



**HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY  
STANCE HELD ON 10 MAY 2018<sup>1</sup>**

**I. Monetary Policy Decision**

The Monetary Board decided to:

- a) Increase the BSP's key policy interest rate by 25 basis points to 3.25 percent for the overnight RRP (borrowing) facility;
- b) Adjust the interest rates on the overnight deposit and overnight lending facilities accordingly.

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

- The Monetary Board's decision was based on its assessment that latest forecasts have further shifted higher, indicating that inflation pressures could become more broad-based over the policy horizon. While inflation momentum has started to slow down, inflation may still breach the inflation target range of 3.0 percent  $\pm$  1.0 percentage point for 2018 due primarily to temporary supply-side factors. Nevertheless, inflation is expected to return inside the target range in 2019. The Monetary Board assessed that the balance of risks to the inflation outlook continues to lean toward the upside, with price pressures emanating from possible adjustments in transport fares, utility rates, and wages.
- At the same time, the Monetary Board believed that a timely increase in the BSP's policy interest rate will help arrest potential second-round effects by tempering the buildup in inflation expectations. The Monetary Board observed that strong domestic demand allows some scope for a measured adjustment in the policy rate without adversely affecting the country's economic growth momentum. In assessing the stance of monetary policy, the Monetary Board also emphasized that it continues to closely monitor domestic macroeconomic conditions as well as the evolving global economic environment, including the potential impact of the ongoing normalization of monetary policy in some advanced economies.

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<sup>1</sup> The discussions herein reflect the assessment made by the Monetary Board based on a comprehensive set of economic information available at the time of the policy meeting. The highlights of the discussions during the 10 May 2018 monetary policy meeting were approved by the Monetary Board during its regular meeting held on \_\_ May 2018. The next meeting of the Monetary Board on the monetary policy stance is scheduled on 21 June 2018.

### III. Recent Developments and Inflation Outlook

The MB considered the following developments in deciding on the monetary policy stance:

#### A. Domestic price conditions

- In April, headline and core inflation rose further. The new 2012-based CPI series showed a higher headline inflation rate for April at 4.5 percent from 4.3 percent in March. This brought the year-to-date average to 4.1 percent, which is above the Government's inflation target of 2-4 percent for the year. Other indicators, such as the official core inflation, three of the alternative measures of core inflation estimated by the BSP, the number and weight of above-threshold items, as well as the diffusion index of price changes, also increased. However, the impact of the new tax appears to have mostly dissipated based on month-on-month trends while a majority of CPI items remains within or below the target range.

#### B. Inflation expectations

- Mean inflation forecasts of private analysts have stabilized, remaining elevated for 2018 but within target for 2019-2020. Results of the BSP's April 2018 survey of private sector economists showed steady mean inflation forecasts at 4.1 percent for 2018 based on the 2012-CPI series. Mean inflation forecasts were broadly steady and within the target range at 3.6 percent for 2019-2020.

#### C. Inflation outlook

- Compared with the previous forecast round, the latest baseline inflation forecasts for 2018 and 2019 were higher at 4.6 percent and 3.4 percent, respectively. The balance of risks to the baseline inflation path was judged to remain tilted toward the upside. Additional wage adjustments and transport fare hikes due to the increase in excise taxes on petroleum products, pending petitions for adjustments in jeepney fares and electricity rates, and faster-than-expected monetary policy normalization in the US were seen as the key upside risks to inflation. Meanwhile, the potential for slower global economic growth due to protectionist policies in advanced economies and geopolitical tensions, along with the proposed tariffication of quantitative restrictions (QR) on rice imports, continued to be the main downside risks to inflation.

Baseline Inflation Forecasts		
	2012-based CPI	
	22 Mar 2018 MB policy meeting	10 May 2018 MB policy meeting
2018	3.9	4.6
2019	3.0	3.4

#### D. Demand conditions

- Domestic demand continued to be firm, with GDP growth in the first quarter of 2018 coming in at 6.8 percent. Strong domestic demand fueled output growth, supported by household consumption, capital formation, and government spending. Growth momentum remained above the ten-year average and is consistent with the BSP's firm growth outlook over the policy horizon.

## **E. Supply-side indicators**

### Developments in Agriculture

- Domestic rice prices increased due to the end of the harvest season as well as to logistics and distribution issues. The Monetary Board noted the measures to address rising rice prices, including the “Tulong sa Bayan” project and NFA-approved rice importation scheme.
- The Monetary Board also discussed the progress of the proposed tariffication of QRs on rice imports. The bill is pending before the Senate Committee on Agriculture and Food. Staff analysis indicated that tariffication of rice imports could lower domestic rice prices.

### Wage Developments

- The Monetary Board noted that wage petitions have been filed in the NCR and Regions VI, VII, and XI as of 18 April 2018. Nevertheless, most of these wage petitions are in accordance with the rule that allows new wage petitions after the expiration of the 12-month period since the last wage order.

### Oil Price Developments

- Average crude oil prices are significantly higher in April 2018, with prices reaching US\$70 per barrel over rising geopolitical tensions in the Middle East and declining global oil inventories. Risks to near-term oil prices lean toward the upside with reinstated sanctions by the US against Iran, lower output from Venezuela, and rising OPEC compliance rate on production cuts. On the downside, US oil production has been rising consistent with industry expectations as oil prices continued to trend within the shale oil ‘sweet spot’ of US\$61-US\$65 per barrel. Expectations of higher US production are reflected in the oil futures prices which remained in backwardation.
- The Monetary Board noted the several fare hike petitions filed by the transport sectors (PUJ, PUB, UV express, airport taxis and TNVS). The hearings were scheduled in April and May 2018.

### Developments in the Utilities Sector

- The overall electricity rate increased in April 2018 due mainly to higher generation charges. The upward adjustment in power generation costs in April was primarily due to tighter supply conditions in the Luzon grid.

## **F. Financial market developments**

- The Philippine Stock Exchange index (PSEi) continued to consolidate on concerns over higher inflation and the looming trade row between the US and China. Foreign investors were net sellers from February to April. Meanwhile, the peso depreciated against the US dollar in April on risk aversion amid geopolitical tensions in the Middle East and the general strengthening of the dollar on the back of rising US Treasury yields.

## **G. Domestic liquidity and credit conditions**

- Available data continue to indicate ample liquidity in the financial system to support non-inflationary growth. Domestic liquidity growth accelerated to 14.4 percent while bank lending growth slowed down to 18.3 percent in March 2018. Meanwhile, total bids and placements through the BSP's open market operations (OMOs) as well as the weighted average accepted rates in the term deposit facility (TDF) increased in April relative to the previous month following the operational RR adjustment in March.

#### **H. Fiscal developments**

- The government's commitment to sustain implementation of the programmed infrastructure spending provided a boost to domestic activity. The National Government (NG) recorded a fiscal deficit of ₱51.5 billion for the first two months of 2018, more than double the previous year's deficit of ₱21.5 billion due to strong revenues and expenditure growth.

#### **I. External developments**

- The global economy is expected to sustain its broad-based recovery in 2018-2019. In its April 2018 World Economic Outlook (WEO), the IMF projected global economic output to expand by 3.9 percent in 2018 and 2019. The strength in the global economic outlook could be attributed to favorable market sentiment, accommodative financial conditions, and expansionary fiscal policy in the US, and the recovery in commodity prices. The IMF maintains its view that the risks to the growth outlook continue to be broadly balanced in the near term but remains skewed to the downside over the medium term.