# MONETARY POLICY REPORT

FEBRUARY 2024

# 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 sought to help fulfill this objective.

One of the key features of inflation targeting is greater transparency, which means greater disclosure and communication by the Bangko Sentral ng Pilipinas (BSP) of its policy actions and decisions. The *Monetary Policy Report* or MPR plays a primary part in the BSP's transparency mechanisms under inflation targeting. It shares with stakeholders, including market counterparties, the latest assessment of the stance of monetary policy based on an analysis of economic and financial prospects. The broad aim is to contribute to making monetary policy accessible to the public, who through the report may better understand and monitor the BSP's commitment to the inflation target, promote the anchoring of inflation expectations, and encourage informed debate on monetary policy issues.

The MPR, which replaced the quarterly *Inflation Report*, is the flagship BSP publication on monetary policy that provides the public a detailed view of the BSP's forecasts and guidance on the likely direction of monetary policy over the next two years. The report conveys to the public the overall thinking behind the BSP's decisions on monetary policy. The greater part of the report is devoted to forward-looking discussions on inflation and the key macroeconomic variables that affect inflation as well as the risks and uncertainty surrounding the BSP's inflation forecasts.

Under the inflation targeting framework, the government's annual headline inflation target has been retained at 3.0 percent ± 1.0 percentage point (ppt) for 2024–2028 by the Development Budget Coordination Committee. The inflation target range continues to be an appropriate quantitative representation of the medium-term goal of price stability that is aligned with the Philippines' current structure of economy and outlook of macroeconomic conditions over the next few years.

The Monetary Board approved this *Monetary Policy Report* at its meeting on 14 February 2024.

**ELI M. REMOLONA, JR.**
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 and employment 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 the overnight reverse repurchase (RRP) facility.[1] 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) and BSP Securities Facility; (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 is the average annual 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 2024-2028 is 3.0 percent ± 1.0 ppt.[3]

## BSP's Explanation Clauses

Explanation clauses are a prespecified 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] On 8 September 2023, the overnight RRP facility was transformed into a variable-rate auction format with the policy rate of the BSP renamed to target RRP rate.
[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] During the DBCC meeting on 15 December 2023, the DBCC, in consultation with the BSP, decided to retain the inflation target of 3.0 percent ± 1.0 ppt for 2024 and set the same inflation target for 2025–2028.

## The Monetary Board

The powers and functions of the BSP, such as the conduct of monetary policy and supervision over the banking system, are exercised by its Monetary Board (MB), which has seven members appointed by the President of the Philippines. For 2024, the MB is scheduled to hold seven monetary policy meetings to review and decide on monetary policy.

***Chairman and Governor***
Eli M. Remolona, Jr.

***Members***
Ralph G. Recto
Benjamin E. Diokno
V. Bruce J. Tolentino
Anita Linda R. Aquino
Romeo L. Bernardo
Rosalia V. De Leon

## 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 MB. Like the MB, the Committee will meet seven times in 2024 but can have additional regular meetings when necessary.

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**Eli M. Remolona, Jr.**
*Governor*

***Members***

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*Deputy Governor*
*Monetary and Economics Sector*

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*Financial Markets Research Group*
*Real and External Sectors Research Group*

| 2024 schedule of MB monetary policy meetings and publication of the *MB Highlights* and the *Monetary Policy Report* | | | |
|---|---|---|---|
| **2024** | **Monetary Board (MB) meeting** | **Publication of *MB highlights*** | **Publication of the *Monetary Policy Report* (MPR)** |
| **January** | | 11 (Thursday)<br>(14 December 2023 MB meeting) | |
| **February** | 15 (Thursday)<br>(MB Meeting no. 1) | | 16 (Friday)<br>(MPR I, February 2024) |
| **March** | | 14 (Thursday)<br>(15 February 2024 MB meeting) | |
| **April** | 4 (Thursday)<br>(MB Meeting no. 2) | | |
| **May** | 16 (Thursday)<br>(MB Meeting no. 3) | 2 (Thursday)<br>(4 April 2024 MB meeting) | 17 (Friday)<br>(MPR II, May 2024) |
| **June** | 27 (Thursday)<br>(MB Meeting no. 4) | 13 (Thursday)<br>(16 May 2024 MB meeting) | |
| **July** | | 25 (Thursday)<br>(27 June 2024 MB meeting) | |
| **August** | 15 (Thursday)<br>(MB Meeting no. 5) | | 16 (Friday)<br>(MPR III, August 2024) |
| **September** | | 12 (Thursday)<br>(15 August 2024 MB meeting) | |
| **October** | 17 (Thursday)<br>(MB Meeting no. 6) | | |
| **November** | | 14 (Thursday)<br>(17 October 2023 MB meeting) | |
| **December** | 19 (Thursday)<br>(MB Meeting no. 7) | | 20 (Friday)<br>(MPR IV, December 2024) |

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# Monetary Policy Summary

**At its monetary policy meeting on 14 February 2024, the BSP decided to keep the target overnight reverse repurchase (RRP) rate unchanged at 6.50 percent.** Thus, the interest rates on the overnight deposit and lending facilities were likewise maintained at 6 percent and 7 percent, respectively.

**The latest baseline forecasts show a slightly lower path. Baseline inflation is seen to settle at an average of 3.6 percent for 2024, and 3.2 percent for 2025.** The forecast path is driven by the lower-than-expected inflation outturns, peso appreciation, and lower global crude oil prices, partly offset by higher assumptions for global non-oil prices, stronger domestic growth outlook, impact of El Niño weather conditions, and minimum wage adjustments in areas outside NCR.

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

**The estimated impact of upside risks on the inflation outlook outweighs the possible effect of downside risks.** Nevertheless, the risk-adjusted forecast of 3.9 percent for 2024 is now within the BSP's inflation target range. Meanwhile, inflation could settle at 3.5 percent in 2025. The risk-adjusted forecast is lower for 2024 which can be attributed to the lower baseline forecast and the decline in the estimated risks for the year. The lower estimated impact of risks for 2024 emanates from (1) the removal of the impact of higher transport fares from the jeepney modernization; (2) lower probability of fare hikes for traditional jeepneys; (3) lower impact of higher global oil prices; and (4) the removal of the risk from the non-extension of Executive Order (E.O.) No. 10. Meanwhile, the risk-adjusted forecast for 2025 is relatively steady due mainly to the shift in the assumed implementation of higher electricity rates.

**Inflation expectations are more firmly anchored within the target range.** The results of the BSP's survey of external forecasters for February 2024 showed unchanged mean inflation forecast for 2024 (at 3.9 percent) as well as for 2026 (at 3.4 percent) relative to the forecasts in the January 2024 survey round. By contrast, the mean inflation forecast for 2025 rose to 3.5 percent (from 3.4 percent).

**Domestic economic activity is seen to remain intact over the medium term.** The projected GDP growth path is supported by the improved global growth outlook and decline in global crude oil prices, tempered in part by the lagged impact of the policy rate adjustments. While the projected impact of the BSP's policy rate adjustments is likely to peak in 2024, growth in the medium term could also be supported by structural reform measures that could enhance investment climate as well as economic sentiment in the country.

**The economy is projected to operate slightly below its potential.** The output gap is estimated to be broadly neutral in Q4 2023, and will turn slightly negative over the rest of the policy horizon. The overall balance of demand and supply conditions, as captured by the output gap, indicates possible disinflationary pressures over the policy horizon.

**In consideration of prevailing risks, the BSP deems it appropriate to keep monetary policy settings unchanged in the near term even as inflation conditions continue to improve.** The decline in headline inflation, as well as the sustained downtrend in core inflation since Q2 2023, suggests that inflation momentum may continue to decelerate in the coming months in the absence of additional supply shocks. In the meantime, non-monetary measures to address lingering supply-side pressures on prices and sustain the disinflation process.

**At the same time, the BSP remains ready to adjust its monetary policy settings as necessary** in keeping with its primary mandate to safeguard price stability.

# I. Economic Outlook

## 1. Baseline Forecasts

**The latest baseline forecasts show a slightly lower path compared to the previous Monetary Policy Report (MPR).** Inflation is projected to average at 3.6 percent for 2024, slightly lower by 0.1 percentage point (ppt). The downward revision is driven by lower-than-expected inflation outturns, peso appreciation, and lower global crude oil prices, partly offset by higher assumptions for global non-oil prices, stronger domestic growth outlook, impact of *El Niño* weather conditions, and minimum wage adjustments in areas outside NCR (AONCR). Meanwhile, the inflation forecast for 2025 is broadly unchanged at 3.2 percent.

**Inflation is projected to average within the target range over the policy horizon.** While inflation is likely to settle within the target in Q1 2024, inflation could rise temporarily above the target for the period April to July 2024 due to possible price pressures from lower domestic supply of rice and corn as well as positive base effects due to the slowdown in food and energy inflation during the same period in 2023. Subsequently, inflation is projected to return to the target range for the rest of the year.

**Table 1. BSP Average Baseline Inflation Projections**
in percent

| | November 2023 MPR[a] | February 2024 MPR[b] |
|---|---|---|
| **2024** | 3.7 | 3.6 |
| **2025** | 3.2 | 3.2 |

Source: BSP estimates
[a] Baseline forecasts from 16 November 2023 monetary policy meeting
[b] Baseline forecasts from 14 February 2024 monetary policy meeting

**Domestic economic activity will remain intact over the medium term, but growth could settle below the DBCC's target of 6.5-7.5 percent for 2024 and 6.5-8.0 percent for 2025.**[4] The projected GDP growth path is supported by the improved global growth outlook and decline in global crude oil prices, tempered in part by the lagged impact of the policy rate adjustments.

While the projected impact of the BSP's policy rate adjustments is likely to peak in 2024, growth in the medium term could also be supported by structural reform measures that could enhance investment climate as well as economic sentiment in the country.[5] These measures include the recent ratification of the Regional Comprehensive Trade Partnership (RCEP) Agreement, which is seen to support greater market access for goods and services, reduced trade barriers, and improved export competitiveness from simplified and harmonized rules. Complementary to RCEP's ratification is the recent implementation of key economic liberalization laws such as the amendments to the Retail Trade Liberalization Act (RTLA), Foreign Investments Act (FIA), Public Service Act (PSA), and the Build-Operate-Transfer (BOT) Law.

[4] Based on the on the 186th Development Budget Coordination Committee (DBCC) Meeting on 15 December 2023.
[5] These measures have not been incorporated in the baseline GDP growth forecasts.

**Nonetheless, the economy is projected to operate slightly below its potential.** The output gap is estimated to be slightly negative in Q4 2023 with the economy projected to operate slightly below its potential over the policy horizon. The overall balance of demand and supply conditions, as captured by the output gap or the difference between actual and potential output, indicates possible disinflationary pressures over the policy horizon.

Estimates from the BSP's Policy Analysis Model for the Philippines (PAMPh)[6] indicate that the output gap is estimated to be slightly negative in 2024 and 2025, as the impact of previous policy interest rate adjustments takes hold on the economy. A projected slowdown in global growth owing in part to tight monetary conditions across countries could likewise dampen aggregate demand. Nonetheless, the output gap could be supported by higher consumption owing to higher wages and the increased value of remittances amid a peso depreciation. Meanwhile, potential output is expected to be sustained by improvements in labor market conditions and continued investment growth. Productivity growth is also seen to continue owing largely to generally robust economic activity and robust infrastructure spending. Moreover, key structural reforms, such as Corporate Recovery and Tax Incentives for Enterprises (CREATE), RCEP, and PSA could shore up investments and business activity, which could in turn help accelerate the country's potential output.

**The exchange rate is expected to settle within the DBCC's assumptions of ₱55.00-58.00/US$1 for 2024 and 2025.**[7] The projected exchange rate for 2024 and 2025 appreciated from previous round due mainly to the wider real interest rate differential arising from the expected larger interest rate reduction by the US Federal Reserve in 2024.

## 2. Key Forecast Assumptions

### *External Factors*

**World GDP Growth.** The global economy is seen to grow below historical average over the policy horizon. While the latest assumptions for 2024 and 2025 are higher compared to the previous round on account of greater-than-expected resilience in the United States, as well as the renewed fiscal support in China, global growth is seen to remain below the pre-pandemic historical average of 3.6 percent from 2000-2019 owing mainly to elevated central bank policy rates to fight inflation and a withdrawal of fiscal support amid high debt weighing on economic activity.

In its January 2024 World Economic Outlook (WEO) Update, the International Monetary Fund (IMF) projects global growth for 2024 at 3.1 percent, higher by 0.2 ppt from the October 2023 WEO. Meanwhile, the forecast for 2025 is unchanged at 3.2 percent. The IMF noted that the likelihood of a hard landing has receded and that the risks to the global outlook are broadly balanced compared to the assessment in the October 2023 WEO.

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[6] The PAMPh is a monetary policy model for a small open economy like the Philippines. It is a semi-structural gap model based on New Keynesian foundations with a general equilibrium framework and forward-looking features that allow for the assessment of the dynamic path of key macroeconomic variables in a theoretically consistent manner. The BSP is currently undergoing a multi-year technical assistance (TA) mission with the IMF's Institute for Capacity Development to further improve the structural features and forecasting performance of the PAMPh to serve as the BSP's workhorse model for medium-term forecasting and policy analysis.

[7] Based on the on the 186th Development Budget Coordination Committee (DBCC) Meeting on 15 December 2023.

**Table 2. World GDP Growth**
in percent

| | November 2023 MPR | February 2024 MPR |
|---|---|---|
| **2024** | 2.9 | 3.1 |
| **2025** | 3.2 | 3.2 |

Source: WEO Update (IMF, January 2024), WEO (IMF, October 2023)

**Dubai Crude Oil Prices.** Global crude oil prices are set consistent with oil futures market data and the latest assessment by international energy agencies on the outlook for the global oil market. Developments in the domestic oil market in turn are assumed to broadly follow the trend in the world oil market. The Dubai crude oil assumptions in the latest round are based on the average futures path from 23 January to 5 February 2024.

**Table 3. Dubai Crude Oil Price Assumptions**
average, in US$ per barrel

| | November 2023 MPR | February 2024 MPR |
|---|---|---|
| **2024** | 82.3 | 77.5 |
| **2025** | 78.0 | 73.5 |

Source: Bloomberg, BSP Estimates

**Assumptions for global crude oil prices are lower compared to the previous round.** The latest futures path shows crude oil prices declining in the next two years as production growth is expected to slightly outpace demand increase, allowing inventories to build up modestly and contribute to downward pressures on crude oil prices. This reflected projections of lower global fuel consumption growth over the next two years, with the US Energy Information Agency (US EIA) citing the slowdown of oil demand in China due to easing GDP expansion, shift to electric cars, and the end to the post-pandemic recovery-related growth. The increase in global oil production is also seen to slowdown as OPEC+ continues its policy of production restraint. Nonetheless, global production is still anticipated to exceed consumption by mid-2025, leading to an increase in petroleum inventories from non-OPEC countries.

To determine the impact on the inflation forecasts for 2024 and 2025 of various outturns for world oil prices, scenarios ranging from US$70-US$130 per barrel were simulated. The scenarios assume that oil prices are sustained at these levels starting in March 2024. Inflation is seen to breach the upper end of target range if Dubai crude oil price averages above US$90 per barrel in 2024 and around US$95 per barrel in 2025. It should be noted that these oil price scenarios considered only the direct effects and do not incorporate any potential second-round effects on transport fares, food prices, and wage increases among others.

**Table 4. Impact of Alternative Dubai Crude Oil Price Scenarios on Inflation**
in percentage points

| Year | 2024 | 2025 |
|---|---|---|
| Baseline Inflation Forecast (in US$) | 3.6 | 3.2 |
| 70 | 3.4 | 3.0 |
| 75 | 3.5 | 3.2 |
| 80 | 3.7 | 3.5 |
| 85 | 3.8 | 3.7 |
| 90 | 4.0 | 3.9 |
| 95 | 4.1 | 4.1 |
| 100 | 4.2 | 4.3 |
| 105 | 4.4 | 4.5 |
| 110 | 4.5 | 4.7 |
| 115 | 4.6 | 4.9 |
| 120 | 4.7 | 5.0 |

Source: BSP estimates

**World Non-Oil Prices.** The latest assumptions for global non-oil commodities show a continued decline in prices over the policy horizon, but at a slower rate compared to previous round for 2024, based on the IMF's January 2024 WEO Update. Global non-fuel price inflation is seen to decline by 0.9 percent in 2024 and 0.4 percent in 2025 compared to the previous assumption of 2.7 percent and 0.1 percent decrease for 2024 and 2025, respectively. Adverse risks from commodity price spikes amid geopolitical and weather shocks remain. The conflict in Gaza and Israel could escalate further, while continued attacks in the Red Sea and the ongoing war in Ukraine could lead to resurgence of supply-side constraints. Container shipping costs have already increased sharply and the situation in the Middle East remains volatile. More extreme weather shocks, including floods and drought, together with the *El Niño* phenomenon, could also cause spikes in food prices.

**Table 5. World Non-Oil Price Inflation**
in percent

| | November 2023 MPR | February 2024 MPR |
|---|---|---|
| **2024** | -2.6 | -0.9 |
| **2025** | -0.1 | -0.4 |

Source: WEO (IMF, November 2023), WEO Update (IMF, July 2023)

**Federal Funds Rate.** The latest federal funds rate assumptions, based on the futures prices as of 5 February 2024, are lower for 2024 and 2025 relative to the previous round. The current futures path is consistent with the market expectations of the US Federal Reserve keeping the federal funds rate target unchanged until April 2024. Markets are pricing in a 100-bp easing in 2024 starting in May with an additional 75-bp rate cut in 2025. By contrast, the Federal Open Market Committee's (FOMC's) dot plot in its December 2023 meeting indicated a 75-bp cut in 2024 followed by a 100-bp cut in 2025.

**Table 6. Federal Funds Rate**
end-period, in percent

| | November 2023 MPR | February 2024 MPR |
|---|---|---|
| **2024** | 4.6 | 4.3 |
| **2025** | 4.1 | 3.6 |

Source: Bloomberg

### *Domestic Factors*

**RRP Rate and Reserve Requirement Ratio (RRR).** The forecast path assumes unchanged interest rate over the policy horizon with the target RRP rate at 6.50 percent. Meanwhile, the RRR was maintained at 9.5 percent until end-2025.

**Wages.** The baseline forecast is consistent with the ₱40.00 minimum wage hikes for NCR in July 2023 as well as the 8.7 percent average wage increase for non-agricultural workers in AONCR. Furthermore, further increases of ₱28.00 in August 2024 and ₱29.00 in September 2025 are assumed. This is equivalent to an annual increase of 4.6 percent for both years, in line with historical wage increases.

**Fiscal Sector.** The baseline inflation forecasts are consistent with the government's fiscal deficit assumption of 5.1 percent for 2024 and 4.1 percent for 2025 based on the medium-term fiscal program of the DBCC as of 15 December 2023.

**Alcoholic Drinks.** The baseline forecasts reflect the impact of annual adjustments in the prices of alcoholic beverages (0.7 percent of the CPI basket) as mandated in Republic Act (R.A.) no. 11467. Higher excise taxes for fermented liquor, wine, and distilled spirits will be implemented on a staggered basis from 2020 to 2024 and shall increase by 6.0 percent every year from 2025 onwards.

**Tobacco Products.** The President signed R.A. no. 11346, increasing further the excise tax on tobacco products (0.9 percent of the CPI basket) to fund the Universal Healthcare Act. Under the law, the tax per pack of cigarettes will be raised on a staggered basis to ₱60.00 per pack in 2023 and subject to a 5.0 percent annual indexation onwards.

**Table 7. Excise Tax**

| Year | Cigarettes (₱ per pack) | Fermented Liquor (₱ per liter) | Wine (₱ per liter) | Distilled Spirits | |
|---|---|---|---|---|---|
| | | | | Excise Tax (₱ per liter) | Ad Valorem Tax (%) |
| **2024** | 5% | 43.0 | 63.1 | 66.0 | 22% |
| **2025** | | | 6% indexation | | 22% |

Source: R.A. nos. 11346 and 11467

**Water Rates.** The Metropolitan Waterworks and Sewerage System (MWSS) approved the rate hike requests of Manila Water Company and Maynilad Water Services for 2023-2026. The water rate rebasing process is conducted every five years to set the rates for water and sewerage services for water concessionaires to recover its operating, capital, maintenance, and investment expenditures. The second tranche of the rate rebasing adjustment took effect on 1 January 2024 with Maynilad Water Services Inc. raising rates by an average of ₱7.87 per cubic meter and Manila Water Co. Inc. increasing their rates by an average of ₱6.41 per cubic meter. For the subsequent years, the rates for Manila Water customers will be higher by ₱3.25 in 2025, ₱3.00 in 2026, and ₱1.08 in 2027 per cubic meter.

Meanwhile, the rates for Maynilad customers will be higher by ₱2.12 in 2025, ₱0.84 in 2026, and ₱0.80 in 2027.

**Lower domestic supply due to weather conditions and higher global prices.** The baseline forecast considers NEDA's latest supply and demand outlook indicating total rice and corn supplies to contract year-on-year (y-o-y) for the period Q2 to Q4 2024. The NEDA projections reflect the impact of *El Niño* and other weather disturbances as well as higher global prices, with *El Niño* dry conditions seen to be strong until February 2024 before transitioning to weak conditions from March to May 2024 and reverting to ENSO-neutral conditions from June 2024 onwards, based on the latest climate outlook of PAGASA as of 24 January 2024. Despite weakening *El Niño* conditions by June 2024, rice and corn prices are expected to remain higher for the rest of 2024 due to the projected decline in domestic supply.

## 3. Risks to the Outlook

**While the risks to the inflation outlook continue to tilt toward the upside over the policy horizon, inflation risks in 2024 have eased compared to the previous round.** The latest fan chart remains skewed towards the upside as reflected in the high probability of inflation breaching high-end of the target band in 2024 to 2025.

Using the 90 percent confidence interval for the fan chart, estimates indicate that the probability of average annual inflation settling within the 3.0 percent ± 1.0 percentage point target range is 44.6 percent for 2024 and 49.7 percent for 2025. The probability of inflation breaching the high end of the target range is 51.4 percent for 2024 and 37.1 percent for 2025. This reflects the downward adjustment in the baseline forecasts over the policy horizon.

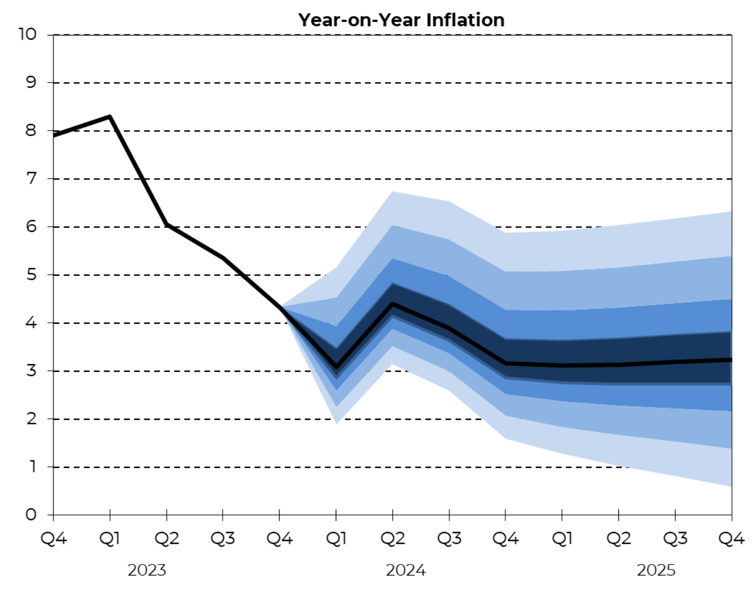
The latest probability distribution shows a higher likelihood of inflation settling within the target for 2024 at 44.6 percent compared to 42.8 percent in the previous round. Meanwhile, the probabilities of inflation breaching the low end of the target range for 2024 to 2025 remain low.

**Table 8. Probability Distribution of Inflation Forecasts**
in percent

| | Pr(<2%) | | Pr(2-4%) | | Pr(>4%) | |
|---|---|---|---|---|---|---|
| | Nov 2023 MPR | Feb 2024 MPR | Nov 2023 MPR | Feb 2024 MPR | Nov 2023 MPR | Feb 2024 MPR |
| **2024** | 3.4 | 4.0 | 42.8 | 44.6 | 53.8 | 51.4 |
| **2025** | 12.8 | 13.2 | 49.5 | 49.7 | 37.7 | 37.1 |

Source: BSP estimates

**Figure 1. Inflation Projection**
**in percent**




Source: BSP estimates

## Table 9. Inflation Projection Ranges at Various Confidence Intervals Using the Fan Chart

in percent

| Confidence Interval (%) | Projection Range (%) | |
|---|---|---|
| | 2024 | 2025 |
| **80** | 2.6 – 5.5 | 1.4 – 5.5 |
| **90** | 2.3 – 6.1 | 0.9 – 6.1 |

Source: BSP estimates

## Table 10. Risk Matrix[8]

| | Risks | Probability | |
|---|---|---|---|
| | | **November 2023 MPR** | **February 2024 MPR** |
| **Upside Risks** | Higher electricity rates | High | High |
| | Higher transport charges | Medium | Low |
| | Higher oil prices | Medium | Low |
| | Higher domestic food prices | Medium | Medium |
| | Impact of *El Niño* conditions | Medium | Low |
| **Downside Risk** | Measures to Mitigate Impact of *El Niño* | Medium | Low |

[8] The BSP considers different scenarios that pertain to upside and downside risks to the inflation outlook, which is summarized in a risk matrix. The various scenarios are then assigned probability values. Scenarios that have more than 75 percent probability of taking place over the forecast horizon are incorporated in the baseline. The estimated impact of each scenario is then multiplied by the assigned probabilities. The sum of the weighted impact for each year will indicate whether the risks to the outlook are balanced, on the upside, or on the downside.

**The estimated impact of upside risks to the inflation outlook outweighs the possible impact of downside risks.** Should the risks materialize at their assigned probabilities, inflation is seen to average at 3.9 percent in 2024 and 3.5 percent in 2025.

Compared to the previous MPR, the risk-adjusted forecast is lower for 2024 by 0.5 ppt, which can be attributed to the lower baseline forecast and the decline in the estimated risks for the year. The lower estimated impact of risks for 2024 emanates from the removal of the impact of higher transport fares from the jeepney modernization; the lower probability of fare hikes for traditional jeepneys; the lower impact of higher global oil prices; and the removal of the risk from the non-extension of E.O. no. 10. Meanwhile, the risk-adjusted forecast for 2025 is only marginally higher by 0.1 ppt percent due mainly to the shift in the assumed implementation of higher electricity rates.

**Table 11. BSP Baseline and Risk-Adjusted Projections**
in percent

| | | November 2023 Monetary Policy Report | February 2024 Monetary Policy Report |
|---|---|---|---|
| Baseline inflation forecast | 2024 | 3.7 | 3.6 |
| | 2025 | 3.2 | 3.2 |
| Risk-adjusted inflation forecast | 2024 | 4.4 | 3.9 |
| | 2025 | 3.4 | 3.5 |

The upside risks to the inflation outlook could emanate from higher transport charges, increased electricity rates, higher oil and domestic food prices, and the additional impact on food prices of a strong *El Niño* episode. Meanwhile, the implementation of government measures to mitigate the impact of *El Niño* weather conditions is the primary downside risk to the outlook.

**Electricity rates could further increase in 2024.** In July 2023, the Supreme Court nullified Energy Regulatory Commission's (ERC) 2014 decision to cap Wholesale Electricity Market (WESM) prices in November to December 2013. The ERC's decision was made to address the higher prices during the maintenance shutdown of the Malampaya gas field. The risk scenario assumes that an estimated ₱22 billion worth of power generation cost will be passed on to consumers starting in June 2024 with the adjustment spread equally over the next two years.

A high probability is assigned to this risk as the ERC is set to release an order that will authorize the collection of the said power generation cost.

**Higher transport charges also provide upside risks to the inflation outlook.** On 8 October 2023, the LTFRB approved a ₱1.00 provisional increase in the minimum jeepney fare for both traditional and modern jeepneys. As the original petition indicated a ₱5.00 increase, the alternative scenario assumes that the remaining ₱4.00 will be approved and implemented by Q2 2024. A low probability is assigned to this risk given the on-going jeepney modernization.

In addition, a petition was filed by the MRT-3 management with the Department of Transportation (DOTr) on 3 July 2023 to raise the minimum fare of the rail line from ₱13.00 to ₱19.00. A high probability is assigned to this risk following the adjustments in LRT-1 and LRT-2 fares. The alternative scenario assumes implementation by Q2 2024.

Similarly, taxi operators have filed a petition with the LTFRB to raise the ₱5.00 provisional increase in the flagdown rate granted in October 2022, bringing the flagdown rate from the current ₱45.00 to ₱55.00. The scenario assumes that the LTFRB will grant the increase by Q2 2024 with a low probability given broadly stable oil prices.

Meanwhile, the risk of higher jeepney fares following full implementation of the public utility vehicle (PUV) modernization program included in the previous round has been removed. The year-end deadline for the consolidation of the PUV drivers and operators into cooperatives and corporations was moved to Q2 2024 which could push the timeline of the entire program beyond the policy horizon.

An overall low probability is assigned to this risk based on the CPI weights of the transport items.

**The escalation of conflicts in the Middle East could lead to higher global crude oil prices.** In addition to the conflict between Israel and Palestine, the intensification of tensions in Yemen due to attacks by Houthi rebels could disrupt world oil supply and induce additional uncertainty in global oil prices.

The risk scenario assumes Dubai crude oil prices averaging at US$90/bbl in 2024 based on the peak price levels experienced during start of the Israel-Hamas conflict in 2023. A low probability is assigned to this scenario as tensions have eased and there are no indications of escalation into a direct military exchange between the two regional enemies.

**Ongoing supply constraints on livestock, poultry, fish, sugar, and onions could cause a slight uptick to inflation.**

- Pork prices remain elevated compared to previous year with the recovery in domestic hog industry still reeling from the impact of the African Swine Fever (ASF) outbreak. As of 19 January 2024, active ASF cases increased to 12 regions from only six in end-December 2023 based on data from the Bureau of Animal Industry (BAI). A medium probability is assigned to this risk with the ASF vaccine still undergoing trials and amid ban of entry of live hogs and pork products in some local government units.

- Meanwhile, after high production costs and the Avian Influenza (AI) put a strain on producers' operations since 2022, chicken meat prices have stabilized while farmgate prices of eggs have declined in 2023 following easing consumption and expanding supply due to favorable weather. A low probability is assigned to this risk with no new cases of AI reported since 13 January 2024.

- Average prices of fish have continued to creep up from December 2023 amid the closed fishing season. While the DA issued Circular No. 36 dated 15 August 2023 on the importation of 35,000 MT of frozen fish, all import clearances are deemed expired after 15 January 2024. A medium probability is assigned to this risk in the absence of adequate sustainable fisheries production programs to ensure sufficiency of fish supply.

- Sugar Regulatory Administration Resolution 2023-159, signed on 26 September 2023 and released on 5 October 2023, halted the release of sugar imports to keep farmgate prices at around ₱3,000 per bag. The resolution applies to the 150,000 metric tons of imported sugar under Sugar Order No. 7 issued in July 2023. A medium probability is assigned to this risk in the absence of a new import program.

- As of January 2024, onion prices remained elevated albeit lower y-o-y. While the DA expects positive growth in harvest in 2024, infestation of armyworms could negatively affect yield. In Nueva Ecija, the DA reported that 366 hectares out of the 10,217 hectares of farmlands planted to onion have been infested by armyworms. In addition, the DA Secretary has ordered a temporary halt to onion imports until May 2024 – possibly extending through July – if domestic harvest of the high value crop remains sufficient to meet local demand. A medium probability is assigned to this risk with the temporary halt in onion imports and possible worsening of armyworms infestation.

An overall medium probability is assigned to this risk based on the relative weights of the commodities in the CPI basket. The scenario assumes that the elevated price levels of the identified commodities will be sustained until Q2 2024.

**Further declines in crop production due to strong *El Niño* conditions could lead to higher rice prices.** The baseline scenario considers strong *El Niño* conditions until February 2024, easing to moderate conditions in Q2 2024. The risk scenario assumes the strong *El Niño* to persist until Q2 2024, further increasing rice prices due to lower rice production until the end of the year. A low probability is assigned to this risk based on the latest climate outlook from PAGASA.

**The effective implementation of government measures to combat the impact of *El Niño* could lower inflation.** Government measures include improvement and concreting of irrigation canals, distribution of pumps and engine sets, construction of solar powered irrigation system, established greenhouses, provision of planting materials and farm supplies, various support to fisheries sector, and information campaigns on *El Niño*.

### Box article no. 1: Monetary policy developments

On 14 December 2023, the BSP kept the target RRP rate unchanged at 6.5 percent. Accordingly, the interest rates on the overnight deposit and lending facilities remained at 6.0 percent and 7.0 percent, respectively.

Relative to the November 2023 MPR, the baseline inflation forecast presented in the 14 December 2023 policy meeting was unchanged at 3.7 percent for 2024 and 3.2 percent for 2025. The forecast path was driven by the lower-than-expected inflation outturn in November 2023, lower world crude oil prices, and the peso appreciation, which offset in full the impact of stronger domestic growth outlook, strong El Niño weather conditions, and minimum wage adjustments in areas outside NCR.

| | | November 2023 MPR [a] | December 2023 MPR [b] |
|---|---|---|---|
| **Baseline inflation forecast** | **2024** | 3.7 | 3.7 |
| | **2025** | 3.2 | 3.2 |
| **Risk-adjusted inflation forecast** | **2024** | 4.4 | 4.2 |
| | **2025** | 3.4 | 3.4 |

Source: BSP estimates
[a] Baseline forecasts from 16 November 2023 monetary policy meeting
[b] Baseline forecasts from 14 December 2023 monetary policy meeting

Compared to the November policy meeting, the risk-adjusted inflation forecast for 2024 declined to 4.2 percent, reflecting lower estimates of inflation risks. Meanwhile, the risk-adjusted forecast for 2025 was stable at 3.4 percent.

The balance of risks to the inflation outlook leaned significantly toward the upside. Key upside risks included higher transport charges, increased electricity rates, higher oil prices, non-extension of E.O 10, higher domestic food prices, and the additional impact of strong El Niño episode persisting until Q2 2024 on food prices, utility rates and utility rates. Meanwhile, the impact of a relatively weak global recovery as well as government measures to mitigate the effects of El Niño weather conditions could reduce the central forecast. Meanwhile, the impact of a weaker-than-expected global recovery and successful implementation of government measures to mitigate impact of El Niño weather conditions are the primary downside risks to the outlook.

With the sum of the latest information available during the December meeting, the BSP continued to see the need to keep monetary policy settings sufficiently tight to allow inflation expectations to settle more firmly within the target range. The BSP also noted that previous adjustments have continued to work their way through the economy, as can be seen from the declining path for core inflation. The national government’s non-monetary interventions were seen to remain crucial to sustain the disinflation process. Going forward, the BSP remains ready to adjust monetary policy settings as necessary, in line with its mandate to ensure price stability.

# II. Current Developments

## Overview of current developments

**Headline inflation eases further in January 2024.** Inflation eased further to 2.8 percent in January 2024 from 3.9 percent in December 2023. The January inflation rate was the lowest since October 2020 when inflation was at 2.3 percent. The bulk of the decline can be traced primarily to lower y-o-y food inflation as prices of vegetables, tubers, plantains, cooking bananas and pulses, and meat and other parts of slaughtered land animals declined. Inflation for fish and other seafood also slowed. Similarly, non-food inflation eased owing to slower price increases of housing, water, electricity, gas and other fuels.

**Core inflation points to sustained easing in underlying price pressures.** The official core inflation further moderated to 3.8 percent in January 2024 from 4.4 percent in the previous month. Similarly, the alternative measures of core inflation also continued to ease in January 2024.

**Global crude oil prices increase amid concerns on possible supply disruptions.** Dubai crude oil prices slightly increased in the first week of February 2024 from the full-month average price in January, driven primarily by fears of possible supply disruptions due to the on-going geopolitical tensions in the Middle East; continued disputes in the Red Sea; and Ukraine's attacks on Russian oil facilities. The uptick in oil prices was partly tempered by possible ceasefire between Israel and Hamas.

**Inflation expectations for 2024 and 2026 are steady while mean inflation forecast for 2025 increased slightly.** Results of the BSP's survey of external forecasters for February 2024 showed unchanged mean inflation forecasts for 2024 at 3.9 percent and 2026 at 3.4 percent relative to the results of the January 2024 survey round. Meanwhile, the mean inflation forecast for 2025 increased slightly to 3.5 percent from 3.4 percent. Analysts expect inflation to remain manageable this year and settle within the target range. However, risks to the inflation outlook continue to be dominated by upside pressures owing to supply-side shocks and second-round effects.

**Domestic economy continues to expand in Q4 2023 despite global headwinds.** Real GDP grew by 5.6 percent y-o-y in Q4 2023, slower than the 6.0-percent growth posted in the previous quarter and 7.1-percent growth in the same period a year ago. This brought the full-year 2023 real GDP growth to 5.6 percent, which fell below the government target of 6.0 to 7.0 percent for 2023. On the demand side, household spending and investments grew by 5.3 percent and 11.2 percent, respectively. By contrast, government spending decreased by 1.8 percent. On the supply side, the services and agriculture sectors expanded by 7.4 percent and 1.4 percent, respectively, while the industry sector declined by 3.2 percent.

**Demand indicators continue to signal expansion although outlook points to easing in some subsectors.** The manufacturing sector's preliminary average capacity utilization rate eased but remained high at 74.3 percent in December 2023 from the revised month-ago level of 74.8 percent. Firms maintained factory capacity to support operations during the December holidays. Meanwhile, the preliminary composite PMI in January 2024 stood at 50.2 index points, lower than the previous month's PMI of 54.6 (revised). Slower expansions in the services and manufacturing sectors, as well as faster contraction in the retail and wholesale sector weighed on overall growth. For the month ahead, retail and wholesale managers anticipate further slowdown for the sector. Meanwhile, economic conditions for the manufacturing and services sectors are expected to improve in February 2024.

**Labor market conditions improve.** The unemployment rate fell to 3.1 percent in December 2023 from 3.6 percent in November 2023. The unemployment rate was also the lowest since it peaked at 17.6 percent at the onset of the pandemic in April 2020.

**Domestic liquidity remains adequate but market participants continue to price in the BSP's prior policy rate increases.** Preliminary data showed that domestic liquidity (M3) grew by 5.9 percent in December 2023 from 7.0 percent in November. During the same period, bank lending rose by 7.0 percent, the same rate of increase as in the previous month. In terms of credit conditions, lending standards based on the diffusion index method were mixed with a net tightening of credit standards on businesses and net easing on households. In the government securities market, the auctions of the Bureau of the Treasury were fully awarded amid strong demand.

**Prospects for global economic growth improve, as downside risks to economic activity recede.** The JP Morgan All-Industry Output Index increased in December 2023 as output and new orders grew at faster rates. Meanwhile, the IMF raised its 2024 global economic growth projection to 3.1 percent, reflecting the greater-than-expected resilience in the US and several large emerging market and developing economies (EMDEs), as well as fiscal support in China. Nonetheless, global economic expansion is expected to remain well below the annual average of 3.8 percent until[9] at least 2025. Elevated central bank policy rates to fight inflation, the withdrawal of fiscal support and high debt, as well as low underlying productivity growth were seen to weigh on economic activity.

[9] Historical average global growth from 2000–2019

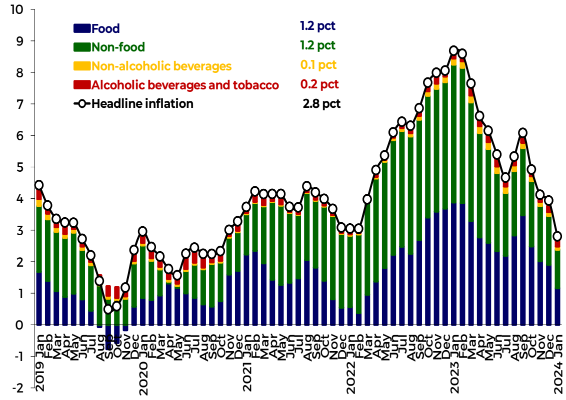
## 1. Price Conditions

**Headline inflation.** The y-o-y headline inflation fell to 2.8 percent in January 2024 from 3.9 percent in December 2023. The January inflation rate is the lowest since October 2020 when inflation was at 2.3 percent. The bulk of the decline can be traced primarily to lower y-o-y food inflation as prices of vegetables and meat fell while inflation for fish and other seafood slowed. Non-food inflation also moderated as a result of slower price increases of housing, water, electricity, gas and other fuels, along with the decline in transport inflation. On a month-on-month (m-o-m) seasonally adjusted basis, inflation declined to -0.1 percent in January 2024 from 0.1 percent in the previous month.

Of the 315 total CPI items, the number of items with inflation rates above the threshold of 4.0 percent decreased significantly to 118 in January 2024 from 140 items in the previous month. These 118 items accounted for around 40.8 percent of the total CPI weight, lower than the 44.8 percent share in the previous month.

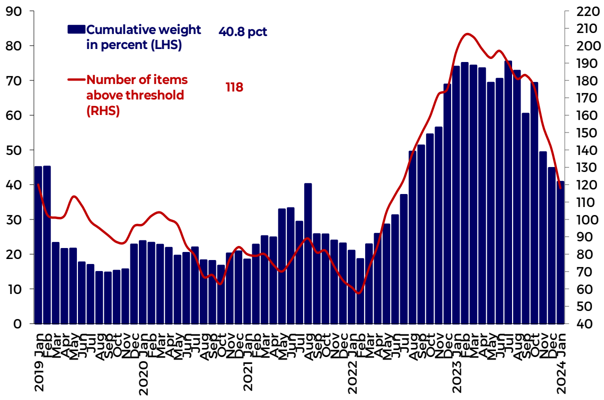
The number of CPI items below target increased to 112 items in January 2024 from 94 items in December 2023. These 112 items accounted for 25.3 percent of the total CPI weight, higher than the 20.3 percent in the previous month. The remaining 85 CPI items in January 2024 (which accounted for 33.8 percent of the total CPI weight) were within threshold.

**Figure 2. Headline Inflation**
(2018=100); in percent




Source: Philippine Statistical Authority (PSA), BSP

**Figure 3. CPI Items with Inflation Rates Above Threshold (2018=100)**

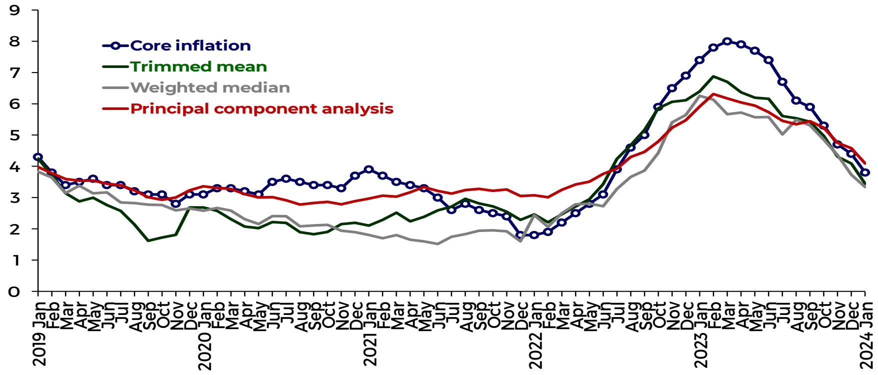



Source: PSA, BSP staff estimates

**Core inflation.** The official core inflation further eased to 3.8 percent in January 2024 from 4.4 percent in December 2023. Similarly, other measures of core inflation also continued to ease in January 2024.

## Figure 4. Estimates of Core Inflation Measures

y-o-y; in percent




Note: Core inflation excludes ten (10) volatile food and energy CPI items from the headline CPI equivalent to around 29.6 percent of total basket. This includes (1) cereals (rice and corn); (2) meat, fresh, chilled and frozen; (3) fish, live, fresh, chilled and frozen; (4) dates, figs, and tropical fruits; (5) other vegetables, fresh and chilled; (6) fruit-bearing vegetables; (7) electricity; (8) liquefied hydrocarbons; (9) diesel; and (10) gasoline. In total, this accounts for around 29.6 percent of total CPI basket.
Sources: PSA and BSP staff calculations using 5-digit disaggregation for the BSP-computed core inflation namely, trimmed mean, and weighted median.

**Food inflation.** Food inflation moderated to 3.5 percent in January 2024 from 5.4 percent in December as prices of vegetables, tubers, plantains, cooking bananas and pulses, and meat and other parts of slaughtered land animals declined. Similarly, inflation for fish and other seafood also slowed.

**Non-food inflation.** Non-food inflation also slowed down to 2.0 percent in January 2024 from 2.6 percent in the previous month as a result of slower price increases of housing, water, electricity, gas and other fuels. Transport inflation also declined y-o-y due to lower gasoline and diesel prices, along with easing inflation for sea fares.

## Table 11. Inflation rates for Selected Food Items (2018=100)

year-on-year; in percent

| Commodity | Jan 2023 | Dec 2023 | Jan 2024 |
|---|---|---|---|
| **Food and non-alcoholic beverages** | **10.7** | **5.4** | **3.5** |
| Food | 11.2 | 5.5 | 3.3 |
| Cereals and cereal products | 5.6 | 14.6 | 16.3 |
| Cereals | 3.6 | 17.9 | 20.5 |
| Rice | 2.7 | 19.6 | 22.6 |
| Corn | 16.0 | -3.5 | -4.3 |
| Flour, bread and other bakery products, pasta products, and other cereals | 11.3 | 6.3 | 5.6 |
| Meat and other parts of slaughtered land animals | 7.0 | 0.2 | -0.7 |
| Fish and other seafood | 6.7 | 4.8 | 1.2 |
| Milk, other dairy products, and eggs | 11.3 | 7.4 | 5.6 |
| Oils and fats | 18.5 | -3.6 | -4.3 |
| Fruits and nuts | 9.8 | 12.2 | 10.0 |
| Vegetables tubers, cooking bananas and pulses | 37.8 | -9.2 | -20.8 |
| Sugar, confectionery and desserts | 38.8 | 0.1 | -1.0 |
| Ready-made food and other food products, n.e.c. | 9.2 | 5.0 | 4.7 |
| Non-alcoholic beverages | 6.5 | 4.0 | 3.4 |
| **Alcoholic beverages and tobacco** | **10.9** | **9.0** | **8.4** |

Source of basic data: PSA, BSP

## Table 12. Inflation Rates for Selected Non-Food Items (2018=100)

year-on-year, in percent

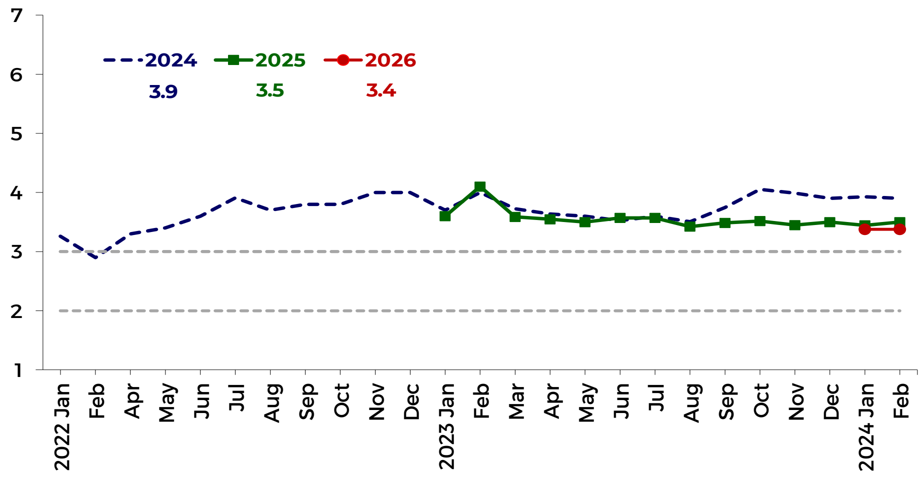
| Commodity | Jan 2023 | Dec 2023 | Jan 2024 |
|---|---|---|---|
| **Non-food** | **7.3** | **2.6** | **2.0** |
| Clothing and footwear | 4.4 | 4.2 | 3.8 |
| Housing, water, electricity, gas and other fuels | 8.6 | 1.5 | 0.7 |
| Electricty, gas, and other fuels | 15.9 | -3.8 | -4.7 |
| Furnishings, household equipment & routine household maintenance | 5.2 | 4.5 | 3.9 |
| Health | 3.3 | 3.7 | 3.3 |
| Transport | 11.1 | 0.4 | -0.3 |
| Passenger transport services | 13.0 | 3.3 | 2.8 |
| Information and communication | 0.7 | 0.5 | 0.5 |
| Recreation, sport and culture | 4.2 | 4.2 | 4.0 |
| Education services | 3.6 | 3.5 | 3.8 |
| Restaurant and accommodation services | 7.6 | 5.6 | 5.5 |
| Financial services | 0.0 | 0.0 | -0.6 |
| Personal care and miscellaneous goods and services | 5.0 | 4.6 | 4.0 |

Source of basic data: PSA, BSP

## 2. Inflation Expectations

Results of the BSP Survey of External Forecasters (BSEF) for the February 2024 round showed steady mean inflation forecasts for 2024 and 2026 at 3.9 percent and 3.4 percent, respectively, relative to the forecasts in the January 2024 survey round.[10] Meanwhile, the average inflation forecast for 2025 rose slightly to 3.5 percent from 3.4 percent.

**Figure 5. BSP Survey of External Forecasters**
mean forecast for full year; in percent




*Based on forecasts provided by 24 respondents. The survey was conducted from 6 to 12 February 2024.
Source: BSP

Analysts expect inflation to remain manageable this year and settle within the target range. However, risks to the inflation outlook continue to be dominated by upside pressures owing to supply-side shocks and second-round effects.

The upside risks to inflation are seen to emanate mainly from the potential rise in basic goods (particularly oil and food, including rice) and services (e.g., restaurants and accommodation services) owing to supply-side pressures attributed mainly to the adverse impact of *El Niño* and geopolitical conflicts in the Middle East and Red Sea. A few analysts also cited second-round effects from wage adjustments and higher electricity rates, as well as positive base effects as upside risks.

The downside risks to the inflation outlook are the (1) continued deceleration of food and non-food inflation, including oil; and (2) implementation of non-monetary government interventions such as E.O. no. 50 which lowers the import tariff of key food items, including rice. A few analysts also cited the subdued global demand as possible downside risks to inflation.

[10] There were 24 respondents in the BSP's survey of external forecasters in February 2024, based on submissions from 6 to 12 February 2024.

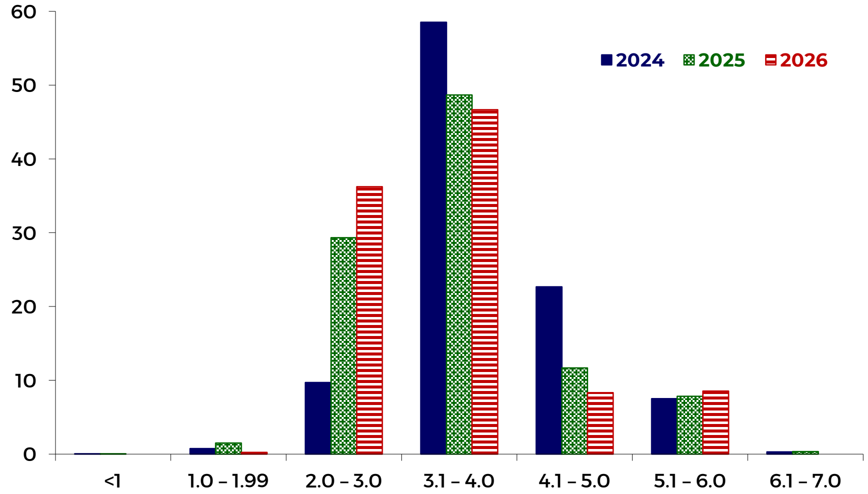
**Table 13. BSP Survey of External Forecasters**
annual percentage change; February 2024

| | 2024 | | | 2025 | 2026 |
|---|---|---|---|---|---|
| | Q1 | Q2 | FY | FY | FY |
| 1) Al-Amanah Islamic Bank | 3.00 | 3.90 | 6.00 | 6.00 | 6.00 |
| 2) ANZ | 2.90 | 4.00 | 3.50 | 3.00 | - |
| 3) Bangkok Bank | 3.20 | 3.50 | 3.60 | 3.50 | 3.30 |
| 4) Bank of Commerce | 3.09 | 4.41 | 3.76 | - | - |
| 5) Barclays | 3.20 | 4.30 | 3.70 | - | - |
| 6) Citibank | 2.90 | 3.90 | 3.40 | 3.30 | - |
| 7) CTBC Bank | 3.50 | 4.10 | 3.80 | 3.50 | 3.60 |
| 8) Deutsche Bank | - | - | 3.80 | 3.50 | - |
| 9) Eastwest Bank | 2.70 | 4.00 | 3.50 | 3.90 | 4.00 |
| 10) Land Bank of the Phils | 3.30 | 4.90 | 4.20 | 3.10 | 2.50 |
| 11) Maybank | 3.10 | 4.20 | 3.70 | 3.30 | 3.00 |
| 12) Maybank Investment Banking ( | 3.10 | 4.20 | 3.50 | 3.00 | 3.00 |
| 13) Metrobank | - | - | 4.30 | 4.30 | - |
| 14) Mizuho | 3.70 | 4.20 | 4.00 | 3.10 | - |
| 15) Modular Asset Management | 3.50 | 4.00 | 3.60 | 3.00 | 3.50 |
| 16) Nomura | 2.90 | 3.50 | 3.20 | 3.30 | - |
| 17) RCBC | 3.10 | 4.00 | 3.60 - 4.00 | 3.20 - 3.70 | 3.00 - 3.50 |
| 18) Regis Partners | - | - | 4.60 | 3.50 | - |
| 19) Philippine National Bank | 3.00 | 5.00 | 4.00 | 3.30 | 3.20 |
| 20) Security Bank | 3.50 | 4.30 | 3.70 | 3.20 | 3.00 |
| 21) Standard Chartered | 3.60 | 4.30 | 3.80 | 3.50 | - |
| 22) Sun Life Investment Managem | 3.80 | 2.00 | 3.80 | 2.70 | 3.00 |
| 23) Union Bank of the Phils. | 3.20 | 4.60 | 4.10 | 3.80 | 3.00 |
| 24) UBS | 3.15 | 4.05 | 3.57 | 3.05 | 2.79 |
| Median Forecast | 3.1 | 4.1 | 3.8 | 3.3 | 3.1 |
| **Mean Forecast** | **3.2** | **4.1** | **3.9** | **3.5** | **3.4** |
| High | 3.8 | 5.0 | 6.0 | 6.0 | 6.0 |
| Low | 2.7 | 2.0 | 3.2 | 2.7 | 2.5 |
| Number of Observations | 21 | 21 | 24 | 22 | 14 |
| **Government Target** | **3.0±1.01** | **3.0±1.01** | **3.0±1.01** | **3.0±1.01** | **3.0±1.00** |

Source: BSP

Based on the probability distribution of the forecasts provided by 17 out of 24 respondents, there is a 68.2-percent probability (from 63.4 percent) that inflation will settle within the 2-4 percent target range in 2024, and 31.0 percent chance that inflation will breach the upper end of the target range. For 2025, the probability that inflation will fall within the target band increased to 78.0 percent (from 65.9 percent). For 2026, there is an 82.9-percent (from 64.2 percent) chance of inflation settling well within the target band.

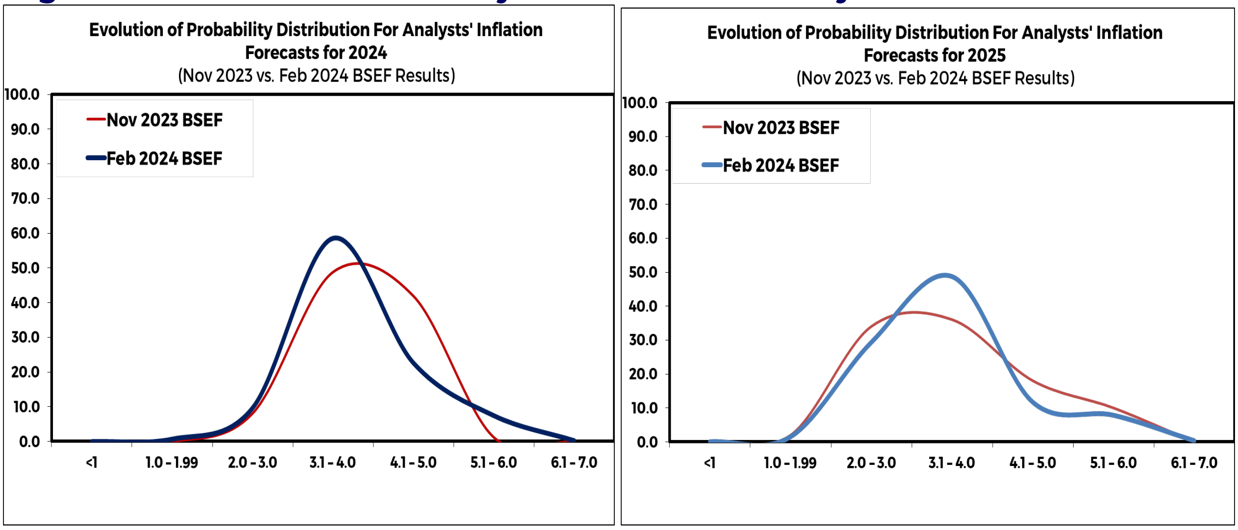
**Figure 6. Probability Distribution for Analysts' Inflation Forecasts* (2024-2026)**




*Probability distributions were averages of those provided by 17 out of 24 respondents.
Source: February 2024 BSP Survey

The results of the survey showed that majority of the analysts anticipate the BSP to keep the current policy setting until Q2 2024 before reducing the policy rate in the second half of this year by a range of 50 to 125 bps. For 2025, the BSP is seen to further loosen its policy stance by a range of 25 to 300 bps.

**Figure 7. Evolution of Probability Distribution for Analysts' Inflation Forecasts**

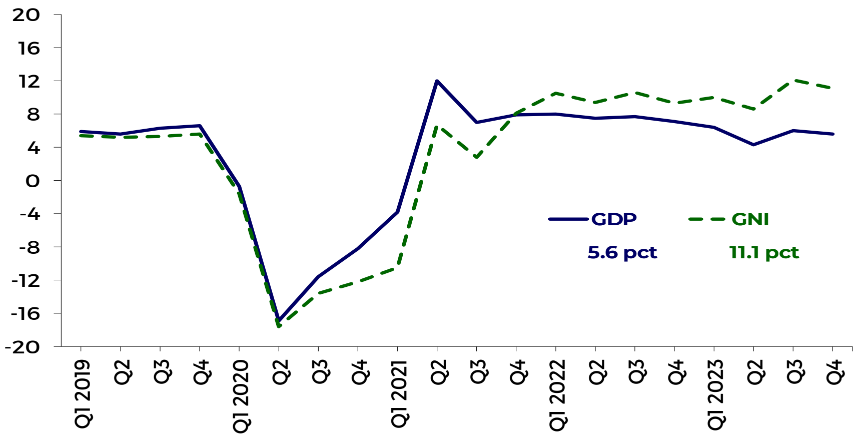



Relative to the November 2023 MPR, the shape of the February 2024 BSEF's probability distribution for analysts' inflation forecasts for 2024 and 2025 has shifted to the left (i.e., returning to within the inflation target band of 2-4 percent), which could indicate anchoring of inflation expectations. The probability distribution during the November 2023 round suggests heightened uncertainty with responses showing greater mass on a wider range of inflation outcomes.

## 3. Demand Conditions

Real GDP grew by 5.6 percent y-o-y in Q4 2023 from 6.0 percent in Q3 2023 and 7.1 percent in the same period a year ago. Output growth in Q4 2023 was supported by firm domestic demand.

**Figure 8. Gross Domestic Product and Gross National Income**
at constant 2018 prices; year-on-year growth in percent



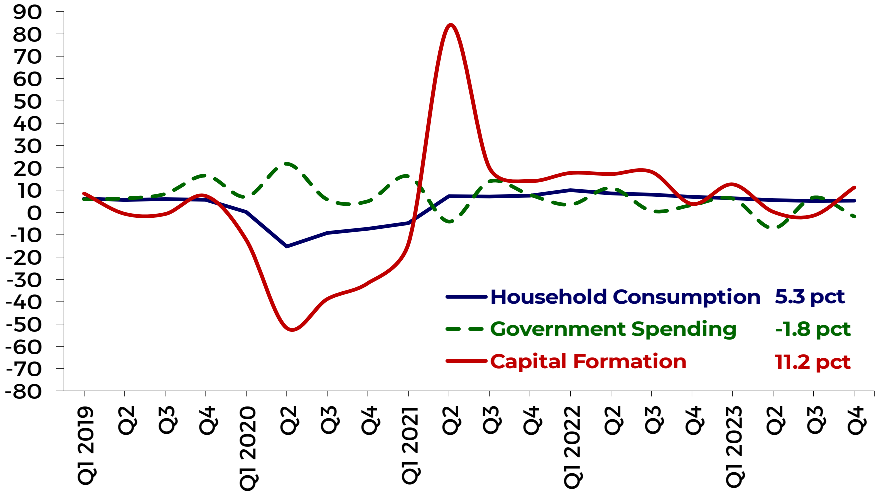

Source: PSA

The gross national income (GNI) grew by 11.1 percent y-o-y in Q4 2023 from 12.1 percent in Q3 2023 and 9.3 percent in Q4 2022. Net primary income moderated to 97.7 percent in Q4 2023 from the 111.6-percent growth in Q3 2023, albeit higher than the 59.9-percent increase in Q4 2022.

The full year 2023 real GDP growth stood at 5.6 percent, which is below the government target of 6.0 to 7.0 percent. On a seasonally adjusted basis, quarter-on-quarter (q-o-q) GDP growth also slowed down to 2.1 percent in Q4 2023 from 3.8 percent in the previous quarter.

**Aggregate demand.** Under the expenditure approach, household spending, government spending, investments (or capital formation), and exports contributed 4.0 percentage points (ppts), -0.2 ppt, 2.4 ppts, and -0.7 ppt, respectively, to total GDP growth in Q4 2023.

**Figure 9. Gross Domestic Product by Expenditure Shares**
at constant 2018 prices; growth rate in percent




Source: PSA

Household consumption, which accounted for 75.1 percent of GDP in Q4 2023, grew by 5.3 percent y-o-y during the review quarter, due to sustained strong consumer spending for restaurants and hotels, transport, and miscellaneous goods and services. This reflects some recovery in the labor market as well as steady growth in remittances.[11] Nevertheless, real spending on food items moderated amid still high food prices albeit moderating in recent months.

Capital formation or investments expanded by 11.2 percent in Q4 2023, a reversal of the 1.4-percent contraction in Q3 2023, owing to significant growth in fixed capital. In particular, the expansion in durable equipment more than offset the slowdown in construction.

In contrast, government expenditures decreased by 1.8 percent in Q4 2023, a reversal of the 6.7-percent increase in Q3 2023 and 3.3-percent growth in Q4 2022. Based on the NG's disbursement report,[12] this was due to lower disbursements for maintenance and other operating expenditures (MOOE), infrastructure and other capital outlays, and allotment to LGUs.

Similarly, overall exports contracted by 2.6 percent in Q4 2023 from a growth of 2.6 percent in Q3 2023 and 14.6 percent in Q4 2022. Goods exports fell by

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[11] From the NEDA Statement on the Q4 2023 Performance of the Philippine Economy. Retrieved from https://neda.gov.ph/statement-of-neda-secretary-arsenio-m-balisacan-on-the-2023-fourth-quarter-performance-of-the-philippine-economy/

[12] Based on latest available DBM report on NG Disbursement Performance as of November 2023. DBM Report on the National Government Disbursement Performance (November 2023). Retrieved from: https://www.dbm.gov.ph/index.php/reports/ng-disbursement-performance?view=article&id=1088&catid=201.

11.6 percent in Q4 2023, led by components/devices (semiconductors), control instrumentation, electronic data processing, office equipment, and consumer electronics.

Meanwhile, overall imports posted a 2.9 percent growth y-o-y, a turnaround from the 1.1-percent decline in Q3 2023 but lower from the 7.0 percent rate of expansion in Q4 2022. Imports of services continued to grow at double-digit rates at 21.0 percent in Q4 2023, owing to growth in travel, business services, and transport. Meanwhile, imports of goods declined y-o-y by 2.6 percent in Q4 2023 due to weaker growth in mineral fuels, lubricants and related materials, components/devices (semiconductors), other imports of goods, industrial machinery and equipment, and electronic data processing.

**Table 14. Gross Domestic Product by Expenditure Shares**
at constant 2018 prices; growth rate in percent

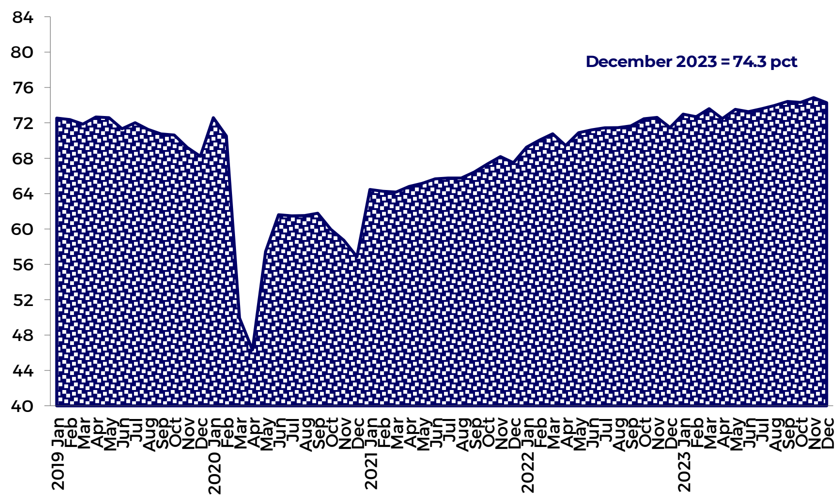
| Expenditure Shares | 2022 | 2023 | |
|---|---|---|---|
| | Q4 | Q3 | Q4 |
| Household Final Consumption Expenditure | 7.0 | 5.1 | 5.3 |
| Government Final Consumption Expenditure | 3.3 | 6.7 | -1.8 |
| Gross Capital Formation | 3.8 | -1.4 | 11.2 |
| Gross Fixed Capital Formation | 6.0 | 8.1 | 10.2 |
| Exports of Goods and Services | 14.6 | 2.6 | -2.6 |
| Imports of Goods and Services | 7.0 | -1.1 | 2.9 |

Source: PSA

## Other demand indicators

**Capacity utilization.** The manufacturing sector's preliminary average capacity utilization rate stood at 74.3 percent in December 2023, slightly lower than the revised month-ago level of 74.8 percent, based on the Philippine Statistics Authority's (PSA) Monthly Integrated Survey of Selected Industries (MISSI).

**Figure 10. Monthly Average of Capacity Utilization for Manufacturing**
(2018=100); in percent




Source: PSA

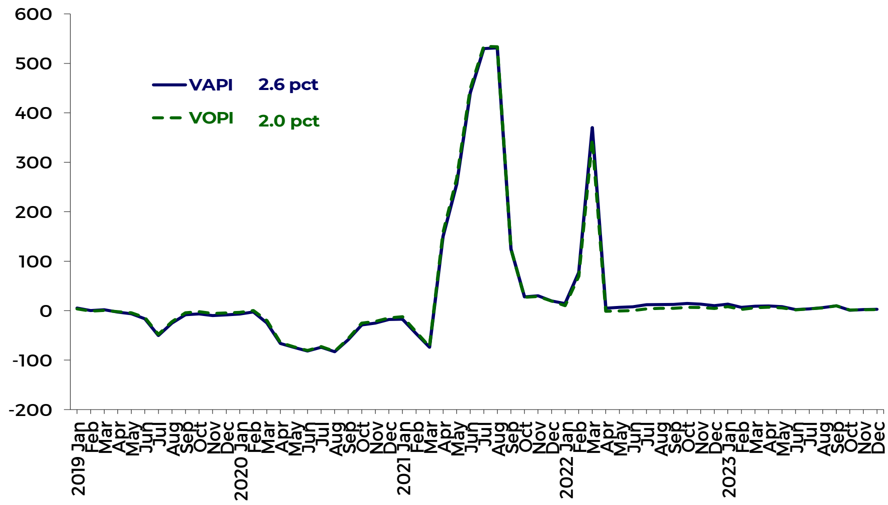
Of the 612 respondent-establishments surveyed by the PSA, 51.9 percent operated at or above the 80.0 percent capacity level in December 2023, an increase from the 49.8 percent recorded in November 2023. Based on preliminary numbers, the response rate of surveyed establishments rose to 69.4 percent (preliminary) in

December from 64.9 percent (preliminary) in November. The revised response rate for November was 76.8 percent.

Average capacity utilization eased but remained high in December 2023 as firms maintained factory capacity to support operations during the holiday period. Of the 22 major industries, only the manufacture of rubber and plastic products operated at 80 percent capacity level. Meanwhile, the remaining 21 industries operated above 60 percent, but below the 80 percent capacity range.

**Volume and value of production.** Preliminary results of the MISSI showed that factory output – as measured by the volume of production index (VoPI) – grew by 2.0 percent y-o-y in December 2023. This was faster than the 1.8-percent (revised) growth recorded in November 2023, but slower than the 4.5-percent growth in December 2022. Of the 22 subsectors, there were nine that posted y-o-y expansions, while the remaining 13 subsectors recorded contractions.

**Figure 11. Volume and Value Indices of Manufacturing Production**
2018=100; year-on-year in percent




Source: PSA

Similarly, the value of production index (VaPI) grew by 2.6 percent in December 2023, an improvement from the (revised) growth of 2.0 percent in November, but weaker than last year's double-digit expansion of 10.1 percent. Of the 22 sub-sectors, a total of nine subsectors posted y-o-y expansions, while the remaining 13 sub-sectors recorded contractions.

**Table 15. Growth in Volume of Production Index by Industry Division**
2018=100; year-on-year; in percent

| Gainers | Dec-23 |
|---|---|
| 1) Basic Pharmaceutical Products and Pharmaceutical Preparations | 38.2 |
| 2) Coke and Refined Petroluem Products | 38.1 |
| 3) Electrical Equipment | 30.8 |
| 4) Basic Metals | 20.8 |
| 5) Transport Equipment | 16.4 |
| 6) Textiles | 10.0 |
| 7) Furniture | 3.3 |
| 8) Paper and Paper Products | 2.8 |
| 9) Printing and Reproduction of Recorded Media | 1.3 |
| **Losers** | **Dec-23** |
| 1) Wood, Bamboo, Cane, Rattan Articles and Related Products | -55.3 |
| 2) Leather and Related Products, Including Footwear | -33.0 |
| 3) Machinery and Equipment Except Electrical | -17.8 |
| 4) Beverages | -16.5 |
| 5) Computer, Electronic and Optical Products | -16.5 |
| 6) Other Non-Metallic Mineral Products | -15.6 |
| 7) Fabricated Metal Products, except Machinery and Equipment | -12.0 |
| 8) Rubber and Plastic Products | -8.9 |
| 9) Wearing Apparel | -7.8 |
| 10) Chemical and Chemical Products | -2.8 |
| 11) Other Manufacturing and Repair and Installation of Machinery and Equipment | -2.3 |
| 12) Food Products | -1.4 |

Source: PSA

**Table 16. Growth in Value of Production Index by Industry Division**
2018=100; year-on-year; in percent

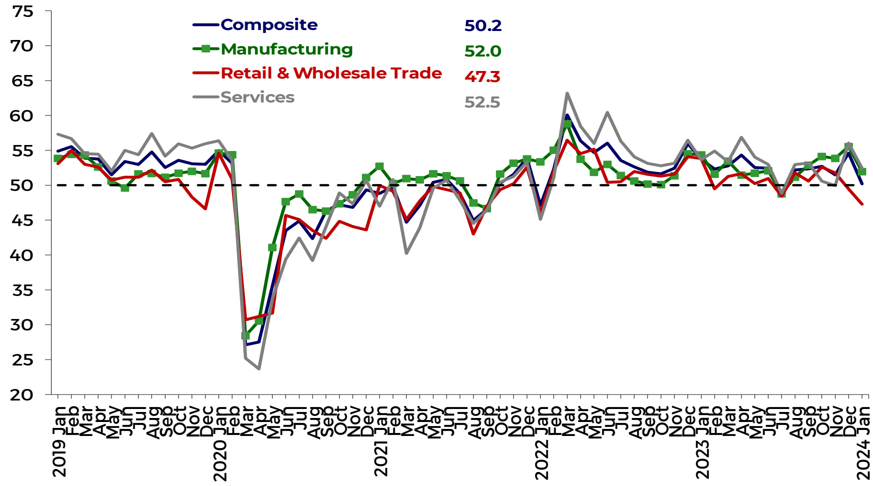
| Gainers | Dec-23 |
|---|---|
| 1) Basic Pharmaceutical Products and Pharmaceutical Preparations | 38.4 |
| 2) Coke and Refined Petroluem Products | 32.5 |
| 3) Electrical Equipment | 31.9 |
| 4) Basic Metals | 16.0 |
| 5) Transport Equipment | 11.8 |
| 6) Furniture | 3.5 |
| 7) Printing and Reproduction of Recorded Media | 2.2 |
| 8) Paper and Paper Products | 1.1 |
| **Losers** | **Dec-23** |
| 1) Wood, Bamboo,Cane, Rattan Articles and Related Products | -56.1 |
| 2) Leather and Related Products, Including Footwear | -31.2 |
| 3) Machinery and Equipment Except Electrical | -18.3 |
| 4) Other Non-Metallic Mineral Products | -17.6 |
| 5) Computer, Electronic and Optical Products | -13.4 |
| 6) Fabricated Metal Products, except Machinery and Equipment | -9.6 |
| 7) Wearing Apparel | -9.4 |
| 8) Chemical and Chemical Products | -9.2 |
| 9) Rubber and Plastic Products | -8.5 |
| 10) Beverages | -6.8 |
| 11) Other Manufacturing and Repair and Installation of Machinery and Equipment | -3.3 |
| 12) Tobacco Products | -3.1 |
| 13) Food Products | -0.8 |

Source: PSA

**Purchasing managers' index.**[13] The preliminary composite PMI in January 2024 stood at 50.2, lower than the previous month's PMI of 54.6 (revised), indicating a slower pace of expansion in economic activity.[14] Slower expansions in the services and manufacturing sectors, as well as faster contraction in the retail and wholesale sector weighed on overall growth. For the month ahead, retail and wholesale managers anticipate further slowdown for the sector. Meanwhile, economic conditions for the manufacturing and services sectors are expected to improve in February 2024.

[13] Data based on the monthly PMI report of the Philippine Institute for Supply Management (PISM).
[14] 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.

**Figure 12. Purchasing Managers' Index Diffusion Index**

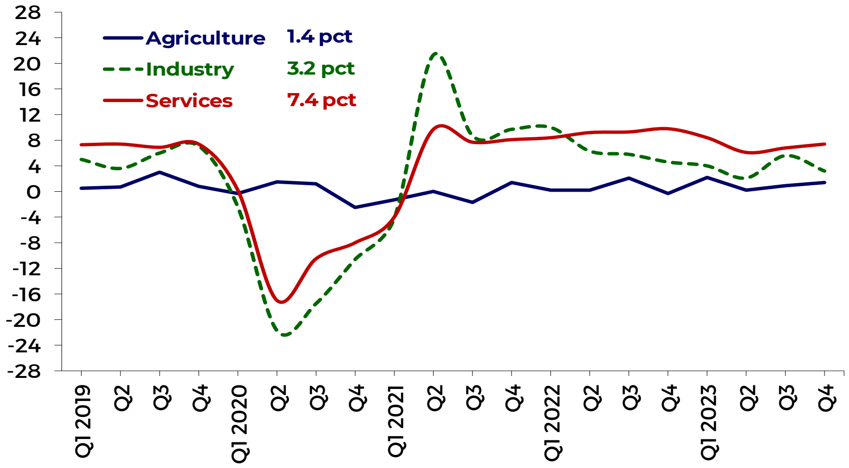



Source: Philippine Institute of Supply Management (PISM)

## 4. Supply Conditions

**Aggregate supply.** On the production side of the economy, output for most sectors has already rebounded to pre-pandemic levels, led by financial and insurance activities, transportation and storage, and information and communication, public administration and defense, among others.

**Figure 13. Gross Domestic Product by Industrial Origin**
at constant 2018 prices




Source: PSA

The services sector was the top contributor to Q4 2023 GDP growth, expanding by 7.4 percent in Q4 2023 as all its sub-industries increased during the quarter, with the growth in financial and insurance activities, particularly banking institutions, driving the bulk of the growth.

The agriculture sector's performance also improved, as output grew by 1.4 percent y-o-y in Q4 2023 after a 0.9-percent expansion in the previous quarter. This was mainly due to the higher output for poultry and egg production, support activities to agriculture, forestry and fishing (such as contract farming and post-harvest crop activities), livestock, other animal production,[15] sugarcane including muscovado

[15] Other animal production refers to sericulture (silkworm culture for the production of cocoon), apiary (bee culture for the production of honey), vermiculture, crocodile/alligator farming, rabbit

sugar-making in the farm, as well as mango, palay, pineapple, cacao, abaca, and tobacco.

By contrast, the industry sector decelerated in Q4 2023 at 3.2 percent compared to the expansions in the previous quarter and year of 5.6 percent and 4.6 percent, respectively. This can be traced mainly to the slower growth in construction, particularly government construction, and manufacturing activities.

**Table 17. Gross Domestic Product by Industrial Origin**
at constant 2018 prices; growth rate in percent

| Industrial Origin | 2022 | 2023 | |
|---|---|---|---|
| | Q4 | Q3 | Q4 |
| Agriculture, Forestry, and Fishing | -0.3 | 0.9 | 1.4 |
| Industry Sector | 4.6 | 5.6 | 3.2 |
| Mining and Quarrying | 1.8 | 5.1 | 10.3 |
| Manufacturing | 3.9 | 1.8 | 0.6 |
| Electricity, Steam, Water and Waste Management | 5.7 | 6.7 | 6.4 |
| Construction | 6.2 | 14.2 | 8.5 |
| Service Sector | 9.8 | 6.8 | 7.4 |
| Wholesale and Retail Trade and Repair of Motor Vehicles and Motorcycles | 8.8 | 4.9 | 5.2 |
| Transportation and Storage | 18.9 | 12.1 | 9.7 |
| Accomodation and Food Service Activities | 36.7 | 21.0 | 19.2 |
| Information and Communcation | 6.2 | 4.2 | 3.6 |
| Financial and Insurance Activities | 9.3 | 9.6 | 11.8 |
| Real Estate and Ownership of Dwellings | 7.4 | 4.2 | 3.9 |
| Professional and Business Services | 9.8 | 6.3 | 6.0 |
| Public Administration and Defense; Compulsory Social Security | 3.7 | 3.6 | 8.6 |
| Education | 10.0 | 6.4 | 7.9 |
| Human Health and Social Work Activities | 6.3 | 7.1 | 6.4 |
| Other Services | 18.6 | 15.9 | 11.9 |

Source: PSA

**Oil market developments.** The spot price of Dubai crude oil slightly increased in the first week of February 2024 compared to the full-month average price in January 2024. The rise in world oil prices was driven primarily by fears of possible supply disruptions due to the on-going geopolitical tensions in the Middle East; the continued disputes in the Red Sea; and Ukraine's attacks on Russian oil facilities. The uptick in oil prices was partly tempered by possible ceasefire between Israel and Hamas, as Hamas received a ceasefire proposal last 30 January 2024.

On the demand side, the worsening real estate situation in China,[16] as well as the continued contraction in Chinese manufacturing activity in January 2024 and high global interest rate environment also counterbalanced the increase in oil prices.

On the domestic front, domestic prices for gasoline and kerosene as of 30 January 2024 edged up week-on-week by ₱2.80 per liter and ₱0.45 per liter, respectively, while diesel price slid by ₱1.95 per liter.

**Developments in the agriculture sector.** The Agriculture, Forestry, and Fishing (AFF) posted a growth of 1.4 percent in Q4 2023, faster than the 0.9-percent growth in Q3 2023, and a reversal of the 0.3-percent contraction in Q4 2022.[17]

farming, raising of semi-domesticated or wild animals including birds, reptiles, insects (e.g., butterfly) and turtles, raising and breeding of cats and dogs, and game propagation and breeding activities.
[16] A Hong Kong court ordered the liquidation of Chinese property giant Evergrande Group.
[17] Based on the Q4 2023 National Accounts report published by the Philippine Statistics Authority on 31 January 2024.

Cumulative growth of the AFF sector was recorded at 1.2 percent for 2023, higher than the 2022 outturn of 0.5 percent. The higher AFF output in Q4 2023 was attributed mainly to the positive contribution of poultry, egg, livestock, other animal production, sugarcane, and support activities to AFF, which more than compensated for the lower output in fishing and aquaculture, corn, coconut, rubber, cassava, and other agricultural crops production.

Crop production, which contributed more than half (58.7 percent) of the total value of production in agriculture and fisheries, increased by 0.1 percent in Q4 2023,[18] a reversal of the 0.2-percent contraction in Q3 2023 and decrease of 1.0 percent in the previous year. Government support through productivity-enhancing programs and input subsidies, as well as more favorable weather conditions have contributed to improved crop production this year. Despite lower production, onion prices have also remained stable due to the arrival of sufficient imports to meet demand in Q4 2023.

Likewise, Q4 2023 livestock and poultry production, which accounted for 14.6 percent and 13.7 percent of total agricultural output, increased by 2.7 percent and 7.8 percent, respectively. The hog industry gradually recovered despite the continuous threat of African Swine Fever. As an alternative source of less expensive protein, chicken production is also improving as more integrators and big commercial players are expanding production.

Meanwhile, the fisheries sector, which comprised 13.0 percent of total value of production in agriculture and fisheries, recorded a contraction of 5.2 percent in Q4 2023. The government underscores the need to upgrade and expedite the development of more aquaculture farms and mariculture parks to support the fisheries sub-sector.

**Global food prices.** The FAO All Rice Price Index[19] averaged 142.8 points in January 2024, higher by 1.2 percent from 141.1 points in December 2023 and up by 13.0 percent from 126.4 points in the previous year. The m-o-m increase was primarily attributed to the strong export demand for Thai rice overseas, particularly, Indonesia. Meanwhile, the price of Vietnam 5% broken rice eased due mainly to currency depreciation and subdued demand.

As of January 2024, quotes for 5% broken rice varieties from Vietnam, Thailand, and Pakistan increased by 41.2 percent, 28.1 percent, and 33.6 percent, respectively.

The FAO Food Price Index (FPI) declined to 118.0 points in January 2024, relative to the previous month and year levels of 120.8 points and 131.6 points, respectively. The benchmark for world food commodity prices fell in January, weighed down by ample supplies of cereals, particularly wheat and maize.

[18] The growth rates of the subsectors and commodities are based on the October to December 2023 Performance of Philippine Agriculture report published by the Philippine Statistics Authority on 30 January 2023.
[19] The FAO All Rice Price Index is based on 21 rice export quotations. These quotations are combined into four groups consisting of Indica, Aromatic, Japonica, and Glutinous rice varieties.

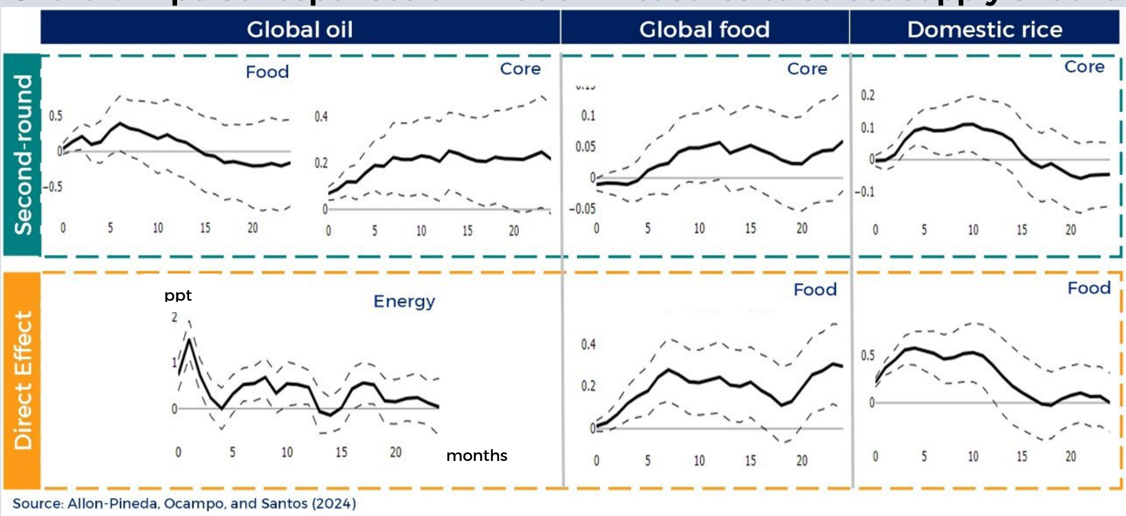
## Box article no. 2: Second-round effects of supply shocks on inflation[1]

The Philippines experienced successive supply shocks from 2021 to 2023 which exerted significant upward pressures on inflation. Given the large swings in oil and food prices, assessing the inflation outlook requires an understanding of how these price changes affect domestic inflation including the indirect or so-called second-round effects. The standard view is that monetary policy should look through transitory supply shocks if there are no observed second-round effects due to the lags in monetary policy transmission. However, looking through supply shocks in the presence of second-round effects may not be optimal since the central bank can bring inflation closer to the target with a corresponding policy response (Bandera et al., 2023).

This note estimates the direct and second-round effects of shocks to global oil, global food, and domestic rice prices on various measures of inflation as well as inflation expectations for the Philippines.[2] In the case of oil price shocks, the direct effect is defined as the impact on energy inflation, while the second-round effect is the weighted impact on core and food inflation. Meanwhile, for food shocks, the direct effect refers to the impact on food inflation, while the second-round effect reflects as the impact of the shock on core inflation. In addition, we examine whether there is some asymmetry in the pass-through of a price increase vis-à-vis a price reduction on headline, core, and inflation expectations.

### *Oil and rice price shocks have significant and persistent second-round effects*

**Chart 1. Impulse responses of inflation measures to select supply shocks**



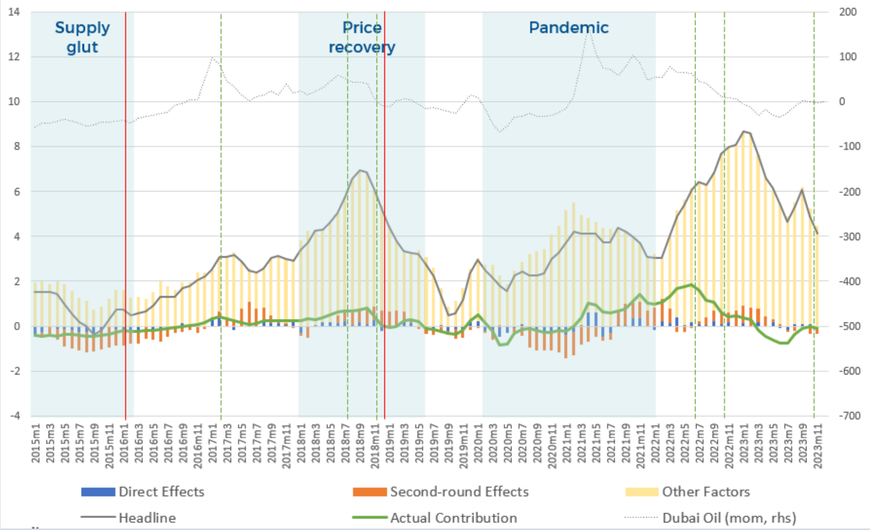
Source: Allon-Pineda, Ocampo, and Santos (2024)

Chart 1 shows the impulse responses of core, food, and energy to oil and food price shocks. The first column suggests that a 10-percent increase in Dubai crude oil prices leads to second-round effects that are smaller than the direct effects but are longer-lasting. This combined impact on core and non-core food inflation builds and persists for 18 months and, at its peak, reaches 0.28 ppt on the 13th month. The combined direct and second-round effects of global oil price shocks on headline inflation last for a year and reach a peak of 0.40 ppt on the 11th month, consistent with the findings of Alp, Klepacz, Saxena (2023) and Choi et. al. (2018) for advanced economies.

Looking at the second column, a one percent increase in global food inflation is found to have a significant and persistent direct impact on non-core food inflation but minimal second-round effects with the impact on core inflation being insignificant over the horizon. The weak pass-through may be attributed to the global food price index not being able to adequately capture domestic price movements. For instance, rice prices comprise only 2.2 percent of the food basket in the IMF's index, compared to the 8.9 percent share in the domestic CPI, suggesting that the former may not be representative of the latter. By contrast, the impact of a one percent increase in domestic rice prices leads to significant second-round effects that appear by the third month and persist for a year with a peak of 0.11 ppt on the 10th month. The significant indirect effect as well as the larger direct effect is due to the importance of rice in the Filipino food basket.

***Second-round effects of oil price shocks outweigh their direct effects***

**Chart 2. Historical decomposition of the impact of oil price shocks**

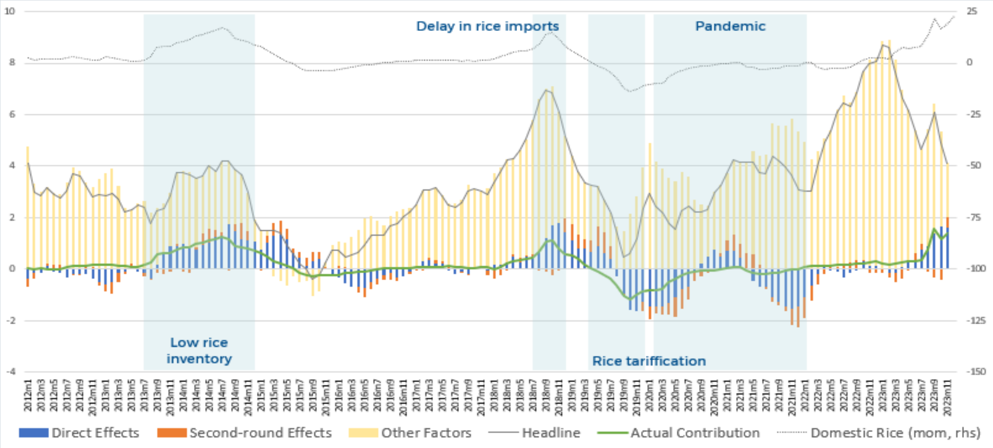



*Note: -- upward PUJ fare adjustments; — downward PUJ fare adjustments*
*Source: BSP staff estimates*

Chart 2 decomposes headline inflation into the impact of historical oil price shocks. Second-round effects appear to outweigh the contribution of direct effects to headline inflation since oil serves as an intermediate input to the production of other goods and services. Gasoline and diesel prices account for only 2.4 percent of the CPI basket while items affected by higher oil prices such as transport services have higher CPI weights. When matched with known oil shock episodes, negative second-round effects are observed a few months into the global oil supply glut of 2014-2015, the start of the pandemic in 2020, and two of the four times when public utility jeepney (PUJ) fares went down. Meanwhile, positive second-round effects appeared during the global oil price recovery in 2018 as well as in six of the eight times when PUJ fares increased. To further validate the estimates, the direct effects of oil price shocks on headline inflation are observed to align with the actual changes in Dubai crude oil prices and the actual contribution of gasoline and diesel prices.

## *Direct effects of domestic rice price shocks larger than second-round effects*

**Chart 3. Historical decomposition of the impact of rice price shocks**

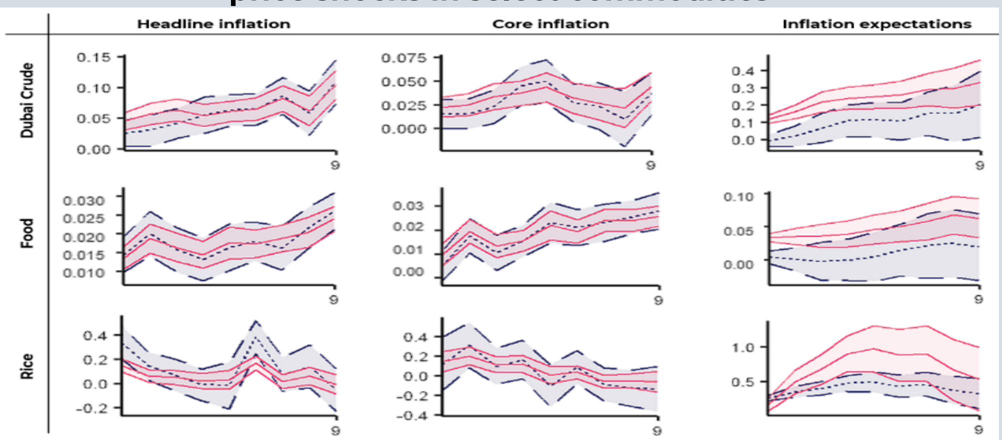



*Source: BSP staff estimates*

Compared with the impact of oil price shocks, the impact of domestic rice price shocks has larger direct effects on headline inflation relative to the contribution of second-round effects (Chart 3). Moreover, the estimated direct effects of rice price shocks on headline inflation are aligned with the actual contribution of rice prices. The larger direct impact can be attributed to the significant share of rice in the CPI basket and its limited role in the production of other goods and services. When matched with known rice price shock episodes, positive direct and second-round effects are observed in the latter part of the low rice inventory episode in 2013-2014[3] and the delays in rice imports in late 2018. Meanwhile, negative direct and second-round effects appeared months following the enactment of the rice tariffication law and continued well into the pandemic.

## *Price shocks tend to induce an asymmetric response to inflation expectations*

**Chart 4. Impulse response functions of inflation to price shocks in select commodities**




*Note: Red lines indicate positive price shocks on commodities, while blue lines indicate negative price shocks. To facilitate direct comparison, we flip the signs of the impulse response functions of a negative price shock. All results are reported using 95 percent confidence intervals based on robust standard errors.*

Chart 4 shows the impulse responses of headline inflation, core inflation, and inflation expectations to both positive and negative supply shocks coming from domestic rice, global food, and Dubai crude oil prices.[4] Given the overlap in the confidence intervals seen in the first two columns, there appears to be no asymmetry, in terms of magnitude and speed, in the inflationary response to positive or negative price shocks to both headline and core inflation.

However, looking at the third column, inflation expectations, as measured by the month-ahead inflation forecasts of professional analysts, appear to respond asymmetrically towards price shocks coming from global food and Dubai crude oil. Comparing shocks of the same magnitude, positive price shocks tend to raise inflation expectations more than negative price shocks tend to decrease inflation expectations. Additionally, the median response of inflation expectations towards a positive price shock tends to be slightly higher, possibly indicating that expectations are stickier in the face of downward price adjustments. In the case of domestic rice price shocks, positive price shocks trigger an increase in inflation expectations that is more dispersed, possibly indicating higher uncertainty.

**Endnotes**:

1/ The authors of this box article are Joan Christine Allon-Pineda, Jan Christopher Ocampo, and Eduard Renzo Santos of the Department of Economic Research. A full version of this study will be forthcoming in the BSP Discussion Paper Series.

2/ As suggested in Alp, Klepacz & Saxena (2023), we measure the impact and duration of the second-round effects of key price shocks on domestic inflation using a local projections approach. As an extension from the said reference note which only looked at oil price shocks, the estimations in this paper also consider global food and domestic rice price shocks, as well as the impact of such shocks on inflation expectations. Headline inflation is also historically decomposed into the direct and indirect contributions of each selected shock using the estimation technique outlined in Benigno et. al. (2022).

3/ Typhoon Haiyan and government actions against agri smugglers and hoarders led to low rice inventories in 2013-2014.

4/ The impulse response functions are derived using a state-based local projections model, with the “state” being an upward or downward adjustment in the shock variables.

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## Box article no. 3: Constructing a Philippine Supply Pressure Index[1]

### *Background of the Study*

Global Supply Chains (GSCs) faced supply disruptions in 2020 and 2021 as pandemic-related lockdowns hindered businesses operating in emerging market economies (EMEs) from meeting the recovering demand in advanced economies (AEs). Multiple waves of COVID-19 infections led to the repeated imposition of pandemic-related restrictions, which in turn delayed the production schedule of manufacturers and limited the operational capacity of critical logistics facilities (ILO, 2020 and Twinn, Qureshi, Conde, & Rojas, 2020).[2,3] While certain pandemic-related disruptions began to ease as economies relaxed quarantine restrictions towards the end of 2021, the escalation of geopolitical tensions in Eastern Europe and the Middle East, along with adverse weather disturbances, further exacerbated and prolonged the supply shocks initially caused by the pandemic. Consequently, this led to a reduction in the availability of raw materials, food commodities, and manufactured goods which contributed to broadened price pressures that affected AEs just as acutely as EMEs. Governments found themselves compelled to implement non-monetary interventions to address the shortfall in supply, while central banks tightened financial conditions to anchor inflation expectations and prevent second-round effects from taking root in their respective economies.

In the Philippines, the resulting shortages and subsequent increase in input prices reverberated throughout domestic industries as the backward linkages of firms to GSCs created mechanisms in transmitting global supply shocks into domestic prices (de Soyres & Franco, 2019).[4] Accordingly, the BSP has since expanded its surveillance toolkit to monitor supply-related risks that could potentially impact the formation of inflation expectations. However, available indicators at the time failed to provide a comprehensive overview of supply chain-related developments, and this prompted the BSP to develop an indicator that can quantitatively assess the supply-side pressures impacting the domestic economy.

The Philippines Supply Chain Pressure Index (PSPI) serves as an additional surveillance tool for the BSP to estimate the impact of supply-related shocks on domestic prices, second-round effects, and inflation expectations. It offers a systematic approach to analyzing supply chain dynamics by breaking down shocks into components that can be easily monitored and assessed by technical staff. Integrating the PSPI into the BSP's analytical framework will enhance the institution's capacity to monitor developments that pose risks to the inflation outlook, thereby strengthening its ability to fulfill its primary mandate of maintaining price stability.

### *Data and Methodology*

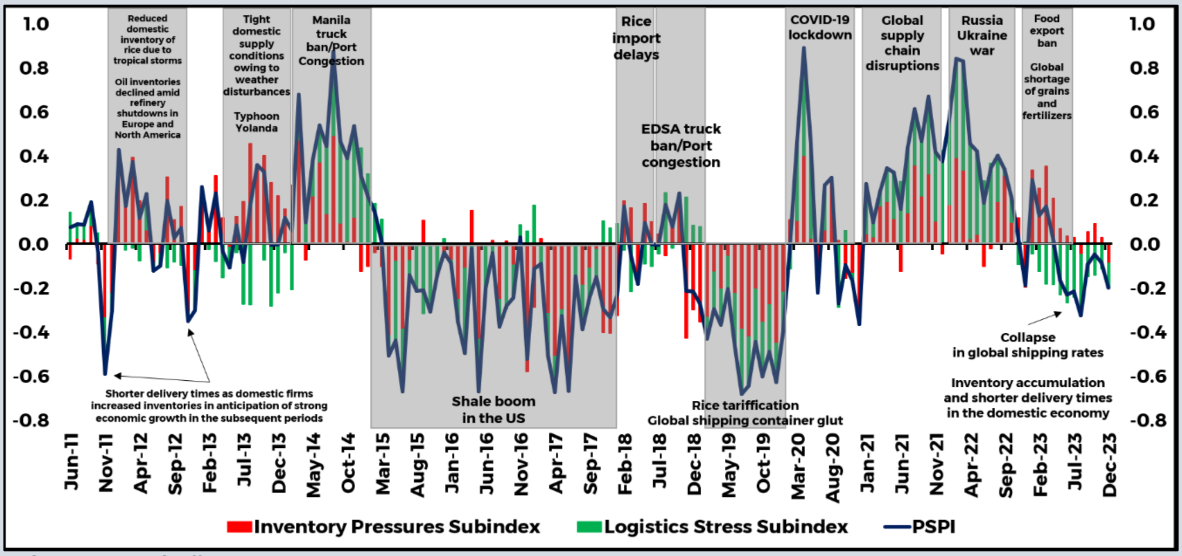
To ensure that the PSPI adequately reflects supply shocks commonly experienced by small open economies such as the Philippines, the BSP has integrated global and domestic supply indicators into the index's structure. These indicators include inventory PMIs, domestic supply of select food commodities, global oil inventory, and world food prices. In addition, logistics indicators have been included to capture how transport disruptions affect the cost of moving goods across domestic industries and GSCs. These indicators include supplier delivery PMIs, the Baltic Dry Index, timecharter averages of clean and dirty tankers as published by the Baltic Exchange, the Drewry World Container index, and Drewry air freight rates.

The construction of the PSPI begins by obtaining residuals after regressing all indicators on the contemporaneous and lagged values of global as well as domestic new order PMIs. This process is intended to remove as many demand factors as possible from the identified indicators. In theory, the residuals should solely reflect the non-demand effects of the identified index components (Benigno, di Giovanni, Groen, & Noble, 2022).[5] Subsequently, the obtained residuals are winsorized[6] to reduce the effect of spurious outliers that could disproportionately affect the statistical analysis. The winsorized indicators are then standardized to ensure that all indicators are scaled uniformly. Without standardization, variables with larger variances would disproportionately influence the principal components, potentially biasing the results. Following this, the index was created by calculating the corresponding weight of each component through principal component analysis.[7]

### *Preliminary Estimates and Potential Applications of the PSPI*

As shown in Chart 1, preliminary estimates of the PSPI have effectively captured notable events that precipitated supply-related shocks in the domestic economy. These events include tight domestic supply conditions resulting from weather disturbances and typhoon Yolanda in 2013; the imposition of a truck ban in Manila and ensuing port congestion in 2014; elevated crude oil inventory from 2015 to 2017 following the US shale boom; the delay of rice imports in 2018; and the impact of the rice tariffication law on domestic grains inventory in 2019. Additionally, the PSPI reflected the disruptions caused by COVID-19 lockdowns in 2020, global supply chain disruptions in 2021, Russia's invasion of Ukraine starting in 2022, and the food export bans implemented by several countries amid a global shortage of fertilizers in 2023.

**Chart 1. Preliminary Estimates of the Philippine Supply Pressure Index (PSPI), June 2011 – December 2023**




*Source: DER Staff Estimates*

To enhance the analysis of the current study and capitalize on the potential applications of the new indicator, the BSP will develop econometric models to quantitatively assess the impact of supply shocks—as measured by the PSPI—on key macroeconomic variables such as domestic prices, second-round effects, and inflation expectations, among others. Furthermore, the BSP intends to extend the PSPI to include supply pressures emanating from the service sector, including labor shortages resulting from demographic shifts and migration.

**Endnotes:**

1/ The author of this box article is Justin Jerome G. Valle of the Department of Economic Research. A full version of this study will be forthcoming.

2/ ILO. (2020). *The effects of COVID 19 on trade and global supply chains*. International Labour Organization.

3/ Twinn, I., Qureshi, N., Conde, M., & Rojas, D. (2020). *The Impact of COVID-19 on Logistics*. International Finance Corporation - World Bank Group.

4/ De Soyres, F., & Franco, S. (2019). *Inflation Dynamics and Global Value Chains*. World Bank.

5/ Benigno, G., di Giovanni, J., Groen, J., & Noble, A. (2022). *A New Barometer of Global Supply Chain Pressur*es. New York: Federal Reserve Bank of New York (FRBNY).

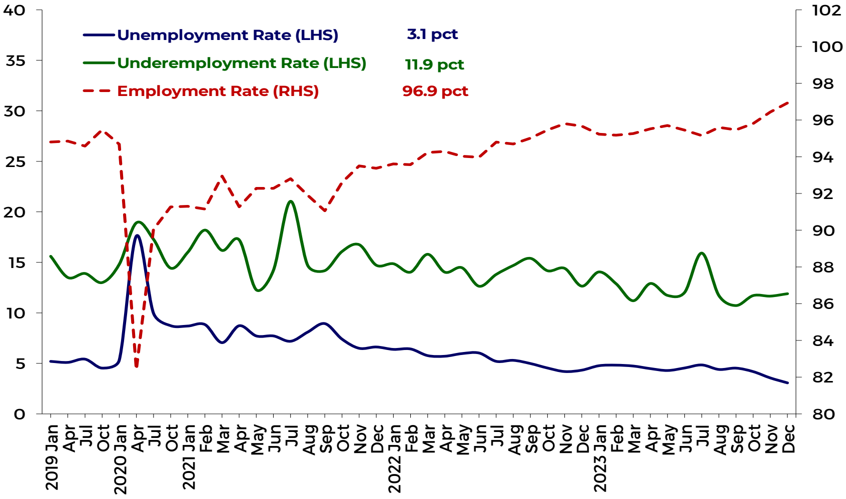
6/ The bottom and top 5 percent (outliers) with the 5th and 95th percentiles, respectively. This is commonly referred to as 90 percent winsorization.

7/ In essence, Principal Component Analysis is a statistical technique that measures the significance of pre-selected variables in determining the principal components of the index. It offers the benefit of evaluating the individual importance of the indicators used, ensuring that each receives a weight consistent with its historical relevance to changes in the index. A notable advantage of this method is that the more correlated a component is with the other indicators, the greater its assigned weight becomes. Therefore, a slight change in a heavily weighted component holds more significance in capturing variations within the index than a sizeable fluctuation of a component with minimal weight. (See: Smith, L. I. (2002). *A tutorial on Principal Components Analysis*. University of Otago. and Holland, S. M. (2019). *Principal Components Analysis (PCA)*. R.)

## 5. Labor Market Conditions

The unemployment rate fell to 3.1 percent in December 2023 from 3.6 percent in November 2023 and 4.3 percent in December 2022. The unemployment rate in December translated to about 1.60 million unemployed Filipinos during the month, lower compared to 1.83 million in the previous month. The unemployment rate was also the lowest since it peaked at 17.6 percent at the onset of the pandemic in April 2020.

**Figure 14. Labor Market Indicators**
in percent




Source: PSA

However, underemployment rate was slightly higher at 11.9 percent in December 2023 from 11.7 percent in November due mainly to an increase in visible underemployment rate.[20] Nevertheless, the latest underemployment rate was an improvement from the 12.6-percent record in December 2022. The December 2023 underemployment corresponded to about 6.01 million underemployed Filipinos.

### Wage developments

Following the minimum wage review across the regions amid the continued elevated inflation environment, fifteen (15) regional wage boards have approved new wage orders in their respective jurisdictions since January 2023. Regions X (Northern Mindanao) and XIII (CARAGA) have approved adjustments in January 2024. The average increase in the non-agriculture industry minimum wage is 8.6 percent for the 15 regions and 8.7 percent for areas outside the National Capital Region.

[20] Visibly underemployed persons are those who worked for less than 40 hours a week during the survey period and want additional hours of work or an additional job.

## 6. Monetary Operations

As of 31 January 2024, the total outstanding amount absorbed in the BSP liquidity facilities stood at about ₱1.72 trillion. The bulk of the BSP's monetary operations to absorb excess liquidity had been conducted through the BSP Securities facility (BSP-SF), comprising about 45.27 percent (or about ₱778.27 billion). Placements in the term deposit facility (TDF) made up 23.17 percent of total placements (or around ₱398.35 billion), while for the daily instruments, the overnight reverse repurchase (ON RRP) facility and the overnight deposit facility composed 21.23 percent (or around ₱365 billion) and 10.32 percent (or around ₱177.41 billion), respectively, of the total placements.

During the 31 January 2024 TDF auction, the weighted average interest rate (WAIR) for the 7-day TDF rose slightly to 6.5871 percent from the 6.5847 percent fetched during the 24 January 2024 TDF auction. Meanwhile, the WAIR for the 14-day TDF fell marginally to 6.6106 percent from the 6.6187 percent during the previous auction.

During the BSP Bill (BSPB) auction on 2 February 2024, the WAIR for the 28-day BSPB rose slightly to 6.7726 percent from the 6.7703 percent fetched during the 26 January 2024 BSPB auction. Meanwhile, the WAIR for the 56-day BSPB went down to 6.7693 percent from the 6.7740 percent during the previous auction.

The auction results for the TDF and the BSPB during the review period reflected how eligible counterparties managed their asset and liquidity positions as they tended to client requirements during the holiday season. There has also been a noted preference for the 56-day BSPB.

For the daily RRP auction[21], the average bid-to-cover ratio (BCR) for the period 31 January-6 February 2024 was at 0.97x, higher than the BCR of 0.90x for the period 24-30 January 2024.

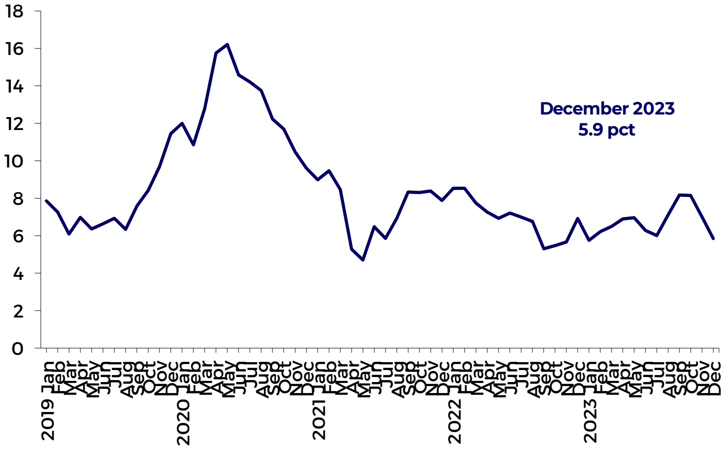
[21] Beginning 8 September 2023, the BSP shifted to a variable-rate format for the RRP facility.

## 7. Financial Conditions

**Domestic liquidity.** Preliminary data showed that domestic liquidity (M3) grew by 5.9 percent y-o-y to about ₱17.4 trillion in December from 7.0 percent in November. On a m-o-m seasonally adjusted basis, M3 increased by about 0.4 percent.

Domestic claims continued to drive the expansion in M3, as claims on the private sector grew with the sustained expansion in bank lending to non-financial private corporations and households. Net claims on the central government also rose with the decrease in deposits by the national government with the BSP.

**Figure 15. Domestic Liquidity**
year-on-year growth rate; in percent

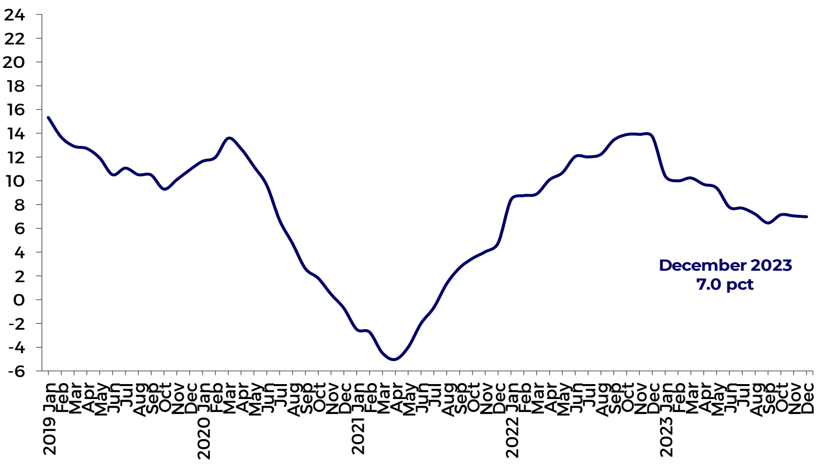



Source: BSP

On the liabilities side, the growth in M3 was driven mainly by the expansion in time deposits.

**Bank lending.** Preliminary data indicated that outstanding loans of universal and commercial banks (U/KBs), net of reverse repurchase (RRP) placements with the BSP, grew by 7.0 percent y-o-y in December 2023, the same rate of increase as in November 2023. On a m-o-m seasonally adjusted basis, outstanding universal and commercial bank loans, net of RRPs, increased by 0.3 percent.

**Figure 16. Loans Outstanding of Commercial Banks**
**year-on-year growth rate; in percent**




Source: BSP

Meanwhile, outstanding loans to residents, net of RRPs, went up by 7.3 percent in December from 7.4 percent in the previous month, while outstanding loans to non-residents[22] decreased by 2.8 percent in December from a decline of 5.0 percent in November. Outstanding loans for production activities rose by 5.5 percent in December from 5.7 percent in November, driven largely by the expansion in lending to key industries such as real estate activities (10.9 percent); wholesale and retail trade, and repair of motor vehicles and motorcycles (7.2 percent); and electricity, gas, steam, and air-conditioning supply (6.2 percent).

Likewise, consumer loans to residents increased by 23.5 percent in December from 23.6 percent in November, due to the faster increase in motor vehicle loans and salary-based general purpose consumption loans.

## Credit Standards

Respondents see unchanged credit standards for enterprises over the next quarter using the modal approach. Loan demand from businesses is also expected to be broadly steady based on the same approach.

**Lending to enterprises.** Based on the modal approach, results for Q4 2023 indicated that a majority of the participant banks (88.0 percent) maintained credit standards for businesses. Meanwhile, the DI approach showed a net tightening of overall credit standards[23] across all borrower firm sizes due to banks' lower risk tolerance, deterioration of borrowers' profiles and profitability of banks' portfolios, along with stricter financial system regulations.

Over the next quarter, both the modal and DI methods indicated respondents' expectations of generally unchanged credit standards for enterprises amid banks' sustained tolerance for risk and stable outlook for the overall economy as well as for industries and firms, along with the steady profiles of borrowers.

### Table 18. General Credit Standards for Loans to Enterprises (Overall)

| | 2021 | | | | 2022 | | | | 2023 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Tightened considerably | 10.6 | 8.0 | 4.2 | 4.2 | 10.0 | 6.5 | 10.4 | 4.3 | 6.7 | 4.3 | 2.1 | 0.0 |
| Tightened somewhat | 14.9 | 20.0 | 20.8 | 14.6 | 16.0 | 13.0 | 8.3 | 12.8 | 13.3 | 4.3 | 10.6 | 12.0 |
| **Remained basically unchanged** | **66.0** | **70.0** | **70.8** | **75.0** | **72.0** | **76.1** | **77.1** | **80.9** | **73.3** | **89.1** | **80.9** | **88.0** |
| Eased somewhat | 8.5 | 2.0 | 4.2 | 6.3 | 2.0 | 4.3 | 4.2 | 2.1 | 6.7 | 2.2 | 6.4 | 0.0 |
| Eased considerably | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 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 | 100.0 | 100.0 | 100.0 | 100.0 |
| **Diffusion index for credit standards** | **17.0** | **26.0** | **20.8** | **12.5** | **24.0** | **15.2** | **14.6** | **14.9** | **13.3** | **6.5** | **6.4** | **12.0** |
| **Number of banks responding** | **47** | **50** | **48** | **48** | **50** | **46** | **48** | **47** | **45** | **46** | **47** | **50** |

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

[22] Outstanding loans to non-residents include loans by UKB's foreign currency deposit units (FCDUs) to non-residents.
[23] The net tightening of credit standards for business loans in Q4 2023 is reflected in the stricter collateral requirements and loan covenants, and more use of interest rate floors.

**Lending to households.** The majority of the surveyed banks (70.6 percent) retained their lending standards for household loans in Q4 2023. On the other hand, DI-based results pointed to net easing credit standards for consumer loans[24] mainly associated with the improvement in profitability of banks' portfolios, higher risk tolerance, and less uncertain economic outlook.

**Table 19. General Credit Standards for Loans to Households (Overall)**

| | 2021 | | | | 2022 | | | | 2023 | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Tightened considerably | 9.4 | 5.7 | 5.6 | 2.9 | 2.5 | 5.4 | 5.4 | 5.7 | 3.0 | 3.0 | 0.0 | 0.0 |
| Tightened somewhat | 9.4 | 20.0 | 11.1 | 8.6 | 12.5 | 5.4 | 10.8 | 8.6 | 18.2 | 9.1 | 15.6 | 11.8 |
| **Remained basically unchanged** | **75.0** | **68.6** | **69.4** | **65.7** | **62.5** | **73.0** | **64.9** | **71.4** | **51.5** | **69.7** | **68.8** | **70.6** |
| Eased somewhat | 6.3 | 5.7 | 13.9 | 17.1 | 17.5 | 13.5 | 18.9 | 14.3 | 27.3 | 12.1 | 12.5 | 14.7 |
| Eased considerably | 0.0 | 0.0 | 0.0 | 5.7 | 5.0 | 2.7 | 0.0 | 0.0 | 0.0 | 6.1 | 3.1 | 2.9 |
| Total | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| **Diffusion index for credit standards** | **12.5** | **20.0** | **2.8** | **-11.4** | **-7.5** | **-5.4** | **-2.7** | **0.0** | **-6.1** | **-6.1** | **0.0** | **-5.9** |
| **Number of banks responding** | **32** | **35** | **36** | **35** | **40** | **37** | **37** | **35** | **33** | **33** | **32** | **34** |

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

For Q1 2024, modal results showed a higher number of bank respondents anticipating maintained loan standards for households, while the DI approach indicated a continued net easing of credit standards driven by banks' expectations of improved profitability of their portfolios, higher risk tolerance, and more favorable economic outlook.

**Loan demand.** In Q4 2023, survey results pointed to generally steady demand for credit from businesses (66.0 percent) and consumers (56.3 percent) based on the modal method. Meanwhile, the DI approach showed a net increase in loan demand from across all firm classifications driven by bank clients' more optimistic economic outlook, increased customer inventory financing and accounts receivable needs, including lack of other sources of funds. On the other hand, DI-based results pointed to net easing credit standards for consumer loans[25] mainly associated with the improvement in profitability of banks' portfolios, higher risk tolerance, and less uncertain economic outlook.

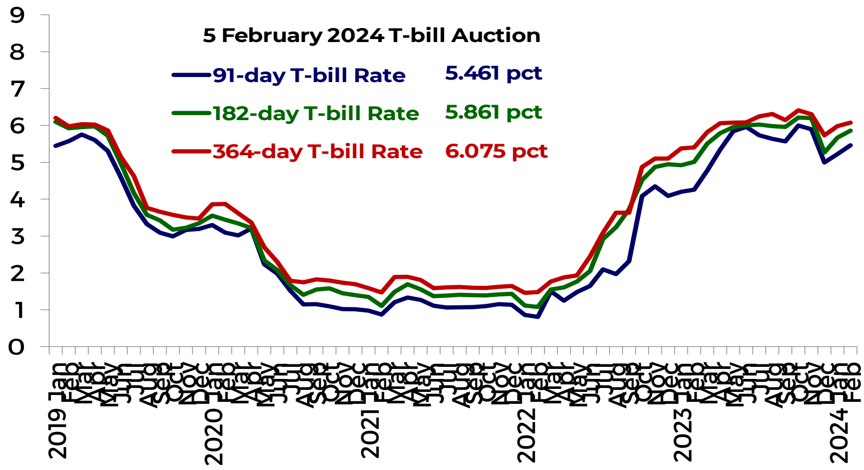
In the next quarter, most of the respondent banks expect broadly steady loan demand from businesses, while about half of the respondent banks expect higher demand for credit from households. Based on the DI method, participating banks anticipate a net rise in credit demand from businesses, driven by customers' more positive economic prospects along with higher customer inventory financing and accounts receivable needs. The DI approach also pointed to a net increase in consumer loan demand driven by expectations of higher household consumption and housing investment, banks' more attractive financing terms, and lower income prospects.

[24] In particular, the DI approach reflected a net easing of loan standards for housing and credit card loans, while there was a net tightening of loan standards for personal/salary loans. Meanwhile, credit standards for auto loans were steady.
[25] In particular, the DI approach reflected a net easing of loan standards for housing and credit card loans, while there was a net tightening of loan standards for personal/salary loans. Meanwhile, credit standards for auto loans were steady.

## Capital markets

**Primary GS market and rates.** During the 5 February 2024 Treasury bill (T-bill) auction, the average interest rates for the 91-day and 182-day rose by 6.3 basis points (bps) to 5.461 percent and 5.1 bps to 5.861 percent, respectively. Meanwhile, the average interest rate for the 364-day T-bills decreased marginally by 0.1 bp to 6.075 percent from the rate fetched during the 29 February 2024 auction.

**Figure 17. Treasury Bill Rates**
in percent



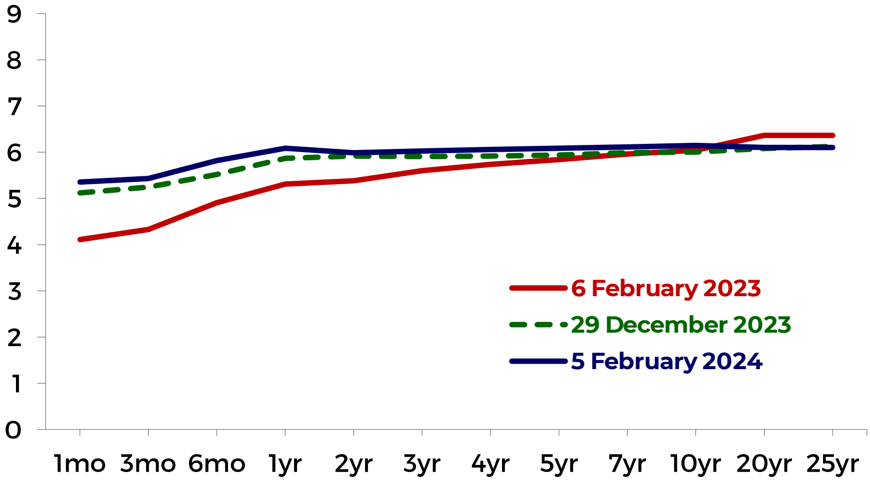

Source: BTr

The Bureau of the Treasury (BTr) Auction Committee awarded in full the offered amounts of ₱5.0 billion each for the 91-day, 182-day, and 364-day T-bills. Total tenders for all maturities reached about ₱47.4 billion, or about 3.2 times the ₱15.0-billion total amount offered.

On 30 January 2024, the BTr fully awarded ₱30 billion as planned of the re-issued 3-year T-bonds with a remaining life of 2 years and 11 months. The said T-bond fetched an average interest rate of 6.007 percent, higher than the 5.9-percent average interest rate quoted for the same paper when it was last awarded on 3 January 2024. The auction was oversubscribed with tenders reaching around ₱62.4 billion or 2.1 times the offered amount of ₱30 billion.

**Secondary market GS yield curve.** On 5 February 2024, secondary market GS yields increased generally relative to end-December 2023 amid market players' cautious sentiment due to mixed signals from prospects of delayed monetary policy rate cuts from the US Fed and the BSP, and the robust GDP report for Q4 2023. The rise in GS interest rates was also supported by the anticipation of an announcement of a retail Treasury bond this month and ahead of the release of the January 2024 Philippine inflation data on 6 February 2024. Consequently, the generally negative spreads in secondary market rates over the BSP overnight RRP rate on 5 February 2024 were generally narrower relative to end-December 2023 levels.

**Figure 18. Yields of Government Securities in the Secondary Market**
in percent

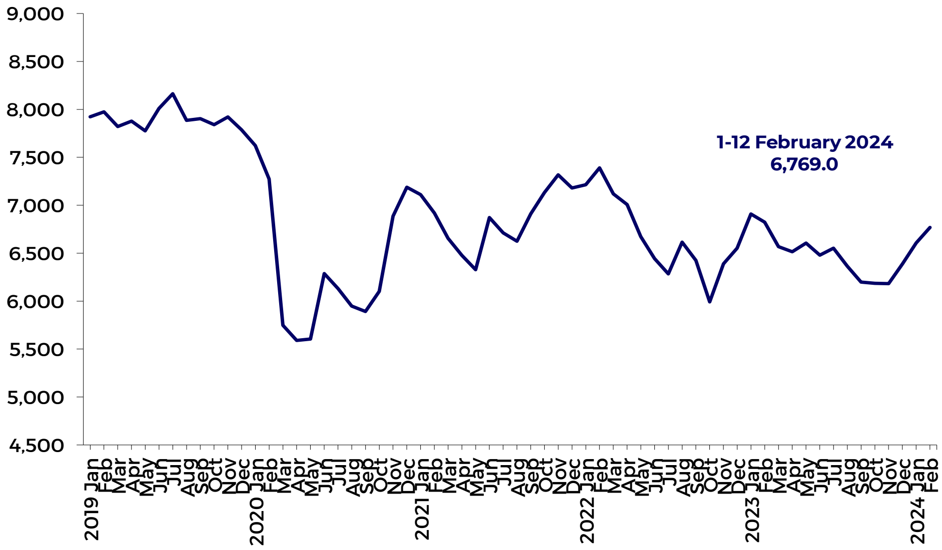



Source: Bloomberg

As of 5 February 2024, the spreads between the 10-year and 1-year GS rates and the 10-year and 5-year GS rates narrowed to 5.9 bps (from 13.4 bps as of end-December 2023) and to 5.8 bps (from 6.3 bps as of end-December 2023), as a result of the larger increase in the 1-year and 5-year GS rates relative to the rise in the 10-year GS rate.

**Stock market.** The Philippine Stock Exchange index (PSEi) averaged at 6,769.0 index points for the period 1-12 February 2024, supported by positive market sentiment amid slower January 2024 inflation and higher-than-expected Q4 2023 GDP. The PSEi was also buoyed by improved GDP outlook by the IMF.[26] On a year-to-date (y-t-d) basis, the PSEi also closed higher by 5.5 percent at 6,807.8 index points on 12 February 2024.

**Figure 19. Philippine Stock Exchange Index**
index points

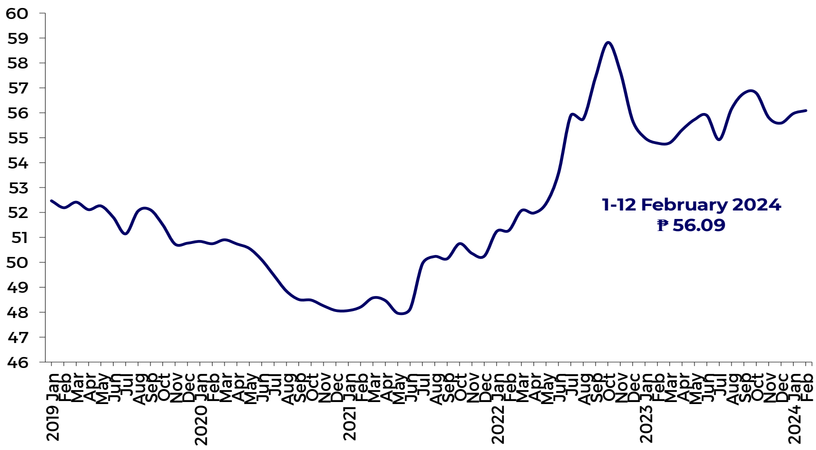



Source: Philippine Stock Exchange, BSP

[26] The IMF revised the GDP growth projection to 6.0 percent for 2024 in its January 2024 World Economic Outlook (WEO), slightly higher from the October WEO forecast of 5.9 percent. Source: IMF

**Exchange rate**. For the period 1-12 February, the peso has averaged ₱56.09/US$1, depreciating further by 0.13 percent relative to the previous month's average. This downward trend reflected partly broad US dollar strength amid expectations of delay in the US Fed's policy easing following stronger-than-expected US jobs data and cautious remarks from US Fed officials,[27] as well as lingering geopolitical tensions in Gaza and the Middle East. On the domestic front, dampened market sentiment amid elevated inflation outlook in Q2 2024, and lower GIR in January[28] contributed to the depreciation of the peso. Nonetheless, these factors were partly offset by the following positive domestic developments: i) robust economic growth prospects in 2024 following the release of stronger-than-expected Q4 and full-year 2023 Gross Domestic Product (GDP) growth;[29] ii) hawkish rhetoric from the BSP despite further easing of inflation in January; iii) sustained growth in the country's manufacturing activity in January;[30] iv) lower government debt-to-GDP ratio in 2023;[31] and v) stronger net FDI inflows in November 2023.[32] As of 12 February, the peso closed at ₱56.01/US$1, depreciating by 1.13 percent against the US dollar, y-t-d, from the end-December 2023 closing rate of ₱55.37/US$.[33]

**Figure 20. Peso-Dollar Rate**
PHP/US$




Source: Reference Exchange Rate Bulletin, Treasury Department, BSP

On a real trade-weighted basis, the peso lost external price competitiveness in January (y-o-y) against the basket of currencies of all trading partners (TPI), trading partners in advanced (TPI-A) and developing (TPI-D) countries as indicated by the increase in the Real Effective Exchange Rate (REER) index of the peso by 3.06

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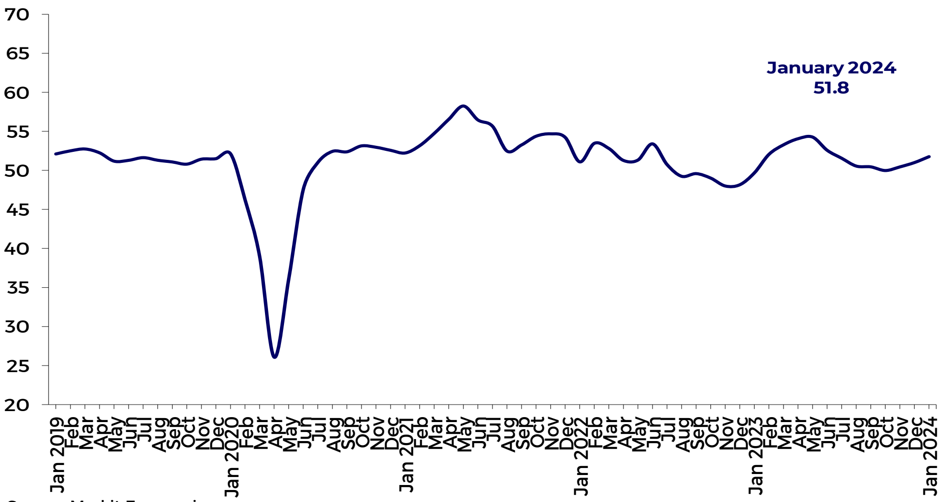
27 The US Fed decided to keep its policy rate unchanged for the fourth consecutive time during the latest FOMC meeting on 31 January-1 February 2024. Chairman Jerome Powell reiterated that the US Fed will require more inflation data to confirm that inflation is easing toward the 2 percent target in a sustainable way before considering rate cuts. (Reuters)
28 Based on preliminary data, the country's GIR level settled at US$103.4 billion as of end-January 2024 from the end-December 2023 level of US$103.8 billion.
29 With the country's 2023 GDP settling below the government's target, Fitch Solutions expects the economy's resilience to persist in 2024, raising its growth forecast to 6.2 percent. (Manila Standard)
30 Purchasing Managers' Index (PMI) settled at 50.9 points in January, a 5-month consecutive growth, albeit lower than the 51.5 points posted in December 2023. (S&P Global)
31 The National Government's outstanding debt-to-GDP ratio declined to 60.2 percent in 2023 relative to the 60.9 percent in the previous year. It is also lower than the 61.2-percent Medium-Term Fiscal Framework government target. (Bureau of the Treasury)
32 FDI net inflows rose by 27.8 percent to reach US$1.0 billion in November 2023 from the US$820 million net inflows recorded in November 2022.
33 Based on the last done deal transaction in the afternoon.

percent, 2.07 percent, and 3.56 percent, respectively, traced mainly to the combined impact of widening inflation differential and nominal appreciation of the peso.[34,35]

## 8. External Developments

Global economic activity improved as output and new orders grew at faster rates. In December 2023, the JP Morgan All-Industry Output Index increased, with the fastest rates of expansion seen in the BRIC nations of Brazil, Russia, India, and China, along with the UK. Expansions were also recorded in the US, Japan, Italy, and Spain. Meanwhile, France, Canada, Germany, and Australia were among the countries which posted contractions.[36]

**Figure 21. JP Morgan Global All-Industry Output Index**
index points




Source: Markit Economics

In the January 2024 WEO, the IMF raised its 2024 global economic growth projection to 3.1 percent, reflecting the greater-than-expected resilience in the US and several large emerging market and developing economies (EMDEs), as well as fiscal support in China. Nonetheless, global economic expansion is expected to remain well below the annual average of 3.8 percent until[37] at least 2025 with elevated central bank policy rates to fight inflation, a withdrawal of fiscal support

[34] The Trading Partners Index (TPI) measures the nominal and real effective exchange rates of the peso across the currencies of 14 major trading partners 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-Advanced (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-Developing (TPI-D) measures the effective exchange rates of the peso across 10 currencies of partner developing countries which includes China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.
[35] 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.
[36] JP Morgan Global Composite PMI, https://www.pmi.spglobal.com/. A diffusion index is calculated for each survey variable. The index is the sum of the percentage of 'higher' responses and half the percentage of 'unchanged' responses. The indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease.
[37] Historical average global growth from 2000 – 2019

and high debt weighing on economic activity, as well as low underlying productivity growth.

For advanced economies (AEs), the IMF 2024 baseline growth estimate slightly declined amid stronger-than-expected US momentum and weaker-than-expected growth in the euro area. Meanwhile, the 2024 growth forecast for emerging markets and developing economies (EMDEs) was unchanged at 4.1 percent for 2024 and expected to rise to 4.2 percent in 2025 with regional differences. The higher forecasts for emerging and developing Europe, Middle East and Central Asia, and sub-Saharan Africa were offset by the lower estimates for emerging and developing Asia, and Latin America and the Caribbean.

With the likelihood of a hard landing receding as adverse supply shocks unwind, the risks to the global outlook are broadly balanced. The IMF cited the following upside risks to the revised baseline growth forecasts: (1) faster disinflation; (2) slower-than-assumed withdrawal of fiscal support; (3) faster economic recovery in China; and (4) artificial intelligence and supply-side reforms. Meanwhile, the following downside risks to global growth remain plausible: (1) commodity price spikes amid geopolitical and weather shocks; (2) persistence of core inflation, requiring a tighter monetary policy stance; (3) faltering of growth in China; and (4) disruptive turn to fiscal consolidation.

**Policy actions by other central banks.** Among the central banks regularly monitored by the BSP, Bank of Korea, Bank Indonesia, People's Bank of China, Bank of Japan, Bank Negara Malaysia, Bank of Canada, European Central Bank, US Federal Reserve, Bank of England, and Reserve Bank of Australia maintained their respective key policy interest rates as they continued to assess the impact of previous monetary policy adjustments.

The *BSP Monetary Policy Report* is published four (4) times a year 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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