSP reduces the key policy rate in November 2020

The decision to lower the key policy rate was based on baseline forecasts which indicated a benign inflation environment over the policy horizon, with inflation expectations remaining firmly anchored within the target range. Average inflation is seen to settle within the lower half of the target band for 2020 up to 2022, reflecting slower domestic economic activity, lower global crude oil prices, and the recent appreciation of the peso. The BSP noted that the balance of risks to the inflation outlook also remains tilted toward the downside owing largely to potential disruptions to domestic and global economic activity amid the ongoing pandemic.

Chart 37. BSP Policy Rates
In percent



* On 3 June 2016, Special Deposit Accounts (SDAs) were replaced by the Overnight Deposit Facility (ODF) in line with the implementation of the Interest Rate Corridor (IRC) System.
Source: BSP

The BSP observed that uncertainty remains elevated amid the resurgence of COVID-19 cases globally as global economic prospects moderated. Equally important, the BSP noted that while domestic output contracted at a slower pace in Q3 2020, muted business and household sentiment and the impact of recent natural calamities could pose strong headwinds to the recovery of the economy in the coming months.

Given these considerations, the BSP assessed that there remains a critical need for continuing policy support measures to bolster economic activity and boost market confidence. With a benign inflation environment and stable inflation expectations, the BSP sees enough policy space for a reduction in the policy rate to uplift market sentiment and nurture the country's economic recovery amid increased downside risks to growth.

The BSP maintained monetary policy settings in its policy meeting on 17 December 2020 amid benign inflation outlook. The latest baseline forecasts have risen slightly due to the sharp increase in global crude oil prices and higher-than-expected food inflation in November. However, since the rise in food prices is transitory, it is expected that the future inflation path will remain firmly within the government's 2-4 percent target over the policy horizon. The balance of risks to the inflation outlook also leans toward the downside from 2020 to 2022 owing largely to potential disruptions to domestic and global economic activity amid the ongoing pandemic. Meanwhile, inflation expectations remain broadly consistent with the inflation target.

The BSP noted that the resurgence of COVID-19 cases globally has tempered economic activity with the reimposition of preventive measures in recent weeks. However, optimism over the delivery of vaccines has lifted market confidence, supporting improved prospects for global growth. On the domestic front, the BSP also observed early indications of improved mobility and sentiment. While recent natural calamities could pose strong headwinds to growth, the further easing of quarantine measures should help facilitate the recovery of the economy in the coming months.

Given these considerations, the BSP is of the view that monetary policy settings remain appropriate. The BSP believes that an accommodative monetary policy stance, together with sustained fiscal initiatives to ensure public welfare, should quicken the economy's transition toward a sustainable recovery. Moreover, the BSP emphasized that, looking ahead, the BSP remains committed to deploying its full range of instruments as needed in fulfillment of its mandate to maintain price and financial stability conducive to growth.

VI. Inflation Outlook

BSP Inflation Forecasts

The latest baseline forecasts continue to suggest a benign inflation environment over the policy horizon. Inflation is expected to average at 3.2 percent for 2021, and 2.9 percent for 2022.

The forecast revision for 2021 was due largely to the higher-than-expected inflation outturn in Q4 2020 and the sharp uptick in global crude oil prices. Meanwhile, the forecast for 2022 was broadly unchanged compared to the previous round.

The latest forecasts continue to suggest that future inflation path will remain firmly within the Government's 2-4 percent target throughout the policy horizon. The recent uptrend in inflation, reflecting the impact of weather disturbances, is seen to be largely transitory. Inflation is also projected to accelerate close to the high-end of the target range in Q2 and Q3 2021 due to the projected recovery in domestic demand as well as positive base effects. Nevertheless, the inflation path is seen to decelerate below the midpoint of the target range by Q4 2021 and Q1 2022 due to negative base effects before settling close to the midpoint by H2 2022.

The risks to the inflation outlook remain tilted to the downside. The potential impact on global and domestic economic growth prospects of a more disruptive COVID-19 pandemic is the primary downside risk to inflation. Nonetheless, upside risks could emanate from the possibility of an early roll out of COVID-19 vaccines in the Philippines, which is expected to ease the existing containment measures and expand further operating capacity of the economy.

Inflation seen to remain within the Government target over the policy horizon

Demand Conditions. Domestic growth in Q3 2020 posted a smaller contraction of 11.5 percent from a 16.9-percent decline in Q2 2020 and 6.3-percent expansion in Q3 2019. On the production side, growth in industry and services sectors continued to contract at a slower pace as lockdown measure eased during the quarter, while output of the agriculture sector increased. On the expenditure side, household consumption and external trade showed signs of recovery, with said sectors posting smaller contractions in Q3 2020.
The nowcast for Q4 2020 growth indicates that the economy could continue to contract at a slower pace. The decline in GDP for the quarter could be driven primarily by the further deterioration in the industry and services sectors, which remain heavily affected by the pandemic despite some easing in quarantine measures.
In particular, the projected weakness in manufacturing and construction activities is expected to drive the decline in the industry sector, although at a slower pace compared to Q3 2020. Similarly, the services sector could continue to contract driven primarily by the slowdown in transport, tourism, and other service activities. Agriculture output is also projected to contract in the quarter due to impact of weather disturbances on production.

There is no steady pattern for high-frequency real sector indicators, thus still pointing to weak growth prospects. Manufacturing's volume of production index further decreased in November 2020, faster than the decline observed the month before. Similarly the composite Purchasing Managers' Index (PMI) in November 2020 remained below the 50-point mark as of 2020, lower than the PMI in October 2020, as the services and retail and wholesale sectors contracted faster compared to last month.
Meanwhile, results of the BSP expectations surveys have indicated that business and consumer confidence improved in Q4 2020. Business confidence turned optimistic, while consumer confidence is less pessimistic in Q4 2020 mainly due to reopening of businesses and easing of quarantine measures.

Despite the deceleration in local COVID-19 cases, consumer and business sentiment could remain subdued and continue to be affected until a vaccine becomes available for mass use. Nonetheless, improvements in mobility indicators could indicate that firms and households are beginning to adjust to the post-pandemic operating environment, which could support resurgence in economic activity in the near term.

Growth is expected to recover in 2021 and 2022

GDP growth is projected to recover in 2021 and 2022 driven by higher government spending and the passage of structural reform programs, such as the Corporate Recovery and Tax Incentives for Enterprises (CREATE) bill and the Financial Institutions Strategic Transfer (FIST) bill. Improvements in global growth prospects along with the further easing of domestic quarantine measures will likewise support the country's growth trajectory. Moreover, the implementation of well-targeted amelioration and recovery programs as well as the restart of the infrastructure spending program will help the country regain confidence, restore employment rates to pre-crisis levels, and attain higher economic growth. The country's recovery from the COVID-19 pandemic is expected to be fast-tracked by additional jobs that could be generated from higher infrastructure investments.

Meanwhile, the latest baseline forecasts is consistent with the assumption of vaccine mass use by H1 2022. An earlier mass deployment of the COVID-19 vaccine will likely result in higher output growth in 2021. The availability of a vaccine for COVID-19 and its subsequent roll out is expected to ease the strict containment measures in place throughout the country, which will likely increase the operating capacity of the economy and accelerate the recovery process.

Supply Conditions. Food inflation picked up in November and December 2020 as weather-related disturbances adversely affected domestic supply condition. Moreover, the impact of *La Niña* weather conditions on global food production as well as the recent uptick in global crude oil prices due to positive market sentiment could be a source of supply-side price pressures for 2021.

Global crude oil prices rose significantly in Q4 2020 due to higher global demand following favorable sentiment on the continued deployment of COVID-19 vaccine. Consequently, the global crude oil price assumptions increased compared to the previous forecast round.

Economic activity is projected to operate below its full capacity over the policy horizon

The balance of demand and supply conditions as captured by the output gap (or the difference between actual and potential output), provides an indication of potential inflationary pressures in the near term.[62]

Based on the Q3 2020 GDP outturn, estimates by the BSP show that the output gap is projected to remain negative over the policy horizon. This reflects the potential adverse impact of the pandemic on economic activity and the country's production capacity. This implies that the economy will likely operate below its full capacity over the policy horizon as firms and households gradually adjust to the post-pandemic economic conditions. However, the projected contraction in economic activity could be temporary in nature, as public health measures to control the spread of the pandemic alongside macroeconomic policy gain full traction in reviving the economy.

Key assumptions used to generate the BSP's inflation forecasts. The BSP's baseline inflation forecasts are based on the following assumptions:

1) BSP's overnight RRP rate at 2.0 percent from January 2021 to December 2022;

2) NG fiscal deficits for 2020 to 2022, which are consistent with the DBCC-approved estimates;

3) Dubai crude oil price assumptions consistent with the trend of futures prices of oil in the international market;

4) Increase in nominal wages consistent with historical wage increases and labor productivity growth;

5) Real GDP growth is endogenously determined; and

Foreign exchange rate is endogenously determined through the purchasing power parity and interest rate parity relationships.

[62] Inflation tends to rise (fall) when demand for goods and services exert pressure on the economy's ability to produce goods and services, i.e., when the output gap is positive (negative).

Risks to the Inflation Outlook

The risks to the inflation outlook may be presented graphically through a fan chart. The fan chart depicts the probability of different inflation outcomes based on the central projection (corresponding to the baseline forecast of the BSP) and the risks surrounding the inflation outlook. Compared to the previous inflation report, the latest fan chart presents an upward shift in the inflation projection for 2021 due largely to higher-than-expected inflation outturns for Q4 2020 and the sharp uptick in global crude oil prices.

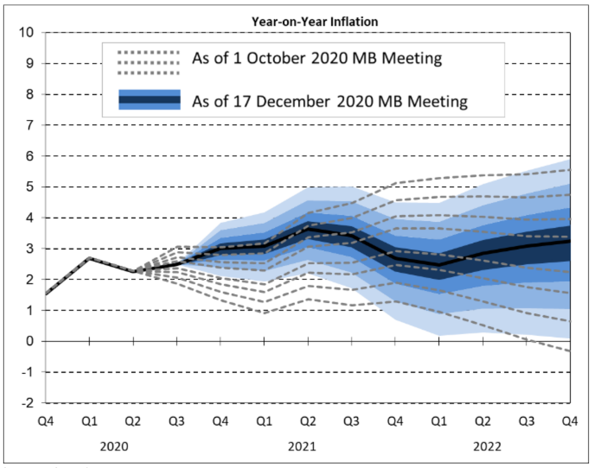
The BSP's review of current inflation dynamics suggests that the risks to the inflation outlook are tilted to the downside for 2021 to 2022.

A more disruptive impact of COVID-19 could lead to a deeper slowdown in global and domestic economic activity. The re-imposition of containment measures among major economies as a result of second wave cases and the failure to contain the pandemic despite the initial availability of a vaccine is expected to further dampen consumer confidence and exacerbate the disruptions in supply chains and trade. In the domestic front, the reimposition of stricter quarantine measures could derail economic recovery and further heighten the uncertainty faced by firms and consumers.

Nonetheless, upside risks could emanate from the possibility of an early roll out of COVID-19 vaccines in the Philippines, which is expected to ease the existing containment measures and expand further operating capacity of the economy. Meanwhile, the recent uptick in global crude oil prices due to positive market sentiment along with the impact of La Niña weather conditions on global food production could be a source of supply-side price pressures for 2021.

The balance of risks to the inflation outlook leans to the downside for 2021 to 2022

Chart 38. Inflation Projection



Source: BSP estimates

The fan chart shows the probability of various outcomes for inflation over the forecast horizon. The darkest band depicts the central projection, which corresponds to the BSP's baseline inflation forecast. It covers 25 percent of the probability distribution. Each successive pair of bands is drawn to cover a further 25 percent of probability, until 75 percent of the probability distribution is covered. Lastly, the lightest band covers the lower and upper 90 percent of the probability distribution. The bands widen (i.e., "fan out") as the time frame is extended, indicating increasing uncertainty about outcomes. The band in wire mesh depicts the inflation profile in the previous report.

The shaded area measures the range of uncertainty which is based on the deviation of forecasts from actual outcomes in the past years. The relative magnitude of the probability areas lying above and below the central projection captures the level of skewness based on the downside and upside shocks that affect the inflationary process over the next two years.

Implications for the Monetary Policy Stance

The Monetary Board (MB) cut the policy rate by 25 basis points at its meeting on 19 November 2020, citing the need to bolster economic activity and boost market confidence amid the resurgence of COVID-19 cases globally. Meanwhile, at its meeting on 17 December 2020, the MB held the policy rate steady to allow the BSP's monetary responses throughout the year to continue to work their way through the usual channels of transmission.

The BSP recognized that inflation is projected to remain relatively benign in 2021 and 2022, as inflation expectations continue to be well-anchored within the target range of 3.0 percent ± 1 percentage point. The balance of risks to the inflation outlook also remains tilted to the downside over the policy horizon owing largely to potential disruptions to domestic and global economic activity amid the ongoing pandemic.

At the same time, while the resurgence of COVID-19 cases globally has prompted the reimposition of preventive measures during the latter part of the quarter, optimism over the delivery of vaccines has lifted market confidence, supporting improved prospects for global growth. On the domestic front, the BSP has observed encouraging signs of recovery amid indications of improved mobility and sentiment.

Given these considerations, the BSP is of the view that prevailing monetary policy settings remain sufficiently accommodative to help quicken the economy's transition toward a sustainable recovery. Continuing monetary policy support, together with sustained fiscal initiatives to ensure public welfare, should help mitigate strong headwinds to growth.

However, possible upside surprises to inflation may be linked to supply-side risks such as weather disturbances and rising global crude oil prices. Looking ahead, the BSP will continue to monitor these developments and their impact on domestic inflation, especially as prospects for demand improve amid the rollout of vaccination programs in many countries. The BSP remains committed to deploying its full range of monetary instruments and regulatory relief measures as needed in fulfillment of its mandate to promote non-inflationary and sustainable growth.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
2008			
31 Jan 2008	5.00	7.00	The Monetary Board (MB) decided to reduce by 25 bps the BSP's key policy interest rates to 5 percent for the overnight borrowing or reverse repurchase (RRP) facility and 7 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts (SDAs) were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest inflation forecasts indicated that inflation would fall within the 4.0 percent ± 1 ppt target range in 2008 and the 3.5 ± 1 ppt target range in 2009.
13 Mar 2008 **24 Apr 2008**	5.00	7.00	The MB decided to keep the BSP's key policy interest rates at 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The MB also decided to implement immediately the following refinements in the SDA facility: (1) the closure of existing windows for the two-, three-, and six-month tenors; and (2) the reduction of the interest rates on the remaining tenors. The interest rates on term RRPs and RPs were also left unchanged.
5 Jun 2008	5.25	7.25	The MB decided to increase by 25 bps the BSP's key policy interest rates to 5.25 percent for the RRP facility and 7.25 percent for RP facility as emerging baseline forecasts indicate a likely breach of the inflation target for 2008 along with indications that supply-driven pressures are beginning to feed into demand. Given the early evidence of second-round effects, the MB recognized the need to act promptly to rein in inflationary expectations. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
17 Jul 2008	5.75	7.75	The MB increased by 50 bps the BSP's key policy interest rates to 5.75 percent for the overnight borrowing or RRP facility and 7.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
28 Aug 2008	6.00	8.00	The MB increased by 25 bps the BSP's key policy interest rates to 6.0 percent for the overnight borrowing or RRP facility and 8.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
6 Oct 2008 **6 Nov 2008**	6.00	8.00	The MB kept the BSP's key policy interest rates unchanged at 6.0 percent for RRP facility and 8.0 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
18 Dec 2008	5.50	7.50	The MB decided to reduce the BSP's key policy interest rates by 50 bps to 5.5 percent for the overnight borrowing or RRP facility and 7.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. This outlook is supported by the downward shift in the balance of risks, following the easing of commodity prices, the moderation in inflation expectations, and the expected slowdown in economic activity.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	RP Overnight	Monetary Policy Decisions
2009			
29 Jan 2009	5.00	7.00	The MB decided to reduce the BSP's key policy interest rates by another 50 bps to 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. The MB based its decision on the latest inflation outlook which shows inflation falling within the target range for 2009 and 2010. The Board noted that the balance of risks to inflation is tilted to the downside due to the softening prices of commodities, the slowdown in core inflation, significantly lower inflation expectations, and moderating demand.
5 Mar 2009	4.75	6.75	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.75 percent for the overnight borrowing or RRP facility and 6.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Given possible upside risks to inflation, notably the volatility in oil prices and in exchange rates, increases in utility rates, and potential price pressures coming from some agricultural commodities, the MB decided that a more measured adjustment of policy rates was needed.
16 Apr 2009	4.50	6.50	The MB reduced key policy rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility, effective immediately. This rate cut brings the cumulative reduction in the BSP's key policy rates to 150 bps since December last year. The current RRP rate is the lowest since 15 May 1992. Meanwhile, the interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest baseline inflation forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the MB considered that the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.
28 May 2009	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Baseline forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the Monetary Board considered that, on balance, the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.
9 Jul 2009	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility, effective immediately. The interest rates on term RRPs, RPs, and SDAs were reduced accordingly. This is the sixth time since December 2008 that the BSP has cut its policy interest rates.
20 Aug 2009 1 Oct 2009 5 Nov 2009 17 Dec 2009	4.00	6.00	The MB kept key policy rates unchanged at 4 percent for the RRP facility and 6 percent for the overnight lending RP facility. The decision to maintain the monetary policy stance comes after a series of policy rate cuts since December 2008 totaling 200 bps and other liquidity enhancing measures.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
2010			
28 Jan 2010 **11 Mar 2010** **22 Apr 2010** **3 Jun 2010** **15 Jul 2010** **26 Aug 2010** **7 Oct 2010** **18 Nov 2010** **29 Dec 2010**	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4 percent for the RRP facility and 6 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
2011			
10 Feb 2011	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
24 Mar 2011	4.25	6.25	The MB decided to increase by 25 bps the BSP's key policy interest rates to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. The MB's decision was based on signs of stronger and broadening inflation pressures as well as a further upward shift in the balance of inflation risks. International food and oil prices have continued to escalate due to the combination of sustained strong global demand and supply disruptions and constraints.
5 May 2011	4.50	6.50	The MB decided to increase the BSP's key policy interest rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. Baseline inflation forecasts continue to suggest that the 3-5 percent inflation target for 2011 remains at risk, mainly as a result of expected pressures from oil prices.
16 Jun 2011	4.50	6.50	The MB decided to keep policy rates steady at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board decided to raise the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on Friday, 24 June 2011. The MB's decision to raise the reserve requirement is a preemptive move to counter any additional inflationary pressures from excess liquidity.
28 Jul 2011	4.50	6.50	The MB maintained the BSP's key policy interest rates at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board increased anew the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on 5 August 2011. The MB's decision to raise the reserve requirement anew is a forward-looking move to better manage liquidity.
8 Sep 2011 **20 Oct 2011** **1 Dec 2011**	4.50	6.50	The MB decided to keep the overnight policy rates (OPR) steady. At the same time, the reserve requirement ratios (RRR) were kept unchanged.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2012			
19 Jan 2012	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB's decision is based on its assessment that the inflation outlook remains comfortably within the target range, with expectations well-anchored and as such, allowed some scope for a reduction in policy rates to help boost economic activity and support market confidence.
1 Mar 2012	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB is of the view that the benign inflation outlook has allowed further scope for a measured reduction in policy rates to support economic activity and reinforce confidence.
19 Apr 2012	4.00	6.00	The MB decided to keep the BSP’s key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
14 Jun 2012	4.00	6.00	The MB decided to keep the BSP’s key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB’s decision was based on its assessment that the inflation environment remains manageable. Baseline forecasts continue to track the lower half of the 3-5 percent target range for 2012 and 2013, while inflation expectations remain firmly anchored. At the same time, domestic macroeconomic readings have improved significantly in Q1 2012.
26 Jul 2012	3.75	5.75	The MB decided to reduce the BSP’s key policy interest rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the third time in 2012 that the BSP has cut its policy rates. The MB’s decision was based on its assessment that price pressures have been receding, with risks to the inflation outlook slightly skewed to the downside. Baseline forecasts indicate that inflation is likely to settle within the lower half of the 3-5 percent target for 2012 and 2013, as pressures on global commodity prices are seen to continue to abate amid weaker global growth prospects. At the same time, the MB is of the view that prospects for global economic activity are likely to remain weak.
13 Sep 2012	3.75	5.75	The MB decided to keep the BSP’s key policy interest rates steady at 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB’s decision was based on its assessment that the inflation environment remains benign, with the risks to the inflation outlook appearing to be broadly balanced.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
25 Oct 2012	3.50	5.50	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the fourth time in 2012 that the BSP has cut its policy rates. The MB's decision was based on its assessment that the inflation environment continued to be benign with latest baseline forecasts indicating that the future inflation path will remain within target for 2012-2014. A rate cut would also be consistent with a symmetric response to the risk of below-target inflation.
13 Dec 2012	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that current monetary settings remained appropriate, as the cumulative 100-bp reduction in policy rates in 2012 continued to work its way through the economy.
2013			
24 Jan 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained accordingly. The reserve requirement ratios were kept steady as well. At the same time, the MB decided to set the interest rates on the SDA facility at 3.00 percent regardless of tenor, effective immediately, consistent with the BSP's continuing efforts to fine-tune the operation of its monetary policy tools.
14 Mar 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Following its previous decision to rationalize the SDA facility in January 2013, the MB further reduced the interest rates on the SDA facility by 50 bps to 2.50 percent across all tenors effective immediately.
25 Apr 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Meanwhile, the SDA rate was further reduced by 50 bps to 2.0 percent across all tenors.
13 Jun 2013 25 Jul 2013 12 Sep 2013 24 Oct 2013 12 Dec 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
2014			
6 Feb 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.
27 Mar 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirement by one percentage point effective on 11 April 2014.
8 May 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirements for U/KBs and TBs by a further one percentage point effective on 30 May 2014.
19 Jun 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained. The reserve requirement ratios were left unchanged as well. Meanwhile, the MB decided to raise the interest rate on the SDA facility by 25 bps from 2.0 percent to 2.25 percent across all tenors effective immediately.
31 Jul 2014	3.75	5.75	The MB decided to increase the BSP's key policy rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also raised accordingly. The rate on special deposit accounts (SDA) was left unchanged. Meanwhile, the reserve requirement ratios were also kept steady.
11 Sep 2014	4.00	6.00	The MB decided to increase the BSP's key policy rates by 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also raised accordingly. Meanwhile, the reserve requirement ratios were left unchanged.
23 Oct 2014 **11 Dec 2014**	4.00	6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.
2015			
12 Feb 2015 **26 Mar 2015** **14 May 2015** **25 Jun 2015** **13 Aug 2015** **24 Sep 2015** **12 Nov 2015** **17 Dec 2015**	4.00	6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
2016				
11 Feb 2016 **23 Mar 2016** **12 May 2016**	4.00		6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.
23 Jun 2016 **11 Aug 2016** **22 Sep 2016** **10 Nov 2016** **22 Dec 2016**	3.00	2.50	3.50	The BSP formally adopted an interest rate corridor (IRC) system as a framework for conducting its monetary operations. The shift to IRC is an operational adjustment and not a change in the monetary policy stance. The IRC is a system for guiding short-term market rates towards the BSP policy interest rate which is the overnight reverse repurchase (RRP) rate. The IRC system consists of the following instruments: standing liquidity facilities, namely, the overnight lending facility (OLF) and the overnight deposit facility (ODF); the overnight RRP facility; and a term deposit auction facility (TDF). The interest rates for the standing liquidity facilities form the upper and lower bound of the corridor while the overnight RRP rate is set at the middle of the corridor. The repurchase (RP) and Special Deposit Account (SDA) windows will be replaced by standing overnight lending and overnight deposit facilities, respectively. Meanwhile, the reverse repurchase (RRP) facility will be modified to a purely overnight RRP. In addition, the term deposit facility (TDF) will serve as the main tool for absorbing liquidity. The interest rates for these facilities will be set as follows starting 3 June 2016: • 3.5 percent in the overnight lending facility (a reduction of the interest rate for the upper bound of the corridor from the current overnight RP rate of 6.0 percent); • 3.0 percent in the overnight RRP rate (an adjustment from the current 4.0 percent); and • 2.5 percent in the overnight deposit facility (no change from the current SDA rate).
2017				
9 Feb 2017 **23 Mar 2017** **11 May 2017** **22 Jun 2017** **10 Aug 2017** **21 Sep 2017** **9 Nov 2017** **14 Dec 2017**	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight (RRP) facility, 3.5 percent for the overnight lending facility (OLF) and 2.5 percent for the overnight deposit facility (ODF). The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
2018				
8 Feb 2018	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
15 Feb 2018				The reserve requirement ratio was reduced by one (1) percentage point as an operational adjustment to support the BSP's shift toward a more market-based implementation of monetary policy as well as its broad financial market reform agenda. The reduction will apply to the reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions with reserve requirement at twenty (20) percent.
22 Mar 2018	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
10 May 2018	3.25	2.75	3.75	The MB decided to increase the BSP's key policy interest rates by 25 basis points to 3.25 percent for the overnight RRP facility, 3.75 percent for the OLF and 2.75 percent for the ODF.
24 May 2018				The reserve requirement ratio was reduced by one (1) percentage point as part of its medium-term financial market reform agenda to promote a more efficient financial system by lowering intermediation costs. The reduction will apply to those reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions that are currently subject to a reserve requirement of nineteen (19) percent.
20 Jun 2018	3.50	3.00	4.00	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 3.50 percent for the overnight RRP facility, 4.00 percent for the OLF and 3.00 percent for the ODF.
9 Aug 2018	4.00	3.50	4.50	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2018	4.50	4.00	5.00	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
15 Nov 2018	4.75	4.25	5.25	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
13 Dec 2018	4.75	4.25	5.25	The MB decided to maintain the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2019				
7 Feb 2019 **21 Mar 2019**	4.75	4.25	5.25	The MB decided to keep the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
9 May 2019	4.50	4.00	5.00	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
16 May 2019	4.50	4.00	5.00	The MB decided to reduce the reserve requirements by 200 basis points (or 2 percentage points) which shall be implemented according to the following schedule: 100 basis points on 31 May 2019; 50 basis points on 28 Jun 2019; and 50 basis points on 26 Jul 2019. The reduction will apply to those reservable liabilities of universal and commercial banks (U/KBs) that are currently subject to a reserve requirement of eighteen (18) percent.
23 May 2019				The MB complemented the reduction in reserve requirements for universal and commercial banks (U/KBs) with a phased 200-basis-point reduction in the reserve requirements for thrift banks (TBs) and non-bank financial institutions with quasi-banking functions (NBQBs), as well as a 100-basis-point reduction for demand deposits and NOW accounts of rural and cooperative banks on 31 May 2019. Moreover, long-term negotiable certificates of time deposits issued by all banks and NBQBs will have reduced and uniform reserve requirement ratio of 4.0 percent. The reductions on reserve requirements will take effect for U/KBs, TBs, and NBQBs on the reserve weeks beginning 31 May 2019, 28 Jun 2019, and 26 Jul 2019. The lower ratios shall apply to all reservable liabilities except bonds and mortgage/chattel mortgage certificates as the BSP continues to assess the impact of a reduction in the reserve requirements on said instruments.
20 Jun 2019	4.50	4.00	5.00	The MB decided to maintain the BSP's key policy interest rates at 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
8 Aug 2019	4.25	3.75	4.75	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.25 percent for the overnight RRP facility, 4.75 percent for the OLF and 3.75 percent for the ODF.
26 Sep 2019	4.00	3.50	4.50	The MB decided to cut the BSP's key policy interest rates by 25 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2019				The MB decided to reduce the reserve requirements for U/KBs, TBs, and RBs by 100 bps (or one percentage point). The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks. The reserve requirement of U/KBs was reduced from 16 percent to 15 percent, TBs from 6 percent to 5 percent, and RBs from 4 percent to 3 percent. The reduction will be effective on the first day of the first reserve week of November 2019.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent): Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
		2019		
24 Oct 2019				The MB decided to reduce the reserve requirements for U/KBs and TBs by 100 bps (or one percentage point). The MB complemented the move with a reduction in the RRs for NBQBs. The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks and NBQBs. The reserve requirement of U/KBs was reduced from 15 percent to 14 percent, TBs from 5 percent to 4 percent, and NBQBs from 16 percent to 14 percent. The reduction will be effective on the first day of the first reserve week of December 2019.
14 Nov 2019	4.00	3.50	4.50	The MB decided to maintain the BSP's key policy interest rate at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
12 Dec 2019	4.00	3.50	4.50	The MB decided to maintain the BSP's key policy interest rates at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
		2020		
6 Feb 2020	3.75	3.25	4.25	The MB decided to cut the key policy interest rate by 25 bps to 3.75 percent. The interest rates on the OLF and ODF were reduced to 4.25 percent and 3.25 percent, respectively.
19 Mar 2020	3.25	2.75	3.75	The MB decided to cut the key policy interest rate by 50 bps to 3.25 percent, effective 20 March 2020. The interest rates on the OLF and ODF were reduced to 3.75 percent and 2.75 percent, respectively.
24 Mar 2020				The MB announced a 200-bp reduction in the RR ratio of reservable liabilities of universal and commercial banks (U/KBs) effective 3 April 2020. This puts RRR of U/KBs to 12 percent. The RR cut is intended to calm the markets and to encourage banks to continue lending to both retail and corporate sectors. This will ensure sufficient domestic liquidity in support of economic activity amidst the global pandemic due to the COVID-19.
16 Apr 2020	2.75	2.25	3.25	The MB decided to cut the interest rate on the BSP's overnight reverse repurchase (RRP) facility by 50 basis points (bps) to 2.75 percent, effective Friday, 17 April 2020. The interest rates on the OLF and ODF were reduced to 3.25 percent and 2.25 percent, respectively. The off-cycle rate cut is meant to strongly encourage lending to various sectors, especially the most vulnerable, amid the COVID-19 pandemic.
25 Jun 2020	2.25	1.75	2.75	The MB decided to cut the interest rate on the BSP's overnight reverse repurchase (RRP) facility by 50 basis points (bps) to 2.25 percent, effective Friday, 26 June 2020. The interest rates on the OLF and ODF were reduced to 2.75 percent and 1.75 percent, respectively. Amidst a benign inflation outlook, the MB sees a critical need for continuing measures to bolster economic activity and support financial conditions.
20 Aug 2020 1 Oct 2020	2.25	1.75	2.75	The MB decided to maintain the BSP's key policy interest rates at 2.25 percent for the overnight RRP facility, 2.75 percent for the OLF and1.75 percent for the ODF.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
2020				
19 Nov 2020	2.00	1.50	2.50	The MB decided to cut the key policy interest rate by 25 bps to 2.00 percent, effective 20 November 2020. The interest rates on the OLF and ODF were reduced to 2.50 percent and 1.50 percent, respectively.
17 Dec 2020	2.00	1.50	2.50	The MB decided to maintain the BSP's key policy interest rates at 2.00 percent for the overnight RRP facility, 2.50 percent for the OLF and1.50 percent for the ODF.

The *BSP Inflation Report* is published every quarter by the Bangko Sentral ng Pilipinas. The report is available as a complete document in pdf format, together with other general information about inflation targeting and the monetary policy of the BSP, on the BSP's website:

https://www.bsp.gov.ph/SitePages/PriceStability/PriceStability.aspx

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