BANGKO SENTRAL NG PILIPINAS

HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 17 NOVEMBER 2022 [1]

I. Monetary Policy Decision

The Monetary Board decided to:

a) Raise the BSP's current policy interest rate by 75 basis points to 5.00 percent for the overnight RRP rate; and

b) Increase the current interest rates on the overnight deposit facility (ODF) to 4.50 percent and overnight lending facility (OLF) to 5.50 percent.

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

- The latest baseline inflation projections indicate a higher inflation path over the policy horizon. Average inflation is projected to breach the upper end of the government's target band of 2-4 percent for 2022 and 2023. Nevertheless, inflation is projected to decelerate towards the midpoint of the target range in 2024 mainly on account of the lower domestic growth outlook as the impact of the cumulative monetary policy rate adjustments by the BSP manifests.

- Inflation remains high and broad-based. Core inflation rose sharply in October, indicating stronger pass-through of elevated food and energy prices as well as demand-side impulses on inflation.

- Moreover, inflation expectations for 2022 and 2023 have risen further above the upper end of the inflation target range.

- At the same time, the risks to the inflation outlook lean strongly toward the upside for 2022 and 2023 but are seen to remain broadly balanced for 2024.

- Given the increased likelihood of further second-round effects, persistent inflationary pressures, and the predominance of upside risks to the inflation outlook, aggressive monetary policy action is needed to safeguard price stability. With the strong growth of the economy in the third quarter of 2022, domestic demand is seen to hold firm owing to improved employment outturns, investment activity, and consumer spending. A sizeable adjustment in the policy interest rate will also help insulate the economy from external headwinds and exchange rate fluctuations that

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[1] The discussions herein reflect the assessment made by the Monetary Board based on a comprehensive set of macroeconomic and financial information available at the time of the policy meeting. The next meeting of the Monetary Board on the monetary policy stance is scheduled on 15 December 2022.

could further entrench price pressures and potentially dislodge inflation expectations.

- The Monetary Board is reassured by the timely non-monetary interventions by the National Government to mitigate the impact of persistent supply-side pressures on commodity prices, including those aimed at alleviating supply-side shortages and strengthening farm productivity.

III. Recent Developments and Inflation Outlook

The Monetary Board considered recent macroeconomic and financial developments in deciding the appropriate monetary policy stance:

A. Domestic price conditions

- Headline inflation increased further to 7.7 percent year-on-year in October 2022 from 6.9 percent in September 2022, the highest recorded rate since December 2008. The rise in inflation in October was primarily due to the higher inflation of food and non-alcoholic beverages, and restaurants and accommodation services. The resulting year-to-date average inflation of 5.4 percent is well above the government's average inflation target range of 2.0–4.0 percent for 2022.

- At the same time, core inflation rose to 5.9 percent in October 2022 from 5.0 percent in September 2022. The higher official core inflation reflects second-round effects from the approval of the fare increases for different public utility vehicles. Higher inflation for the heavily weighted restaurants and accommodation services also contributed to the rise in core inflation.

B. Inflation expectations

- Inflation expectations have also risen further and remain at risk of disanchoring. Private sector economists surveyed in November 2022 reported a higher mean inflation forecast for 2022 at 5.9 percent from 5.7 percent in the October 2022 survey.[2] Similarly, the mean inflation forecast for 2023 and 2024 increased to 4.9 percent (from 4.6 percent) and 4.0 percent (from 3.8 percent), respectively.

- Likewise, the results of the BSP's Q3 2022 survey of business and consumer expectation indicate that both sectors anticipate inflation to breach the upper end of the government's 2-4 percent target range for 2022 and 2023.

C. Inflation outlook

[2] There were 22 respondents in the BSP's survey of private sector economists in November 2022. The survey was conducted from 4 to 10 November 2022.

- Average inflation is projected to settle above the government's target range of 3.0 percent ± 1.0 ppt in 2022 and 2023, before decelerating towards the midpoint of the target range in 2024.

Baseline Inflation Forecasts		
	22 September 2022 MB Meeting	**17 November 2022 MB Meeting**
2022	5.6	5.8
2023	4.1	4.3
2024	3.0	3.1

- The upward revision in the forecasts for 2022 and 2023 was mainly driven by the higher-than-expected inflation outturn in October, the higher nowcast for November, the faster-than-expected GDP expansion in Q3 2022, and the continued depreciation of the peso, which were partly tempered by lower oil price assumptions. Meanwhile, the slight upward revision in the forecast for 2024 was due to the depreciation of the peso, whose impact is partly tempered by the lower domestic growth outlook.

- The risks to the inflation outlook over the policy horizon continue to skew strongly to the upside, particularly for 2023. Nonetheless, the risk to the outlook remains broadly balanced for 2024. The potential impact of higher fertilizer prices; trade restrictions and adverse global weather conditions on international food prices; increased prices of fruits and vegetables owing to domestic weather disturbances; petitions for tricycle fare hikes due to elevated oil prices; higher sugar prices; and the possible reinstatement of the full tariff rates on several imports such as pork and rice that were temporarily lowered under Executive Order No. 171 are the major upside risks to the inflation outlook. Meanwhile, the impact of a weaker-than-expected global recovery is the primary downside risk to the outlook.

D. Demand conditions

- Output growth in Q3 2022 was stronger than expected, driven by robust household spending as well as strong export performance despite inflationary pressures. The economy grew by 7.6 percent year-on-year in Q3 2022, faster than the 7.5-percent (revised) growth in Q2 2022 and the 7.0-percent growth in Q3 2021.

- The Philippine economy is projected to remain on the recovery path over the near term. BSP Staff forecasts indicate GDP growth settling within the DBCC's target of 6.5-7.5 percent for 2022 and below the 6.5-8.0 target for 2023 and 2024.[3] The full-year growth forecasts for 2022 and 2023 were higher than the previous projections due to the upward revisions in Q2 2022 GDP; the stronger-than-expected growth performance in Q3 2022; and the higher world growth assumption for 2022. Meanwhile, the forecast

[3] Government growth targets based on the 182nd Development Budget Coordination Committee (DBCC) Meeting on 8 July 2022.

for 2024 was lower compared to the previous forecasts, reflecting the slower global growth assumption as well as the impact of the BSP's monetary policy tightening.

- Mobility indicators across location categories have reverted to pre-pandemic levels beginning May 2022 based on their 7-day moving averages. Meanwhile, the implementation of full face-to-face classes by November 2022 is expected to increase overall mobility**.**

- Domestic labor market conditions further improved as the unemployment rate eased to 5.0 percent in September 2022 from 5.3 percent in January 2020 before the pandemic. Consequently, the 95.0-percent employment rate in September was its highest since the onset of the pandemic. Additionally, labor force participation rate continues to rise and has now exceeded pre-pandemic level.

E. Supply-side indicators

Developments in Agriculture

- Nationwide average retail rice prices showed mixed outturns in October 2022 based on the results of the 2018-based PSA Retail Price Survey covering all provinces and key cities in the country. Survey results for October were mixed as the start of the main harvest season resulted in generally lower rice prices in areas outside the National Capital Region, while the effects of Super Typhoon Karding led to increases in retail prices, especially in the National Capital Region.

- Domestic supply conditions continue to face challenges emanating from animal diseases, high production costs due to global supply disruptions, and additional uncertainties brought about by the Ukraine-Russia crisis. To cushion the impact of these challenges on the country's food security, the National Government has implemented crucial non-monetary measures to fill supply gaps and boost local production, such as rice imports to augment supply in the domestic market, the extension of lower tariff rates on pork imports, and the relaxation of quantitative import restrictions for sugar processors over the near-term, among others. On a longer-term basis, non-government measures for food security and sustainability include restructuring the food value chain from research and development up to retail, and promotion of urban aquaculture and agriculture as well as unconventional production systems, among others.

- Based on the latest assessment of weather conditions as of 13 October 2022, prevailing La Niña conditions will likely persist through February 2023, and transition to ENSO-neutral by February-March-April 2023. Nonetheless, La Niña event is associated with above normal rainfall conditions, which could improve availability of water supply in harvest areas and potentially enhance agricultural production, particularly during the dry season.

Oil Price Developments

- Global oil prices have remained volatile as concerns over tight supply conditions were weighed against weaker global growth prospects. Dubai crude oil prices have generally been decreasing from July to October 2022 amid concerns over weaker economic outlook given monetary policy tightening of central banks and China's zero-tolerance policy on COVID-19. However, crude oil prices increased in early November on expectations of tighter supply due to lower output arising from OPEC+ sanctions on Russia and the group's announcement to cut production beginning in November. Meanwhile, the futures market remained in backwardation as of 7 November 2022.

- Domestic pump prices of petroleum products remain significantly higher relative to end-2021 levels even with the recent rollback of kerosene and diesel prices. Amid elevated domestic oil prices, there remain pending petitions from two public transport groups to increase fares by ₱1 peso per kilometer and implement surge pricing.

Developments in the Utilities Sector

- Electricity rate increased in November 2022 due mainly to higher generation charges. According to MERALCO, the upward adjustment in generation charges was on the back of the increase in charges from Power Supply Agreements (PSAs) because of the scheduled maintenance outage of First Natgas-San Gabriel plant.

- Meanwhile, the increase in charges from PSAs was partly offset by the decreases in charges from the Independent Power Producers (IPPs) and Wholesale Electricity Spot Market (WESM). IPP charges declined mainly owing to the appreciation of the peso against the US dollar, as well as the reduction of usage of more expensive alternative fuel by First Gas-Sta. Rita. WESM charges also decreased with fewer instances of the secondary price cap imposition.

F. Financial market developments

- On a year-to-date basis, the peso depreciated against the US dollar by 10.9 percent to close at ₱57.21/US$1 on 15 November 2022 from the 31 December 2021 closing rate of ₱51.00/US$1. The peso's depreciation reflected the market's expectations of sustained monetary tightening from the US Federal Reserve. Nonetheless, the depreciation of the peso was partially tempered by the BSP statement that it will raise its policy interest rate by 75 bps at its 17 November meeting.

- The Philippine Stock Exchange Index (PSEi) averaged 6,272.2 index points for the period 1-16 November 2022, higher by 4.7 percent from its October average of 5,992.7 index points. The positive performance of the PSEi can be attributed to improved investor sentiment owing largely to the faster-than-expected Q3 2022 GDP growth and sustained reports of positive corporate earnings. Likewise, contributing to the positive investor sentiment was the 3.1 percent year-on-year increase in cash remittances for the period January to September 2022.

G. Domestic liquidity and credit conditions

- Domestic liquidity and credit remain adequate to support bank lending and broad-based economic recovery. Preliminary data show that M3 grew by 5.0 percent year-on-year in September 2022 from 6.7 percent (revised) in August 2022. Nonetheless, preliminary data on outstanding loans of universal and commercial banks for both production and consumption activities increased by 13.0 percent in September (from 12.1 percent in August) and 20.5 percent (from 18.3 in the previous month), respectively.

- Yields of secondary market government securities rose across all tenors on 15 November 2022 relative to end-October 2022 yields, ranging from 13.2 basis points (bps) to 51.4 bps. The increase in yields was due to the record-high October 2022 inflation outturn and strong Q3 2022 GDP data which raised the prospect of further policy rate hikes from the BSP.

H. Fiscal developments

- The National Government (NG) recorded a deficit of ₱833.0 billion for January - August 2022 which is 13.1 percent lower than recorded in the same period in 2021. Excluding the interest payments in NG expenditures, the primary deficit amounted to ₱492.9 billion, 26.1 percent lower than the amount recorded in 2021. Revenues increased by 18.1 percent to ₱2,368.6 billion in January – August 2022 from ₱2,005.7 billion in the same period in 2021.

I. External developments

- The global economy is in the midst of a general slowdown amid weaker economic activity in the US, euro area and China as well as elevated global inflation impulses. Global factory output and services revenues declined in October 2022 amid slower activity in major economies. In its October 2022 World Economic Outlook report, the International Monetary Fund (IMF) retained its growth forecast for 2022 but reduced its projection for 2023, as waning pandemic-related fiscal support and increasingly restrictive financial conditions further dampened the global economy's recovery momentum.

- Global financial conditions have quickly tightened amid central banks' aggressive monetary policy tightening. Several central banks have raised their respective key policy rates in November to address persistent and broadening price pressures as well as to anchor inflation expectations.