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INFLATION REPORT

Q3 2019

Bangko Sentral ng Pilipinas

Foreword

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

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

The government's target for annual headline inflation under the inflation targeting framework has been set at 3.0 percent ± 1.0 percentage point (ppt) for 2019-2022 by the Development Budget Coordination Committee. This is consistent with the desired disinflation path over the medium term, favorable trends in inflation dynamics, and expected higher capacity of the economy for growth under a low inflation environment.

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

The Monetary Board approved this Inflation Report at its meeting on 17 October 2019.

BENJAMIN E. DIOKNO
Governor

The Monetary Policy of the Bangko Sentral ng Pilipinas

The BSP Mandate

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

Monetary Policy Instruments

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

Policy Target

The BSP's target for monetary policy uses the Consumer Price Index (CPI) or headline inflation rate, which is compiled and released to the public by the Philippine Statistics Authority (PSA). The policy target is set by the Development Budget Coordination Committee (DBCC)[2] in consultation with the BSP. The inflation target for 2018-2020 is 3.0 percent ± 1.0 ppt.[3]

BSP's Explanation Clauses

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

[1] The TDF was introduced under the interest rate corridor system which was implemented on 3 June 2016.
[2] The DBCC, created under Executive Order No. 232 dated 14 May 1970, is an inter-agency committee tasked primarily to formulate the National Government's fiscal program. It is composed of the Office of the President (OP), Department of Budget and Management (DBM), National Economic and Development Authority (NEDA), and the Department of Finance (DOF). The BSP attends the Committee meetings as a resource agency.
[3] The DBCC, in coordination with the BSP, through DBCC Resolution No. 2019-1 dated 26 February 2019, decided to keep the inflation target at 3.0 percent ± 1.0 percentage point for 2019 – 2020 and to set the inflation target at 3.0 percent ± 1.0 percentage point for 2021 – 2022.

The Monetary Board

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

Chairman & Governor
Benjamin E. Diokno

Members
Carlos G. Dominguez III
Felipe M. Medalla
Juan D. De Zuñiga, Jr.
Peter B. Favila
Antonio S. Abacan, Jr.
V. Bruce J. Tolentino

The Advisory Committee

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

Chairman
Benjamin E. Diokno
Governor

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

Ma. Cyd Tuaño-Amador
Deputy Governor
Corporate Services Sector

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Senior Assistant Governor
Financial Market Operations Sub-Sector

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

Iluminada T. Sicat
Assistant Governor
Monetary Policy Sub-sector

2019 SCHEDULE OF MONETARY POLICY MEETINGS, INFLATION REPORT PRESS CONFERENCE AND PUBLICATION OF MB HIGHLIGHTS

2019	Advisory Committee (AC) Meeting	Monetary Board (MB) Meeting	MB Highlights Publication	Inflation Report (IR) Press Conference
Jan			10 (Thu) (13 Dec 2018 MB meeting)	18 (Fri) (Q4 2018 IR)
Feb	1 (Fri) (AC Meeting No. 1)	7 (Thu) (MB Meeting No. 1)		
Mar	15 (Fri) (AC Meeting No. 2)	21 (Thu) (MB Meeting No. 2)	7 (Thu) (7 Feb 2019 MB meeting)	
Apr			17 (Wed) (21 Mar 2019 MB meeting)	26 (Fri) (Q1 2019 IR)
May	3 (Fri) (AC Meeting No. 3)	9 (Thu) (MB Meeting No. 3)		
Jun	14 (Fri) (AC Meeting No. 4)	20 (Thu) (MB Meeting No. 4)	6 (Thu) (9 May 2019 MB meeting)	
Jul			18 (Thu) (20 Jun 2019 MB meeting)	19 (Fri) (Q2 2019 IR)
Aug	2 (Fri) (AC Meeting No. 5)	8 (Thu) (MB Meeting No. 5)		
Sep	20 (Fri) (AC Meeting No. 6)	26 (Thu) (MB Meeting No. 6)	5 (Thu) (8 Aug 2019 MB meeting)	
Oct			24 (Thu) (26 Sep 2019 MB meeting)	25 (Fri) (Q3 2019 IR)
Nov	8 (Fri) (AC Meeting No. 7)	14 (Thu) (MB Meeting No. 7)		
Dec	6 (Fri) (AC Meeting No. 8)	12 (Thu) (MB Meeting No. 8)	12 (Thu) (14 Nov 2019 MB meeting)	

List of Acronyms, Abbreviations, and Symbols

ASF	African Swine Fever
AHFF	Agriculture, Hunting, Forestry and Fishing
AONCR	Areas Outside the National Capital Region
APP	Asset Purchase Programme
BAP	Bankers Association of the Philippines
BES	Business Expectations Survey
BI	Bank Indonesia
BIR	Bureau of Internal Revenue
BIS	Bank for International Settlements
BNM	Bank Negara Malaysia
BOC	Bureau of Customs
BOE	Bank of England
BOJ	Bank of Japan
BOT	Bank of Thailand
bp	Basis Point
BPO	Business Process Outsourcing
BTr	Bureau of the Treasury
CALABARZON	Cavite, Laguna, Batangas, Rizal and Quezon
CAMPI	Chamber of Automotive Manufacturers of the Philippines, Inc.
CAR	Capital Adequacy Ratio
CBD	Central Business District
CDS	Credit Default Swap
CES	Consumer Expectations Survey
CI	Confidence Index
CPI	Consumer Price Index
DAR	Department of Agriculture
DBCC	Development Budget Coordination Committee
DBM	Department of Budget and Management
DepED	Department of Education
DI	Diffusion Index
DOE	Department of Energy
DOF	Department of Finance
ECB	European Central Bank
EIA	Energy Information Administration
EMBIG	Emerging Market Bond Index Global
ERC	Energy Regulatory Commission
FCD	Foreign Currency Deposit
FDI	Foreign Direct Investment
FOMC	Federal Open Market Committee
GDP	Gross Domestic Product
GIR	Gross International Reserve
GNI	Gross National Income
GNPL	Gross Non-Performing Loan
GOUR	Generation Over/Under Recovery
GS	Government Securities
IEA	International Energy Agency
IMF	International Monetary Fund
IMTS	International Merchandise Trade Statistics
kWh	Kilowatt Hour
LEM	Loans Especially Mentioned
LFS	Labor Force Survey
LSOUR	Lifeline Subsidy Over/Under Recovery
MB	Monetary Board
mb/d	Million Barrels per Day
MERALCO	Manila Electric Company
MISSI	Monthly Integrated Survey of Selected Industries
MTP	Major Trading Partner

NBQBs	Non-Banks with Quasi-Banking Function
NCR	National Capital Region
NEDA	National Economic and Development Authority
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NG	National Government
NGCP	National Grid Corporation of the Philippines
NIA	National Income Accounts
NNPL	Net Non-Performing Loans
NPC	National Power Corporation
NSFR	Net Stable Funding Ratio
ODF	Overnight Deposit Facility
OP	Office of the President
OPEC	Organization of the Petroleum Exporting Countries
OPR	Overnight Policy Rate
PBOC	People's Bank of China
PISM	Philippine Institute for Supply Management
PMI	Purchasing Managers' Index
ppt	Percentage Point
PSA	Philippine Statistics Authority; Power Supply Agreement
PSALM	Power Sector Assets and Liabilities Management
PSEi	Philippine Stock Exchange Index
QBs	Quasi-Banks
q-o-q	Quarter-on-Quarter
RBA	Reserve Bank of Australia
RBI	Reserve Bank of India
RBNZ	Reserve Bank of New Zealand
RBs	Rural Banks
REER	Real Effective Exchange Rate
RP	Repurchase
RR	Reserve Requirement
RREL	Residential Real Estate Loan
RREPI	Residential Real Estate Price Index
RRP	Reverse Repurchase
RRR	Reserve Requirement Ratio
SBL	Substandard or Below Loan
SDA	Special Deposit Account
SEC	Securities and Exchange Commission
SLOS	Senior Bank Loan Officers' Survey
SLOUR	System Loss Over/Under Recovery
SME	Small and Medium Enterprise
TAFPPC	True-up Adjustments of Fuel and Purchased Power Cost
TAFxA	True-up Adjustments of Foreign Exchange Related Costs
TBs	Thrift Banks
TDF	Term Deposit Facility
TLP	Total Loan Portfolio
TOUR	Transmission Over/Under Recovery
TPI	Trading Partner Index
TPI-A	Trading Partner Index in Advanced Countries
TPI-D	Trading Partner Index in Developing Countries
U/KBs	Universal and Commercial Banks
VaPI	Value of Production Index
VoPI	Volume of Production Index
WEO	World Economic Outlook
WESM	Wholesale Electricity Spot Market
y-o-y	Year-on-Year
y-t-d	Year-to-Date

Contents

Overview

Headline inflation edges lower. Headline inflation rate declined further to 1.7 percent year-on-year (y-o-y) in Q3 2019 from 3.0 percent in the previous quarter, with lower food inflation accounting for the bulk of the decline. This brought the year-to-date (y-t-d) average to 2.8 percent y-o-y in 2019, which is well within the National Government's (NG) announced target range of 3.0 percent ± 1.0 percentage point (ppt) for the year.

Headline inflation edges lower in Q3 but y-t-d inflation remains within target

Likewise, core inflation—which excludes selected volatile food and energy items to measure underlying price pressures—also slowed down to 2.9 percent y-o-y in Q3 2019 from 3.4 percent in the previous quarter. Meanwhile, most of the BSP-computed alternative core inflation measures also eased in Q3 2019 relative to the previous quarter except for net of volatile items. Consistent with the downtrend in overall inflation, the number of CPI items with inflation rates higher than the threshold of 4.0 percent (the upper end of the 2019 inflation target) also fell in Q3 2019. Collectively, these items accounted for around 12 percent of total CPI basket, lower than the 21.5 percent (revised) share in the previous quarter.

Inflation expectations for 2019 and 2020 are lower. Results of the BSP's survey of private sector economists in September 2019 showed lower mean inflation forecasts for 2019 and 2020 relative to the results in June 2019. In particular, the mean inflation forecast for 2019 decreased to 2.7 percent from 2.9 percent in the June 2019 survey. Similarly, the mean inflation forecast for 2020 declined to 3.1 percent from 3.2 percent during the same review period. Meanwhile, the mean inflation forecast for 2021 was steady at 3.1 percent.

According to analysts, the key downside risks to inflation are seen to emanate from the continued implementation of non-monetary policy actions to increase domestic food supply and stabilize prices, such as the rice tariffication law; base effects; stable global crude oil prices and lower electricity rates; easing domestic rice and other food prices; and weaker global economic prospects amid the escalating trade war between the US and China.

Meanwhile, possible upside risks to inflation are seen to come from the adverse effects of weather conditions on domestic food supply; expectations of elevated pork prices due to the African swine fever and increased demand for other meat products such as chicken; potential rebound in global oil prices; weaker peso against the US dollar; higher domestic demand during the holiday season; the proposed adjustments in excise taxes on oil, tobacco, and alcoholic beverages; and geopolitical tensions.

Real Gross Domestic Product (GDP) growth eases. The Philippine economy grew by 5.5 percent in Q2 2019. This is lower than the 5.6-percent and 6.2-percent expansion in Q1 2019 and Q2 2018, respectively. On the expenditure side, growth in Q2 2019 was driven by household consumption at 5.6 percent (from 6.1 in Q1 2019) and exports at 4.4 percent (from 5.7 percent in Q1 2019). On the production side, the services sector remained resilient, growing by 7.1 percent in Q2 2019 from 6.8 percent in Q1 2019.

Real GDP growth eases in Q2 2019

Meanwhile, trends in higher-frequency demand indicators point to an overall positive outlook for the domestic economy. The composite Purchasing Managers' Index remained firmly above the expansion threshold, indicating brisk activity ahead. Energy sales of Meralco accelerated while sales of new vehicles from the Chamber of Automotive Manufacturers of the Philippines, Inc. (CAMPI) returned to positive growth rate territory, a reversal from the contraction recorded in the same period a year ago. Similarly, business and consumer expectations surveys reported upbeat prospects over the next quarter.

Global economic activity remains subdued. The JP Morgan Global All-Industry Output Index fell to 51.2 in September from 51.3 in August as growth in new business slowed and the downturn in global trade activity continued. At the same time, growth in the US economy cooled down, while the euro area and Japan registered mild output growth. Similarly, real GDP in emerging and developing economies such as China and India posted slower growth rates. The more subdued outlook for global economic activity led a number of central banks to ease their monetary policy settings in order to stimulate their respective domestic economies.

The domestic financial system remains stable, supported by firm macroeconomic fundamentals. The Philippine equities market rallied during the quarter, as investor sentiment was boosted by the country's benign inflation outlook. The peso likewise strengthened amid market expectation of an interest rate cut by the US Federal Reserve. Moreover, investor appetite for local currency government securities remained healthy, affirmed by the continued oversubscription in the scheduled government securities auctions. However, episodes of volatility remain on the external front as global economic conditions become more challenging amid continuing trade tensions and geopolitical risks, as reflected in the country's wider bond spreads. Amid all these external developments, the Philippine banking system remained sound and resilient, marked by sustained growth in assets and deposits, and with capital adequacy ratios comfortably above the BSP's and Bank for International Settlements' prescribed levels. In addition, bank lending standards for loans to both enterprises and households were also broadly unchanged during the quarter, indicating that banks continue to be prudent in managing their risks.

The BSP further eases monetary policy settings in Q3 2019. Given dissipating price pressures during the third quarter, the BSP deemed it appropriate to reduce the policy rate by 25 basis points (bps) each on 8 August and 26 September. The BSP noted that the latest baseline inflation forecasts presented then continued to indicate that inflation is likely to settle within the lower half of the target band of 3.0 ± 1 percentage point for 2019 up to 2021. Inflation expectations also remained well-anchored based on the BSP's survey of private sector economists.

Moreover, the BSP noted that the balance of risks to the inflation outlook has shifted toward the upside for 2020, while it is seen to tilt to the downside for 2021. Upside risks to inflation over the near term were seen to emanate mainly from volatility in oil prices due to geopolitical tensions in the Middle East, as well as the potential impact of the African swine fever (ASF) outbreak on food prices. Meanwhile, subdued pace of global economic activity is considered to continue to temper the inflation outlook.

At the same time, the BSP was of the view that prospects for global economic growth were likely to remain weak owing mainly to uncertainty over trade policies. Nevertheless, firm domestic spending and progress on policy reforms could serve as buffers against global headwinds.

Given these considerations, the BSP believed that the benign inflation outlook provided room for a 50-bp reduction in the policy rate to support economic growth and reinforce market confidence.

Going forward, the BSP emphasized that it will continue to monitor emerging price and output developments to ensure that monetary policy settings remain consistent with price stability while being supportive of sustained non-inflationary economic growth over the medium term.

I. Inflation and Real Sector Developments

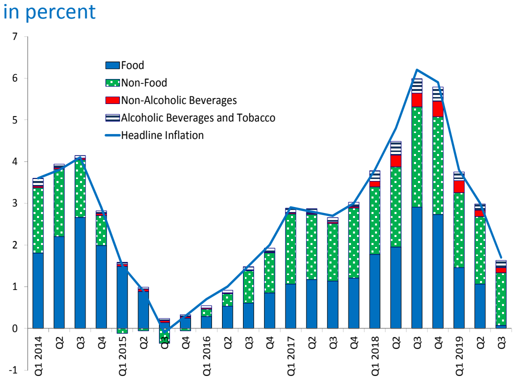
Prices

Headline inflation. Headline inflation rate decelerated further to 1.7 percent y-o-y in Q3 2019 from 3.0 percent due mainly to lower food inflation.

Price pressures ease further in Q3 2019 on lower food, electricity, and fuel inflation

This brought the y-t-d average to 2.8 percent y-o-y in 2019, which is well within the NG's announced target range of 3.0 percent ± 1.0 ppt for the year.

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



Source: Philipine Statistical Authority (PSA), BSP

Core Inflation. Likewise, core inflation—which excludes selected volatile food and energy items to measure underlying price pressures—also slowed down to 2.9 percent year-on-year in Q3 2019 from 3.4 percent in the previous quarter.

Official core inflation likewise slows down

Meanwhile, most of the BSP-computed alternative core inflation measures also eased in Q3 2019 relative to the previous quarter except for net of volatile items (Table 1).

Table 1. Alternative Core Inflation Measures
quarterly averages of year-on-year change

Quarter	Official Headline Inflation	Official Core Inflation	Trimmed Mean [1]	Weighted Median [2]	Net of Volatile Items [3]
2016	**1.3**	**1.6**	**1.2**	**1.3**	**1.9**
Q1	0.7	1.0	0.8	1.0	1.5
Q2	1.0	1.2	1.1	1.4	1.8
Q3	1.5	1.7	1.4	1.3	2.0
Q4	2.0	2.2	1.6	1.5	2.3
2017	**2.9**	**2.4**	**2.2**	**1.8**	**2.7**
Q1	2.9	2.7	2.1	1.9	2.6
Q2	2.8	2.5	2.3	1.7	2.8
Q3	2.7	2.3	2.1	1.6	2.7
Q4	3.0	2.4	2.3	1.7	2.7
2018	**5.2**	**4.2**	**4.2**	**4.1**	**4.5**
Q1	3.8	3.0	2.9	2.8	3.8
Q2	4.8	3.8	3.6	3.8	4.3
Q3	6.2	4.7	5.0	4.6	4.7
Q4	5.9	4.9	5.2	5.2	4.9
2019					
Q1	3.8	3.9	3.8	3.4	3.7
Q2	3.0	3.4	2.9	3.0	3.0
Q3	**1.7**	**2.9**	**1.9**	**2.8**	**3.3**

[1] The trimmed mean represents the average inflation rate of the (weighted) middle 70 percent in a lowest-to-highest ranking of year-on-year inflation rates for all CPI components.

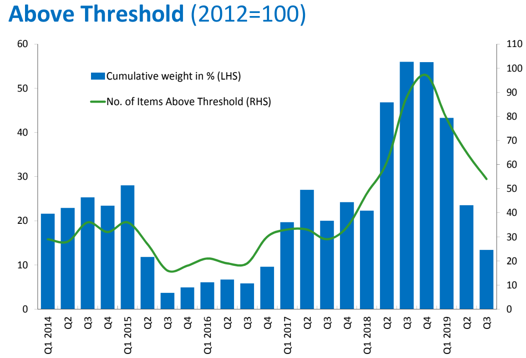
[2] The weighted median represents the middle inflation rate (corresponding to a cumulative CPI weight of 50 percent) in a lowest-to-highest ranking of year-on-year inflation rates.

[3] The net of volatile items method excludes the following items: bread and cereals, vegetables sugar, jam, honey, chocolate, and confectionery, electricity, gas, fuel and lubricants for personal transport equipment, and passenger transport by road, which represents 29.5 percent of all items.

Source: PSA, BSP estimates

Consistent with the downtrend in overall inflation, the number of CPI items with inflation rates higher than the threshold of 4.0 percent (the upper end of the 2019 inflation target) also fell to 54 items in Q3 2019 from 65 items in the previous quarter.

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



Source: PSA, BSP staff estimates

Collectively, these items accounted for around 13.4 percent of total CPI basket, lower than the 23.5 percent share in the previous quarter.

Food Inflation. Improved domestic supply conditions weighed down on food prices in Q3 2019. Food inflation rate slowed down significantly to 0.2 percent y-o-y in Q3 2019 from 3.0 percent in the previous quarter as most key food items registered lower or negative inflation during the quarter (Table 2).

Food inflation is significantly lower

Rice and corn inflation turned even more negative during the quarter while prices for vegetables, sugar, jam, honey, chocolate, and confectionery also declined relative to year-ago levels. At the same time, slower price increases y-o-y in meat, fish, as well as oils and fats also contributed to the slowdown in food inflation.

Table 2. Inflation Rates for Selected Food Items
quarterly averages in percent (2012=100)

Commodity	2018				2019		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Food and Non-Alcoholic Beverages	**5.0**	**5.9**	**8.5**	**8.0**	**4.6**	**3.0**	**0.5**
Food	5.0	5.5	8.2	7.7	4.1	3.0	0.2
Bread and Cereals	2.8	4.2	6.6	7.1	3.0	0.2	-3.6
Rice	2.6	4.4	7.5	8.2	3.0	-0.8	-5.8
Corn	9.7	13.7	11.3	4.9	-0.7	-3.3	-3.6
Meat	6.4	5.0	7.3	6.4	4.4	3.6	2.8
Fish	12.2	11.7	12.4	12.0	6.8	3.8	2.7
Milk, Cheese and Eggs	2.1	2.1	2.7	2.9	2.6	2.5	2.7
Oils and Fats	4.0	3.2	3.8	4.8	4.1	3.1	1.8
Fruit	6.1	5.8	5.6	4.0	1.9	4.1	7.3
Vegetables	3.9	7.4	18.8	11.7	4.8	9.9	-1.0
Sugar, Jam, Honey, Chocolate and Confectionery	-1.4	1.4	8.9	10.4	7.9	4.6	-2.8
Food Products, N.E.C.	2.0	3.2	4.3	5.4	4.3	6.5	6.5
Non-Alcoholic Beverages	4.6	9.9	11.5	12.9	10.0	5.1	4.2
Alcoholic Beverages and Tobacco	15.9	20.5	21.7	21.7	13.0	9.5	11.1

Source of Basic Data: PSA, BSP

Non-food Inflation. Non-food inflation also decelerated in Q3 2019 to 2.1 percent from 2.6 percent in the previous quarter due to lower domestic prices of petroleum products and electricity rates (Table 3). Transport inflation turned negative y-o-y in Q3 2019 due largely to lower fuel prices, influenced by lower international crude oil prices.

Non-food inflation decelerates

At the same time, electricity rates also declined as a result of lower generation charges. The decline in these two components was enough to offset the higher education inflation driven by base effects following the implementation of the Government's free tuition program for the public tertiary level in 2018.

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

Commodity	2018				2019		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Non-Food	**2.6**	**3.4**	**4.1**	**3.9**	**3.0**	**2.6**	**2.1**
Clothing and Footwear	2.0	2.2	2.4	2.6	2.4	2.4	2.6
Housing, Water, Electricity, Gas and Other Fuels	2.7	3.5	5.2	4.3	3.7	3.2	1.6
Electricty, Gas, and Other Fuels	4.3	6.2	10.6	6.8	4.9	3.0	-2.3
Furnishings, Household Equipment & Routine Household Maintenance	2.4	2.9	3.5	3.8	3.7	3.2	2.9
Health	2.2	2.7	4.0	4.5	4.1	3.6	3.1
Transport	4.9	6.0	7.9	7.2	2.3	3.0	-0.2
Communication	0.2	0.3	0.4	0.4	0.4	0.4	0.3
Recreation and Culture	1.4	1.4	2.1	3.2	3.1	3.1	2.1
Education	1.8	2.5	-3.8	-3.8	-3.8	-4.0	4.4
Restaurant and Miscellaneous Goods and Services	2.6	3.6	3.9	4.4	3.9	3.3	2.2

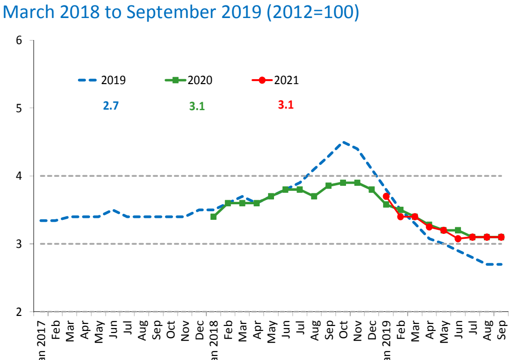
Source of Basic Data: PSA, BSP

Private Sector Economists' Inflation Forecasts. Results of the BSP's survey of private sector economists in September 2019 showed lower mean inflation forecasts for 2019 and 2020 relative to the results in June 2019.

Private sector economists' mean inflation forecasts for 2019 and 2020 are lower

In particular, the mean inflation forecast for 2019 decreased to 2.7 percent from 2.9 percent in the June 2019 survey.[4] Similarly, the mean inflation forecast for 2020 declined to 3.1 percent from 3.2 percent during the same review period. Meanwhile, the mean inflation forecast for 2021 was steady at 3.1 percent.

Chart 3. BSP Private Sector Economists' Survey*
mean forecast for full year; in percent
January 2016 to February 2018 (2006=100)
March 2018 to September 2019 (2012=100)



*Based on forecasts provided by 26 respondents.
Source: BSP

[4] There were 26 respondents in the BSP's survey of private sector economists in September 2019. The survey was conducted from 5 to 16 September 2019.

Analysts expect inflation to remain manageable and lie within the government's target range. The key downside risks to inflation are seen to emanate from the continued implementation of non-monetary policy actions to increase domestic food supply and stabilize prices, such as the rice tariffication law; base effects; stable global crude oil prices and lower electricity rates; easing domestic rice and other food prices; and weaker global economic prospects amid the escalating trade war between the US and China. Meanwhile, possible upside risks to inflation are the adverse effects of weather conditions on domestic food supply; expectations of elevated pork prices due to the African swine fever and increased demand for other meat products such as chicken; potential rebound in global oil prices; weaker peso against the US dollar; higher domestic demand during the holiday season; the proposed adjustments in excise taxes on oil, tobacco, and alcoholic beverages; and geopolitical tensions.

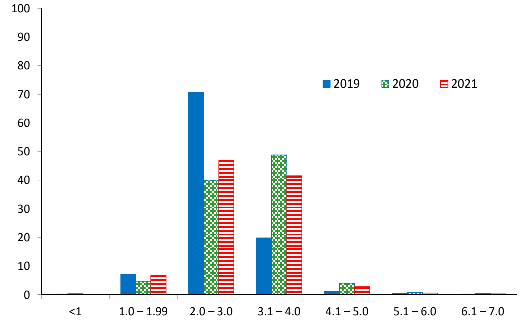
Table 4. Private Sector Forecasts for Inflation
annual percentage change; September 2019 (2012=100)

	2019		2020	2021
	Q4	FY	FY	FY
1) Al-Amanah Islamic Bank	2.00	3.00	3.00	3.00
2) Asia ING	2.30	2.80	3.10	3.20
3) Banco de Oro	1.70	3.00	3.10	3.30
4) Bangkok Bank	2.00	2.70	3.00	3.00
5) Bank of Commerce	1.54	2.51	-	-
6) Bank of China Ltd.	2.90	2.90	3.00	3.20
7) Bank of the Philippine Islands	1.80	2.60	3.20	3.30
8) Barclays	1.80	2.60	3.10	-
9) Citibank	1.70	2.50	3.00	3.10
10) Chinabank	2.90	3.00	3.00	3.00
11) CTBC Bank	2.70	2.60	3.20	3.50
12) Deutsche Bank	2.40	2.60	-	-
13) Eastwest bank	1.10	2.40	2.60	2.90
14) Global Source	1.60	2.50	2.90	3.00
15) Korea Exchange Bank	3.20	3.10	3.00	3.00
16) Land Bank of the Phils.	1.50	2.50	3.20	2.20
17) Maybank	2.00	2.65	3.40	2.90
18) Maybank-ATR KimEng	1.80	2.60	3.00	3.00
19) Mizuho	2.10	2.70	2.90	-
20) Nomura	2.00	2.60	3.10	3.30
21) RCBC	1.40 - 1.50	2.50 - 2.60	3.00 - 3.20	3.50 - 4.00
22) Robinsons Bank	1.90	2.60	3.20	3.00
23) Security Bank	1.50	2.70	3.30	3.50
24) Standard Chartered	2.00	2.70	4.20	4.00
25) Union Bank of the Phils.	1.70	2.60	2.40	2.30
26) UBS	1.70	2.60	3.40	-
Median Forecast	1.9	2.6	3.1	3.0
Mean Forecast	**2.0**	**2.7**	**3.1**	**3.1**
High	3.2	3.1	4.2	4.0
Low	1.1	2.4	2.4	2.2
Number of Observations	26	26	24	21
Government Target	**3.0±1.00**	**3.0±1.00**	**3.0±1.00**	**3.0±1.00**

Source: BSP

Based on the probability distribution of the forecasts provided by 22 out of 26 respondents, there is a 90.4-percent probability that average inflation for 2019 will settle between the 2-4 percent range. For 2020, the respondents assigned a 88.9-percent probability that inflation will fall within the 2-4 percent target range.

Chart 4. Probability Distribution for Analysts' Inflation Forecasts* (2019-2021)



*Probability distributions were averages of those provided by 22 out of 26 respondents.
Source: BSP September 2019 Survey

Businesses expect a within-target inflation, while consumers anticipate a breach in the upper end of the target range

Based on the Q3 2019 BSP Business Expectations Survey (BES), a smaller number of respondents in Q3 2019 expect inflation to decline in the current quarter (i.e., the diffusion index increased slightly from -5.5 percent to -5.1 percent).

By contrast, more respondents anticipate higher inflation in the next quarter (i.e., the diffusion index rose from 2.7 percent to 13.7 percent). Firms generally expect the rate of increase in consumer prices to remain within the government's 2 to 4 percent inflation target range at 3.4 percent in Q3 2019 and 3.5 percent in Q4 2019 (from 3.9 percent and 4 percent, respectively, in the previous quarter's survey results).

Consumer Expectations Survey (CES) results for Q3 2019 indicated that consumers expect inflation to increase over the next 12 months to an average of 4.3 percent from 4 percent in the Q2 2019 survey. This is higher than the upper-end of the government's target range of 2-4 percent for 2019. Consumers expect higher inflation for the following items: rice (3.6 percent); bread and cereals (5.3 percent); meat (4.3 percent); fish and seafood (5.5 percent); fruits (5.7 percent); vegetables (6.5 percent); milk, cheese, and eggs (4.9 percent); non-alcoholic beverages (5.4 percent); alcoholic beverages (7.5 percent); light (6.6 percent); medical care (3.2 percent); communication (1.8 percent); personal care

(4.9 percent); and restaurants and cafes (3.9 percent).

Energy prices. Dubai crude oil prices, on average, declined by 9.2 percent in Q3 2019 relative to the previous quarter's level due to concerns of potentially weaker demand amid uncertainties surrounding the external environment, with the the International Monetary Fund (IMF) downgrading its global growth projections for 2019 and 2020.[5]

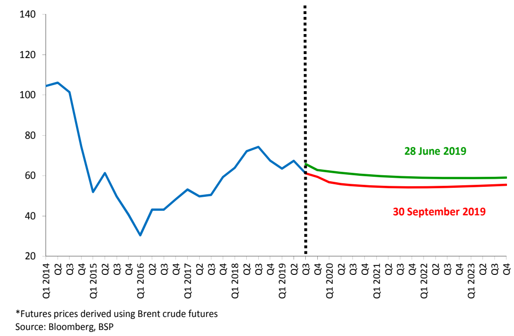
Weaker demand concerns exert downward pressure on global oil prices

At the same time, energy agencies have also lowered their oil demand growth projections. The International Energy Agency (IEA) reduced its estimated global oil demand growth by 100,000 barrels per day (kb/d) for 2019 and 50 kb/d for 2020 in its August 2019 report compared with the previous month's estimates.[6] Likewise, the US Energy Information Administration (EIA) revised downward its total world oil consumption by 0.1 percent for both 2019 and 2020 in its September report compared to the August report.

Nevertheless, there were upside risks to oil prices during the quarter relating to supply concerns, particularly the production disruptions due to adverse weather conditions and geopolitical tensions in the Middle East. In September 2019, a drone strike damaged some of Saudi Arabia's oil infrastructure facilities, which contributed to higher oil prices in September.

Estimated futures prices of Dubai crude oil as of end-September 2019,[7] which are based on movements of Brent futures price, showed a lower path for 2019 – 2023 compared to the estimates in the previous quarter.[8]

Chart 5. Spot and Estimated Prices of Dubai Crude Oil



On a cumulative basis, net price adjustments in domestic petroleum products[9] as of 24 September 2019 remained positive. Based on the Department of Energy (DOE) report,[10] prices of gasoline, kerosene, and diesel went up on a net basis by ₱7.86 per liter, ₱3.76 per liter, and ₱5.82 per liter, respectively.

Power. For Q3 2019, the overall electricity rate in the Meralco-franchised area decreased by around ₱0.78 per kilowatt hour (kWh) to ₱9.53 per kWh (from ₱10.31 per kWh in Q2 2019).

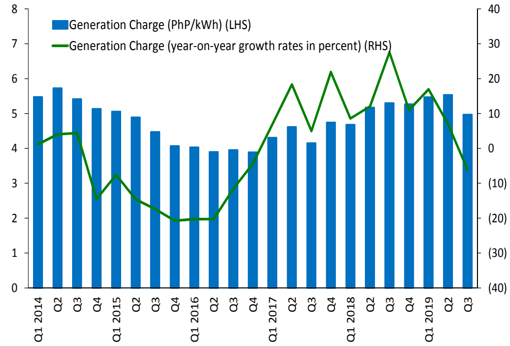
Retail electricity prices decrease due mainly to downward adjustment in generation charge

The downward adjustment was attributed mainly to the average decrease in the generation cost by around ₱0.57 per kWh to about ₱4.97 per kWh (from ₱5.53 per kWh in Q2 2019). In turn, the lower generation cost in Q3 2019 was primarily due to registered decreases in generation charges from Wholesale Electricity Spot Market (WESM) on the back of improved supply conditions in the Luzon grid as well as from Power Supply Agreements (PSAs) due to strengthening of the peso against the US dollar and lower fuel prices. It may be noted that in July 2019, the decrease in the overall electricity rate was mainly brought about by a lower transmission charge for residential customers.

[5] IMF World Economic Outlook (WEO) Update, July 2019.
[6] IEA Oil Market Report, https://www.iea.org/oilmarketreport/reports/
[7] Future prices using Brent crude futures data. Taken as of 30 September 2019.
[8] Future prices derived using Brent crude futures data. Taken as of 28 June 2019 Sources: BSP-staff calculations, Bloomberg L.P.

[9] Based on actual prevailing common prices of domestic petroleum products for Metro Manila reported by the Department of Energy. Net adjustments are based on monitor report on the DOE website: https://www.doe.gov.ph/oil-monitor?page=1
[10] DOE Oil Monitor as of 24 September 2019.

Chart 6. Meralco's Generation Charge
PhP/kWh; year-on-year growth rates in percent



Source: Meralco

There are potential sources of upside pressures on electricity charges. Meralco has existing petitions for rate increases with Energy Regulatory Commission (ERC) which include the petition to implement the Maximum Average Price for 2012, 2013, 2014, and 2015; amended application for a rate increase in the January 2014 billing (consisting of incremental fuel costs and deferred generation cost to be collected monthly for six months); and petitions for the refund of generation over/under recovery (GOUR), transmission over/under recovery (TOUR), system loss over/under recovery (SLOUR), and lifeline subsidy over/under recovery (LSOUR) for the period January-December 2011. In addition, the Power Sector Assets and Liabilities Management (PSALM) has several pending petitions with ERC for the recovery of True-Up Adjustments of Fuel and Purchased Power Costs (TAFPPC), Foreign Exchange Related Costs (TAFxA) and Purchased Power Costs and Foreign Exchange Related Costs by the National Power Corporation (NPC), and NPC's Stranded Debt portion of the universal charge. Likewise, the National Grid Corporation of the Philippines (NGCP) also filed several petitions to recover connection charges and residual sub-transmission charges for 2011-2013 and the costs of repair on damages caused by force majeure events such as earthquake, flooding, landslides, and lightning incidents in 2011-2012.

Aggregate Demand and Supply[11]

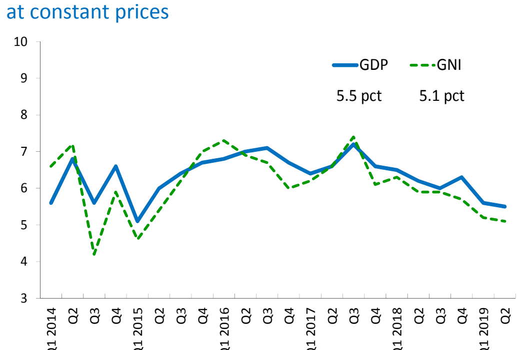
The Philippine economy grew by 5.5 percent in Q2 2019. This is lower than the 5.6-percent and 6.2-percent expansion in Q1 2019 and Q2 2018, respectively.

Real GDP growth is slightly lower in Q2 2019

On the expenditure side, growth in Q2 2019 was driven by household consumption at 5.6 percent (from 6.1 in Q1 2019) and exports at 4.4 percent (from 5.7 percent in Q1 2019). Government spending decelerated to 6.9 percent, lower than the 7.4-percent growth in Q1 2019. Investments contracted by 8.5 percent (from 8.0-percent growth in Q1 2019). Under the production approach, the services sector remained resilient, growing by 7.1 percent in Q2 2019 from 6.8 percent in Q1 2019. The industry sector grew by 3.7 percent in Q2 2019, lower than the 4.8-percent growth recorded a quarter ago. However, growth of the agriculture, hunting, forestry and fishing (AHFF) sector was at 0.6 percent, marginally lower than the 0.7 percent growth in Q1 2019.

Gross national income (GNI) slightly moderated to 5.1 percent in Q2 2019, lower compared with the Q1 2019 growth of 5.2 percent and Q2 2018 growth of 5.9 percent. Likewise, net primary income growth decelerated to 3.1 percent from 3.2 percent in Q1 2019 and 4.5 percent in Q2 2018.

Chart 7. Gross Domestic Product (GDP) and Gross National Income (GNI)
at constant prices



Source: PSA

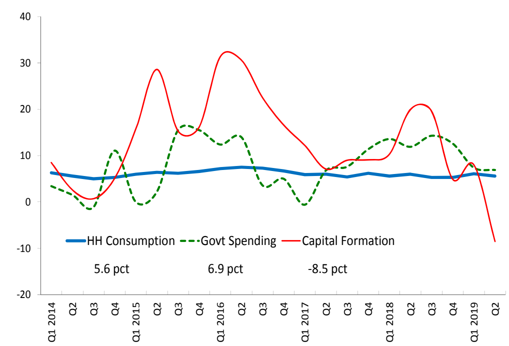
[11] Based on revised National Income Accounts (NIA) released as of 8 August 2019.

Aggregate Demand. On the expenditure side, household spending, exports and government spending contributed 3.7 ppts, 2.7 ppts, and 0.9 ppt, respectively, to total GDP growth in Q2 2019, which more than offset the negative contribution of investments at -2.4 ppts.

Household spending is key growth driver in Q2 2019

Household expenditures, which accounted for 66.3 percent of the country's total output in Q2 2019, grew by 5.6 percent, lower than the quarter- and year-ago growth of 6.1 percent and 6.0 percent, respectively (Table 5). Moderation in household spending was observed generally across commodity groups. The slowdown in spending was mainly due to the slower growth in transport expenditures amid relatively higher pump prices during the quarter. In addition, purchases of private vehicles declined in the second quarter, based on the data from CAMPI. Notably, household spending on food and non-alcoholic beverages, and housing, water, electricity, gas, and other fuels also decelerated.

Chart 8. Gross Domestic Product by Expenditure Shares
at constant prices



Source: PSA

Government expenditures grew by 6.9 percent in Q2 2019, lower than the 7.4-percent growth in Q1 2019 and 11.9-percent growth in Q2 2018. The growth in the government spending was due to the increase in the following government projects and activities: a) rollout of the fourth tranche of salary increase for civilian employees and the base pay increase and pension adjustment for active military and uniform personnel; b) salary adjustment in Q2 2019, which included the retroactive payment for Q1 2019; and c) payment of cash grants to the beneficiaries of the Pantawid Pamilyang Pilipino Program (4Ps).

Capital formation contracted by 8.5 percent in Q2 2019 from an 8 percent growth in Q1 2019. The decline in fixed capital was largely due to the decline in investments in durable equipment, particularly in transport and machineries specialized for particular industries. Specifically, air transport equipment dropped by 49.5 percent in Q2 2019 from high growth rates in the previous quarters (91.5 percent, 36.4 percent and 287.1 percent for Q1 2019, Q4 2018 and Q3 2018, respectively) as the investments made by the Philippine Airlines on its refleeting program have been completed in May 2019. Moreover, other capital outlays of the national and local governments dropped amid the budget impasse and election ban. Contrary to the performance in investment spending, private construction continued to expand at 23.1 percent growth from a lower growth rate of 10.3 percent in Q1 2019, owing to the sustained demand for office and retails spaces as well as residential units. Intellectual property products also improved during the reference period.

Table 5. Gross Domestic Product by Expenditure Shares
at constant 2000 prices; growth rate in percent

BY EXPENDITURE ITEM	2018	2019	
	Q2	Q1	Q2
Household Consumption	6.0	6.1	5.6
Government Consumption	11.9	7.4	6.9
Capital Formation	20.0	8.0	-8.5
Fixed Capital Formation	19.3	6.4	-4.8
Exports	14.7	5.7	4.4
Imports	21.0	8.6	0.0

Source: PSA

Overall exports grew by 4.4 percent in Q2 2019, lower compared to 5.7 percent in Q1 2019. Exports of goods slowed to 4.6 percent (from 6.3 percent in Q1 2019), which tempered the slightly faster growth in exports of services. The slowdown in merchandise exports was caused by the continued deceleration of electronic components for four consecutive quarters on account of lower growth in the sales of semiconductors, mainly to Asian countries such as Hong Kong, Singapore and Taiwan. This was also reflected from the lower sales of semiconductors worldwide due to the US and China trade war. On the other hand, exports in services slightly improved to 3.8 percent in Q2 2019 from 3.6 growth in Q1 2019. This was due to higher growth in travel especially during summer months and continued rise in insurance.

Overall imports registered no growth in Q2 2019 compared with the 8.6 percent growth in Q1 2019. The decline of imports of goods (by 0.2 percent from 9-percent growth in Q1 2019) may be traced from the significant drop in the importation of transport equipment from Japan, Thailand and Indonesia, and base metals. Meanwhile, imports of services recorded a lower growth of 1.5 percent (from 6.8 percent in Q1 2019) due to the decline in imports of transportation and government services, as well as the deceleration in travel and miscellaneous services.

Other Demand Indicators. Higher-frequency demand indicators point to an overall positive outlook for the domestic economy. The composite Purchasing Managers' Index (PMI) remained firmly above the expansion threshold, indicating brisk activity ahead. Energy sales of Meralco accelerated while sales of new vehicles from CAMPI returned to positive growth rate territory, a reversal from the contraction recorded in the same period a year ago. Similarly, business and consumer expectations surveys reported upbeat prospects over the next quarter.

Property Prices

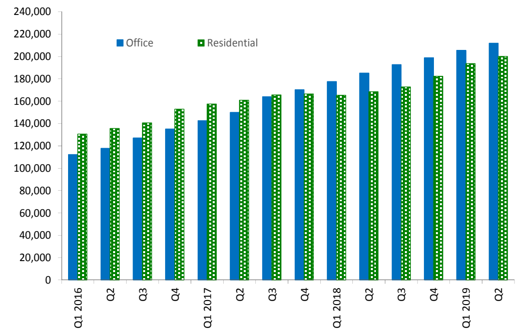
Capital Values. Capital values[12] for office buildings in Metro Manila[13] in Q2 2019 were higher in nominal terms than their quarter- and year-ago levels.

Capital values for office and residential buildings increase

Average capital values in Metro Manila rose to ₱190,600/sq.m., higher by 3.9 percent and 18.4 percent compared to the quarter- and year-ago levels, respectively. In terms of location, capital values for office buildings in Manila Bay area recorded the highest y-o-y growth at 44.8 percent in Q2 2019, a further increase from the 15.2-percent expansion in the same period in 2018.

[12] Probable price that the property would have fetched if sold on the date of the valuation. The valuation includes imputed land and building value.
[13] This includes Makati Central Business District (CBD), Fort Bonifacio, Ortigas, Eastwood, Alabang, and Manila Bay Area.

Chart 9. Capital Values
price per square meter



Source: Colliers International Philippines

Likewise, average capital values for luxury residential buildings[14] in Metro Manila[15] in Q2 2019 increased to ₱202,200/sq.m. from their quarter- and year-ago levels. Average prices for three-bedroom luxury residential condominium units in Metro Manila grew by 3.4 percent q-o-q and 19.4 percent y-o-y. In terms of location, capital values for three-bedroom luxury residential condominium units in Fort Bonifacio area recorded the highest y-o-y growth at 23.3 percent in Q2 2019, a further increase from the 6.5-percent expansion in the same period in 2018.

Rental Values. Average monthly rents in Metro Manila reached ₱985/sq.m. in Q2 2019, an increase of 2.0 percent from the previous quarter. Similarly, average monthly office rents in Metro Manila were higher by 8.9 percent relative to Q2 2018.

Office rental values above 1997 levels in nominal terms

The appreciation in office rental rates was due to the sustained demand from offshore gaming firms. In terms of location, rental values for office buildings in Manila Bay area recorded the highest y-o-y growth at 20.5 percent in Q2 2019, a further increase from the 19.6-percent expansion in the same period in 2018.

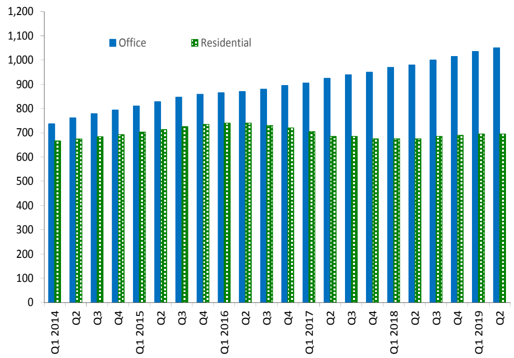
[14] In terms of location, luxury residential units are located within the CBD core and have quality access to/from and have superior visibility from the main avenue. Meanwhile, in terms of general finish, luxury residential units have premium presentation and maintenance.
[15] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, and Rockwell.

Average monthly rents for luxury three-bedroom condominium units in the Metro Manila was recorded at ₱730/sq.m. in Q2 2019, slightly higher by 0.5 percent compared to the previous quarter.

Rental values rise

Meanwhile, average monthly rents for the 3-bedroom segment in Metro Manila were higher by 2.9 percent compared to the year-ago levels.

Chart 10. Rental Values
price per square meter



Source: Colliers International Philippines

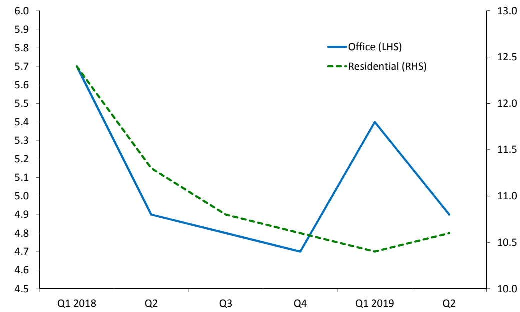
The slight increase in rents in Metro Manila in Q2 2019 could be attributed to the sustained demand for condominium units, especially in business districts housing offshore gaming firms. In terms of location, capital values for three-bedroom luxury residential condominium units in Ortigas Center recorded the highest y-o-y growth at 3.1 percent in Q2 2019, a turnaround from the 1.0 percent contraction in the same period in 2018.

Vacancy Rates. The overall office vacancy rate in Metro Manila declined to 4.9 percent in Q2 2019 from 5.4 percent in Q1 2019 due mainly to substantial absorption of office spaces in Ortigas Center and its fringes.

Office vacancy rates decline

Office vacancy rates in Ortigas Center (1.0 percent from 1.9 percent) decreased in Q2 2019 compared to the previous quarter. By contrast, the office vacancy rates in Makati CBD (1.8 percent from 1.2 percent), Fort Bonifacio (6.8 percent from 6.3 percent), and Manila Bay Area (0.6 percent from 0.5 percent) increased in Q2 2019 compared to Q1 2019. The overall office vacancy rate in Metro Manila is projected at 6.1 percent in 2019 due to sustained take up from offshore gaming, outsourcing, and traditional tenants. Colliers International Philippines noted that an active office leasing market would temper the increase in vacancy rates.

Chart 11. Vacancy Rates
in percent



Source: Colliers International Philippines

Meanwhile, the overall residential vacancy rate in Metro Manila increased to 10.6 percent in Q2 2019 from 10.4 percent in Q1 2019 due to the newly completed condominium units especially in the established business districts. In particular, residential vacancy rates across all major CBDs in Metro Manila, except Fort Bonifacio (unchanged at 14.4 percent), were higher in Q2 2019 from their respective quarter-ago levels, namely: Makati CBD (10.7 percent from 10.6 percent), Rockwell Center (9.6 percent from 9.5 percent), Ortigas Center (4.7 percent from 4.6 percent), Eastwood City (4.2 percent from 4.1 percent), and Manila Bay area (12.1 percent from 11.9 percent). Colliers foresees residential vacancy rate to marginally increase to 10.7 percent in 2019 due to sustained demand, especially in business hubs that house outsourcing firms and offshore gaming firms from China.

BSP Residential Real Estate Price Index (RREPI).[16] Residential real estate prices went up slightly by 0.4 percent y-o-y in Q2 2019 as the RREPI increased to 117.5 from 117.0 in Q2 2018.

[16] The RREPI measures the average changes in prices of different types of housing units over a period of time across different geographical regions where the growth rate of the index measures house inflation. It is computed as a weighted chain-linked index based on the average appraised value per square meter weighted by the share of floor area of new housing units.

Residential real estate prices rise in Q2 2019

Y-o-y, prices across types of housing units increased in Q2 2019, except for single detached/attached houses, which declined by 4.2 percent (Table 6). Prices of duplexes, condominium units, and townhouses rose by 12.5 percent, 9.6 percent, and 4.3 percent, respectively, compared to Q2 2018. Q-o-q, the RREPI decreased by 2.1 percent to 117.5 from 120 in Q1 2019, as all types of housing units registered price decreases, except for condominium units.

Table 6. Residential Real Estate Price Index By Housing Type

Q1 2014=100; growth rate in percent

Quarter	Residential Real Estate Price Index [1] (By Housing Type)				
	Overall [2]	Single Detached/ Attached	Duplex [3]	Townhouse	Condominium Unit
2016 Q1	106.9	98.9	114.7	107.3	123.2
Q2	111.7	105.8	98.6	109.2	123.9
Q3	109.6	102.6	96.7	100.5	126.4
Q4	111.1	104.9	87.5	107.7	125.5
2017 Q1	113.9	108.0	91.2	107.6	128.3
Q2	111.8	103.6	103.6	112.7	129.3
Q3	111.6	103.4	88.4	107.7	131.0
Q4	117.4	104.6	102.6	116.3	143.3
2018 Q1	116.2	107.3	131.5	122.4	130.9
Q2	117.0	105.1	99.0	128.4	138.5
Q3	116.6	103.6	115.5	127.7	138.6
Q4	118.1	102.6	98.8	129.9	144.2
2019 Q1	120.0	105.7	121.0	134.4	145.2
Q2	117.5	100.7	111.4	133.9	151.8
Year-on-Year Growth Rates					
2016 Q1	1.3	-0.9	10.4	4.0	8.7
Q2	5.9	8.1	0.7	12.8	3.3
Q3	3.8	5.4	-5.1	2.9	3.5
Q4	3.3	4.3	-12.3	6.4	3.6
2017 Q1	6.5	9.2	-20.5	0.3	4.1
Q2	0.1	-2.1	5.1	3.2	4.4
Q3	1.8	0.8	-8.6	7.2	3.6
Q4	5.7	-0.3	17.3	8.0	14.2
2018 Q1	2.0	-0.6	44.2	13.8	2.0
Q2	4.7	1.4	-4.4	13.9	7.1
Q3	4.5	0.2	30.7	18.6	5.8
Q4	0.6	-1.9	-3.7	11.7	0.6
2019 Q1	3.3	-1.5	-8.0	9.8	10.9
Q2	0.4	-4.2	12.5	4.3	9.6
Quarter-on-Quarter Growth Rates					
2016 Q1	-0.7	-1.7	14.9	6.0	1.7
Q2	4.5	7.0	-14.0	1.8	0.6
Q3	-1.9	-3.0	-1.9	-8.0	2.0
Q4	1.4	2.2	-9.5	7.2	-0.7
2017 Q1	2.5	3.0	4.2	-0.1	2.2
Q2	-1.8	-4.1	13.6	4.7	0.8
Q3	-0.2	-0.2	-14.7	-4.4	1.3
Q4	5.2	1.2	16.1	8.0	9.4
2018 Q1	-1.0	2.6	28.2	5.2	-8.7
Q2	0.7	-2.1	-24.7	4.9	5.8
Q3	-0.3	-1.4	16.7	-0.5	0.1
Q4	1.3	-1.0	-14.5	1.7	4.0
2019 Q1	1.6	3.0	22.5	3.5	0.7
Q2	-2.1	-4.7	-7.9	-0.4	4.5

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

The average residential property prices in National Capital Region (NCR) increased by 5.2 percent, while those in the Areas Outside the NCR (AONCR) declined by 1.1 percent in Q2 2019 compared to Q2 2018 prices (Table 7). In NCR, the rise in prices of duplexes and condominium units more than offset the decline in prices of single detached/attached houses and townhouses. In AONCR, the decline in the prices of single detached/attached houses outweighed the growth of other housing unit types.

Residential property prices increase in NCR, decline in AONCR

For Q2 2019, 73.4 percent of residential real estate loans (RRELs) were for the acquisition of new housing units. By type of housing unit, 45.8 percent of residential property loans were for the purchase of condominium units, followed by single detached/attached houses (43.0 percent), and townhouses (10.5 percent).

Table 7. Residential Real Estate Price Index By Area

Q1 2014=100; growth rate in percent

Quarter	Residential Real Estate Price Index [1] (By Area)		
	Overall	NCR	AONCR
2016 Q1	106.9	113.4	103.3
Q2	111.7	116.1	109.3
Q3	109.6	115.7	106.2
Q4	111.1	117.3	107.9
2017 Q1	113.9	118.4	111.6
Q2	111.8	120.4	107.5
Q3	111.6	118.2	108.1
Q4	117.4	127.6	111.1
2018 Q1	116.2	121.6	112.5
Q2	117.0	125.7	112.0
Q3	116.6	126.4	110.5
Q4	118.1	129.8	110.2
2019 Q1	120.0	132.5	113.1
Q2	117.5	132.2	110.8
Year-on-Year Growth Rates			
2016 Q1	1.3	3.5	1.8
Q2	5.9	1.9	9.6
Q3	3.8	0.2	6.9
Q4	3.3	0.6	6.0
2017 Q1	6.5	4.4	8.0
Q2	0.1	3.7	-1.6
Q3	1.8	2.2	1.8
Q4	5.7	8.8	3.0
2018 Q1	2.0	2.7	0.8
Q2	4.7	4.4	4.2
Q3	4.5	6.9	2.2
Q4	0.6	1.7	-0.8
2019 Q1	3.3	9.0	0.5
Q2	0.4	5.2	-1.1
Quarter-on-Quarter Growth Rates			
2016 Q1	-0.7	-2.7	1.5
Q2	4.5	2.4	5.8
Q3	-1.9	-0.3	-2.8
Q4	1.4	1.4	1.6
2017 Q1	2.5	0.9	3.4
Q2	-1.8	1.7	-3.7
Q3	-0.2	-1.8	0.6
Q4	5.2	8.0	2.8
2018 Q1	-1.0	-4.7	1.3
Q2	0.7	3.4	-0.4
Q3	-0.3	0.6	-1.3
Q4	1.3	2.7	-0.3
2019 Q1	1.6	2.1	2.6
Q2	-2.1	-0.2	-2.0

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

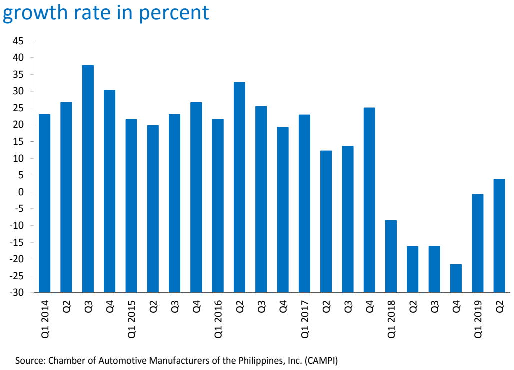
By area, most of the RRELs granted in the NCR were for the purchase of condominium units, while RRELs granted in AONCR were for single detached/attached houses. By region, NCR accounted for 43.0 percent of the total number of RRELs granted during the quarter, followed by CALABARZON (27.4 percent), Central Luzon (8.9 percent), Central Visayas (6.0 percent), Western Visayas (4.3 percent), Northern Mindanao (3.3 percent), and Davao Region (3.0 percent). Together, NCR and the six other regions accounted for 95.9 percent of total housing loans granted by banks during the quarter.

Vehicle Sales. Sales of new vehicles from CAMPI members increased by 3.7 percent y-o-y in Q2 2019, a reversal from the 16.2-percent contraction recorded in the same period a year ago, due mainly to higher sales of commercial vehicles during the period.

Sales of new vehicles increase

Commercial vehicle sales, which account for about 70.4 percent of total vehicle sales, rose by 6.9 percent y-o-y in Q2 2019 from the 12.6-percent decline in the same period of 2018. Commercial vehicles sold during the period reached 62,501 units from 58,476 units in Q2 2018.

Chart 12. Vehicle Sales
growth rate in percent



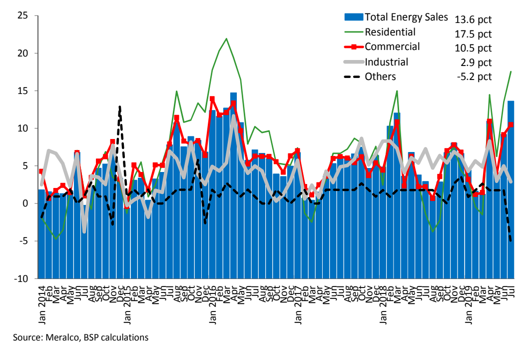
By contrast, sales of passenger cars declined by 3.1 percent y-o-y in Q2 2019, albeit an improvement from the 23.1-percent contraction in the same period in 2018. New passenger car sales accrued to a total of 26,246 units in Q2 2019 from 27,077 units in the same period a year ago.

Energy Sales. Energy sales of Meralco increased by 13.6 percent y-o-y in July 2019, faster compared to the 2.9-percent growth in the same period a year ago.

Energy sales accelerate

Energy sales from the residential sector, commercial sector, and industrial sector increased by 17.5 percent, 10.5 percent, and 2.9 percent, respectively.

Chart 13. Energy Sales
year-on-year growth in percent

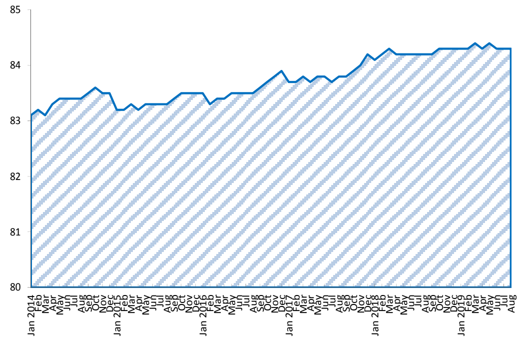


Capacity Utilization. The average capacity utilization rate of the manufacturing sector stood at 84.3 percent in August 2019, unchanged from the month-ago level based on the PSA's Monthly Integrated Survey of Selected Industries (MISSI).

Capacity utilization in manufacturing remains above 80 percent

Of the 702 respondent-establishments, 60.6 percent operated at a capacity of at least 80.0 percent in August 2019. Data showed that most of the manufacturing companies have been operating above the 80.0-percent capacity since 2010.

Chart 14. Monthly Average of Capacity Utilization for Manufacturing
in percent



Source: PSA

There were 13 (out of the 20) major industries in the sector that operated above the 80.0-percent capacity level that include: petroleum products (89.2 percent); basic metals (88.6 percent); machinery except electrical (86.6 percent); non-metallic mineral products (86.4 percent); food manufacturing (85.2 percent); chemical products (85.1 percent); electrical machinery (85 percent); printing (84.1 percent); paper and paper products (83.8 percent); rubber and plastic products (83.5 percent); wood and wood products (82.1 percent); leather products (80.7 percent); and textiles (80.2 percent).

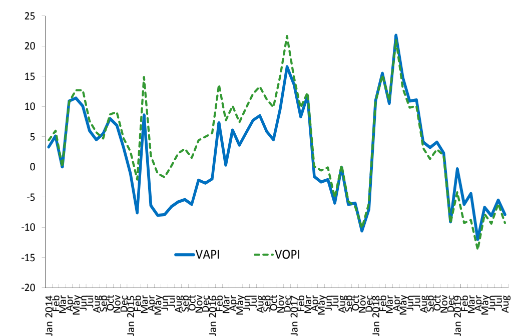
Volume and Value of Production. Preliminary results of the MISSI showed that volume of production index (VoPI) contracted by 9.3 percent year-on-year in August 2019 from a 6.1-percent (revised) slump in the previous month. Of the 20 major industries, seven (from six in July) posted contractions namely, petroleum products (-59 percent), electrical machinery (-11.1 percent), transport equipment (-19 percent), beverages (-8.4 percent), miscellaneous manufactures (-17.7 percent), furniture and fixtures (-43.4 percent), and textiles (-3.6 percent).

Manufacturing output declines

Factory output – as measured by the VoPI – declined due to the weak performance of heavily-weighted industries such as petroleum, furniture and fixtures, transport equipment, electrical machinery, beverages, and miscellaneous manufactures. By contrast, construction-related manufactures grew owing to the construction of new cement plants and in part due to the government's infrastructure spending. NEDA noted that the manufacturing sector will benefit from the implementation of infrastructure projects as transport and logistics will likely improve, despite the less optimistic business outlook brought about by global economic uncertainties.

At the same time, domestic demand is seen to be more favorable for the sector in Q3 2019 as production of consumer goods, i.e. food and beverages, tobacco, footwear and wearing apparel, and furniture and fixtures are expected to increase. Furthermore, the adoption of digital solutions and the amendment of the Foreign Investment Act of 1991, which aims to reduce logistical bottlenecks to encourage expansion of market access and improve labor productivity, will also bode well with the sector in the long-run.

Chart 15. Volume and Value Indices of Manufacturing Production
year-on-year in percent



Source: PSA

Likewise, the value of production index (VaPI) posted a 7.9-percent slump in August 2019 from a 5.5-percent contraction a month-ago. This was attributed to the following sub-sectors: petroleum products (-61.8 percent); electrical machinery (-14.3 percent); transport equipment (-18.5 percent); miscellaneous manufactures (-14 percent); beverages (-5.3 percent); textiles (-6.8 percent); furniture and fixtures (-6.6 percent); footwear and wearing apparel (-1.4 percent); and paper and paper products (-0.3 percent).

Business Expectations. Business outlook on the economy turned less optimistic for Q3 2019, with the overall confidence index (CI)[17] of the Business Expectations Survey (BES)[18] falling to

[17] The CI is computed as the percentage of firms that answered in the affirmative less the percentage of firms that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.
[18] The BES is a quarterly survey of a random sample drawn from the combined list of firms from the Securities and Exchange Commission's (SEC) Top 7,000 Corporations in 2010 and

37.3 percent from 40.5 percent in the previous quarter (Table 8). This means that the number of optimists declined but continued to be greater than the number of pessimists during the quarter.

Business outlook is less optimistic in Q3 2019 but turns more upbeat in Q4 2019

Respondents attributed their weaker sentiment during Q3 2019 to: (a) seasonal factors such as slack in the demand and slowdown of business activities during the rainy season; (b) decline in orders leading to lower sales; (c) lack of supply of raw materials; (d) perceived unfavorable effects of various government policies such as the rice tariffication law and the ban of provincial buses on EDSA, and (e) stiffer competition.

The sentiment of businesses in the Philippines mirrored the less buoyant business outlook in Bulgaria, Croatia, Germany, India, and Norway. By contrast, business sentiments in Australia, Brazil, Canada, Chile, France, Greece, Hungary, Israel, and Ukraine were more optimistic.

Table 8. Business Expectations Survey

BUSINESS OUTLOOK INDEX		Current Quarter	Next Quarter
2016	Q1	41.9	49.6
	Q2	48.7	45.3
	Q3	45.4	56.8
	Q4	39.8	34.5
2017	Q1	39.4	47.2
	Q2	43.0	42.7
	Q3	37.9	51.3
	Q4	43.3	39.7
2018	Q1	39.5	47.8
	Q2	39.3	40.4
	Q3	30.1	42.6
	Q4	27.2	29.4
2019	Q1	35.2	52.0
	Q2	40.5	47.6
	Q3	37.3	56.1

Source: BSP

However, for the quarter ahead (Q4 2019), business outlook turned more upbeat as the next quarter CI rose to 56.1 percent from 47.6 percent in the previous quarter. The positive outlook for the next quarter was due to expectations of: (a) higher consumer demand during the holiday and harvest seasons; (b) continued increases in orders and projects; (c) more favorable macroeconomic conditions (i.e., lower inflation, stable exchange rate, and lower interest rate); (d) higher government spending; and (e) business expansion.

Consumer Expectations. The overall confidence index (CI)[19] of the Consumer Expectations Survey (CES)[20] for Q3 2019 rebounded to positive territory at 4.6 percent from -1.3 percent from Q2 2019 (Table 9). The positive index indicates that optimists outnumbered the pessimist for Q3 2019.

Consumer confidence reverts to positive territory

The positive consumer outlook for Q3 2019 was attributed to expectations of: (a) improvements in the peace and order situation; (b) availability of more jobs; (c) additional and high income; and (d) good governance.

Table 9. Consumer Expectations Survey

CONSUMER OUTLOOK INDEX		Current Quarter	Next 3 Months	Next 12 Months
2016	Q1	-5.7	9.1	25.4
	Q2	-6.4	5.6	26.6
	Q3	2.5	27.3	43.8
	Q4	9.2	18.8	33.4
2017	Q1	8.7	16.5	31.7
	Q2	13.1	13.6	34.3
	Q3	10.2	17.8	33.7
	Q4	9.5	17.5	32.0
2018	Q1	1.7	8.8	24.0
	Q2	3.8	8.7	23.1
	Q3	-7.1	3.8	13.0
	Q4	-22.5	-0.8	10.7
2019	Q1	-0.5	10.7	28.4
	Q2	-1.3	9.7	25.2
	Q3	4.6	15.8	29.8

Source: BSP

BusinessWorld's Top 1,000 Corporations in 2017. The Q3 2019 BES was conducted during the period 10 July - 10 September 2019.

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

[20] The CES is a quarterly survey of a random sample of around 5,000 households in the Philippines. The Q3 2019 CES was conducted during the period 1 - 13 July 2019.

The improved outlook of consumers in the Philippines for Q3 2019 was similar to those in Australia, Czech Republic, France, and Italy. Meanwhile, consumers in Japan, South Korea, Thailand, and the United States registered more pessimistic sentiments.

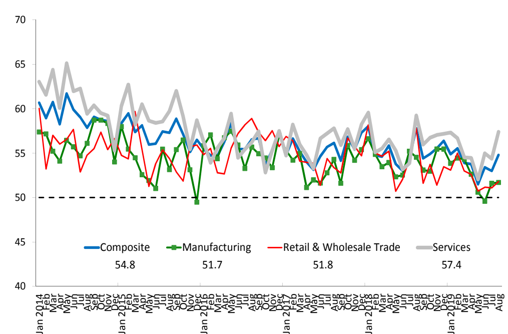
For the next quarter (Q4 2019) and the year ahead, consumers felt more upbeat as the CIs rose to 15.8 percent (from 9.7 percent a quarter ago) and 29.8 percent (from 25.2 percent in the previous quarter's survey results), respectively.

Furthermore, the respondents' more buoyant sentiment for the next quarter and the year ahead stemmed from households' anticipation of: (a) availability of more jobs; (b) additional and high income; (c) good governance; and (d) stable prices of goods.

Purchasing Managers' Index.[21] The composite PMI in August 2019 remained above the 50-point expansion threshold[22] at 54.8, higher than the July PMI at 53. This may be attributed to the faster expansion of all the sectors in review, with the services sector posting the biggest increment.

PMI remains firmly above the 50-point expansion threshold

Chart 16. Purchasing Managers' Index



Source: Philippine Institute of Supply Management (PISM)

The manufacturing PMI rose marginally by 0.1 index point to 51.7 in August 2019 from 51.6 in June, contrary with respondents' expectations of a deceleration during the month. The sector's minimal upturn was mainly a result of firms' early preparations ahead of the upcoming holiday season. In particular, survey respondents noted robust demand, higher orders and production activities, as well as project expansions as contributors to the sector's growth. This is evident mainly in the faster expansion of the New Orders Index, Employment Index, and a steady Supplier Deliveries Index. By contrast, Production and Inventories Indices decelerated. Meanwhile, all exporting firms posted slower expansions in August, except those with export volume of 26-50 percent of their total revenues which contracted during the month. Non-exporting firms expanded at a faster rate in August. On a per sector basis, six out of 12 subsectors grew at a faster pace namely, fuel and fuel products (59), communication and medical equipment (50.9), fabricated metal (53.8), food and beverages (50.7), motor vehicles (59.3), and basic metals (55.5). Rubber and plastic, textiles, and machinery decelerated, while the following posted a contraction: publishing, non-metallic minerals, and paper and paper products. Prospects are assessed to be favorable for the manufacturing sector in September.

Similarly, the services PMI increased by 3.0 index points to 57.4 from 54.4, which is contrary to business managers' expectations of a slowdown in August. Firms attributed the sector's growth to market factors such as stronger demand for services, additional clients, and launch of new projects. This is evident in the faster expansion of all the indices, notably Business Activity Index, New Orders Index, and Outstanding Business Index. At the same time, all the variables in review remained well above the 50-point expansion threshold. On a per sector basis, six of the 13 subsectors expanded faster in August (construction; health and social work; miscellaneous business activities; rental of goods and equipment; education; and electricity, gas, and water). Four subsectors expanded at a slower rate (business and knowledge process management; transportation with travel agency; real estate; and banking and financial intermediation), while the other three subsectors posted contraction (provident/insurance, hotels and restaurants, and postal and telecommunications). Survey respondents expect the sector to accelerate next month.

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

[22] 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.

The retail and wholesale PMI also went up by 0.6 index point to 51.8 in August 2019 from 51.1 in the previous month, which is contrary to managers' expectations of a lackluster performance for the sector. Respondents attributed the slight expansion mainly to strong demand as evident in the higher PMIs of the Sales Revenue Index and Inventories Index. The growth of the Supplier Deliveries Index suggested efficient delivery of goods amid robust demand and problematic traffic congestion. These marginally offset the slowdown of Purchases Index and the contraction of Employment Index. Meanwhile, the PMI of the retail subsector decreased by 2.85 index points to 54.15 in August from 57 in July as the higher PMIs of Sales Revenues and Inventories were offset by the declines of Purchases, Employment, and Supplier Deliveries. By contrast, the PMI of the wholesale subsector increased significantly to 54.96 from 48.05 brought about by the faster growth of all the indices, except the Supplier Deliveries Index. Managers are anticipating an expansion in the month ahead.

External Demand[23]

Exports. Exports of goods rose by 1.8 percent y-o-y in Q2 2019, higher than the 2.9-percent contraction in Q1 2019 and the 1.2-percent expansion in Q2 2018 (Table 10).

Exports of goods increase

The expansion in exports during the period was due mainly to higher foreign shipments of sugar and products, fruits and vegetables, forest products, mineral products, and manufactures.

Table 10. Exports of Goods
growth rate in percent

COMMODITY GROUP	2018	2019	
	Q2	Q1	Q2
Coconut Products	-6.3	-28.7	-4.7
Sugar and Products	-71.8	-55.2	91.0
Fruits and Vegetables	-12.7	43.1	39.1
Other Agro-Based Products	0.3	-3.8	-13.2
Forest Products	81.9	51.8	36.5
Mineral Products	-15.1	4.9	12.3
Petroleum Products	35.4	-26.7	-92.6
Manufactures	2.6	-4.0	1.4
Special Transactions	36.7	-1.2	-24.1
Total Exports	**1.2**	**-2.9**	**1.8**

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

[23] International Merchandise Trade Statistics (IMTS) concept

Imports. Imports of goods went down by 5.9 percent y-o-y in Q2 2019, a turnaround from the 4.7-percent growth in Q1 2019 and the 24.9-percent expansion in Q2 2018 (Table 11). The contraction in inward shipments during the period was due largely to lower imports of capital goods, raw materials and intermediate goods, mineral fuels and lubricant, and consumer goods.

Imports of goods decline

Table 11. Imports of Goods
growth rate in percent

COMMODITY GROUP	2018	2019	
	Q2	Q1	Q2
Capital Goods	14.2	11.5	-0.8
Raw Materials and Intermediate Goods	29.0	-0.9	-14.4
Mineral Fuels and Lubricants	49.5	-5.2	0.0
Consumer Goods	20.5	12.0	-0.1
Special Transactions	62.7	31.5	46.3
Total Imports	**24.9**	**4.7**	**-5.9**

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

Aggregate Supply. On the production side of the economy, growth emanated largely from the services sector, which contributed 4.2 ppts. Meanwhile, the industry and AHFF sectors contributed 1.3 ppts and close to 0 ppt, respectively.

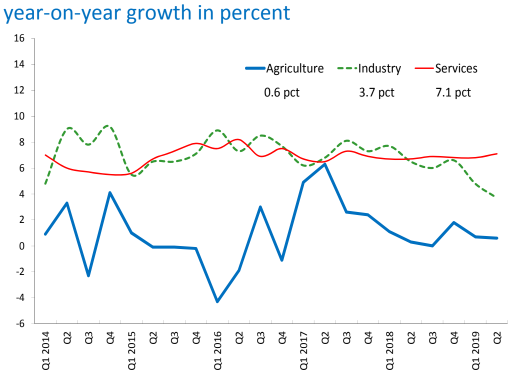
Services sector supports supply-side growth

The services sector posted a strong growth of 7.1 percent in Q2 2019, the highest since Q4 2017 (Table 12). Growth was buoyed mainly by the expansion in the following sub-sectors: a) trade and repair of motor vehicles, motorcycles, personal and household goods; b) other services; and c) real estate, renting and business activities sub-sectors. However, this growth was dampened by the slower growth in: a) financial intermediation; b) transport, storage and communication; and c) public administration and defense.

The robust performance in the trade and repair of motor vehicles, motorcycles, personal and household goods may be attributed to the improvement in both the maintenance and repair of motor vehicles, motorcycles, personal and household goods and retail trade. Meanwhile, the growth of other services was due to expansion in: a) hotels and restaurants; b) other service activities; c) sewage and refuse disposal sanitation and similar activities; and d) education. Lastly, the acceleration in real estate, renting and business activities was due to the higher demand for office property, mainly driven by offshoring and outsourcing, offshore gaming and pharmaceutical companies, while high demand for residential properties was buoyed up by corporate housing, investors and other end-users.

The industry sector growth decelerated to 3.7 percent in Q2 2019 from 4.8 percent in Q1 2019. The main contributor to industry slowdown was the decline in construction which contracted by 0.6 percent in Q2 2019 (from 5.4 percent growth in Q1 2019). The drop in the public construction outweighed the double-digit growth in the private construction at 23.1 percent. Public construction contracted due to the delayed passage of the 2019 national budget and the election ban, both of which affected public infrastructure projects.

Chart 17. Gross Domestic Product by Industrial Origin (at constant prices)
year-on-year growth in percent



Source: PSA

The manufacturing sector grew in moderation by 4.0 percent in Q1 2019 due to the deceleration in growth of food manufactures, and chemical and chemical products. Moreover, the slowdown in household consumption as well as weaker export growth in Q2 2019 also contributed to the slowdown in the manufacturing sub-sector.

Table 12. Gross Domestic Product by Industrial Origin
at constant 2000 prices; growth rate in percent

BY INDUSTRIAL ORIGIN	2018	2019	
	Q2	Q1	Q2
Agri., Hunting, Forestry and Fishing	0.3	0.7	0.6
Agriculture and Forestry	0.3	0.6	0.1
Fishing	0.4	1.4	3.1
Industry Sector	6.5	4.8	3.7
Mining and Quarrying	-5.4	4.7	15.0
Manufacturing	5.7	4.9	4.0
Construction	13.0	5.4	-0.6
Electricity, Gas and Water Supply	4.1	3.1	7.5
Service Sector	6.7	6.8	7.1
Transport, Storage and Communication	6.0	7.6	5.5
Trade and Repair of Motor Vehicles, Motorcycles, Personal and Household Goods	6.0	7.3	8.5
Financial Intermediation	7.6	10.2	9.2
Real Estate, Renting and Business Activities	4.5	3.7	4.0
Public Administration and Defense; Compulsory Social Security	15.0	9.7	8.0
Other Services	6.8	5.3	7.8

Source: PSA

On the contrary, double-digit growth was observed in mining and quarrying (15.0 percent in Q2 2019 from 4.7 percent in Q1 2019), while the utilities sub-sector accelerated (7.5 percent in Q2 2019 from 3.1 percent in Q1 2019). The surge in mining and quarrying was supported by the rebound in the growth of other non-metallic mining and the acceleration of crude oil, natural gas and condensate. Meanwhile, the faster growth in the utilities sub-sector was a result of the higher growth in electricity as Meralco reported revenue growth at 10 percent in the first semester of 2019 compared to the same period in 2018.

The AHFF sector slightly decelerated to 0.6 percent growth from the 0.7 percent growth in Q1 2019. This was due to the further drop in palay production (at -5.5 percent from -4.5 percent in Q1 2019) and the contraction in sugarcane production to 35.8 percent (from 14.6 percent in Q1 2019). This may be the result of the El Niño phenomenon experienced in the first half of the year.

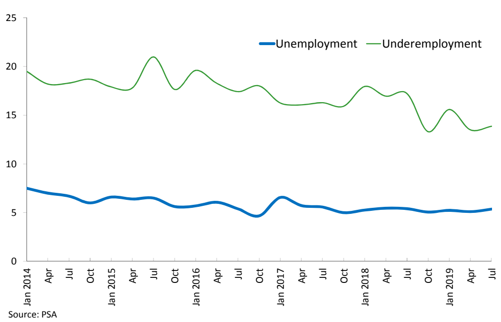
Labor Market Conditions

The Philippine labor market was fairly steady in the third quarter of 2019 as major indicators for both quantity and quality of employment posted mixed results.

Labor market shows mixed results

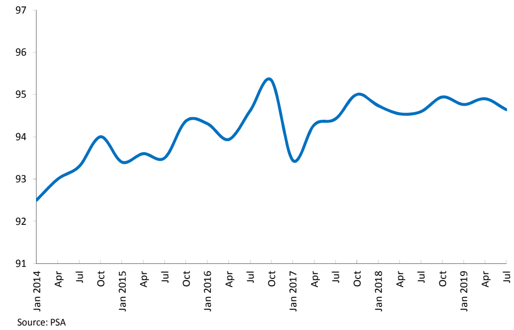
Compared to the July 2018 survey round, the results of the July 2019 round of the labor force survey (LFS) showed that the country's employment and unemployment rates remained steady at 94.6 percent and 5.4 percent, respectively. Meanwhile, the underemployment rate declined to 13.9 percent from 17.2 percent, while youth unemployment rate increased to 14.4 percent from 14.1 percent. The y-t-d youth unemployment rate stood at 13.8 percent, higher relative to the 9.8-percent target of the government for 2019. This is in contrast to the 5.2-percent average unemployment rate in the first three quarters of 2019, which is within the 4.3 to 5.3 percent government target for the year.

Chart 18. Unemployment and Underemployment
in percent



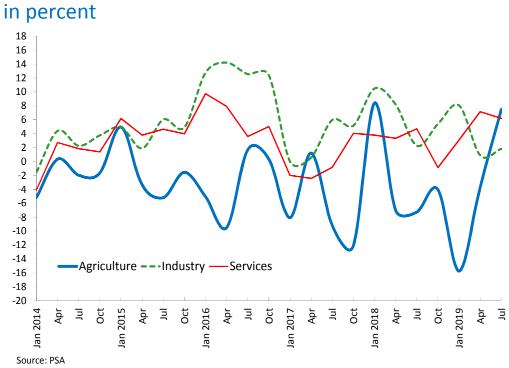
The steady employment rate at 94.6 percent in July 2019 is equivalent to 43.0 million employed individuals. The survey indicated an employment gain of 2.3 million or 5.7 percent higher compared to 40.6 million employed persons in the same period a year ago.

Chart 19. Employment Rate
in percent



Employment gains were recorded in all major sectors of the economy, led by the services and agriculture sectors. Employment in the services sector increased by 6.1 percent to 24.8 million, mainly due to wholesale and retail trade, accommodation and food service activities, as well as public administration and defense. The latter may indicate the start of improvement in public spending, which decelerated in the first half of the year due to the delay in the passage of the government budget.

Chart 20. Employment by Sector
in percent



Employment in the agriculture sector rose by 7.6 percent, bringing to an end the five consecutive quarters of decline in employment in the said sector, mainly caused by adverse weather conditions. Meanwhile, employment growth in the industry sector was recorded at 1.9 percent due to weak growth in manufacturing and decline in water supply, sewerage and waste management subsectors. Employment in construction was the main contributor to the growth of employment in industry, as it posted a faster growth compared to the same period last year. This supports the view that public construction has started gaining momentum in the third quarter of 2019.

Meanwhile, the latest unemployment rate at 5.4 percent is the lowest recorded by the country for all surveys conducted in the July rounds since 2006, although the said rate was already achieved in 2016 and 2018. Notwithstanding, the unemployment level rose by 4.4 percent, equivalent to 103 thousand more unemployed individuals in July 2019. In terms of highest grade completed, majority of the unemployed are college graduates (30.2 percent share) and junior high school graduates (25.2 percent). In terms of age, the bulk belongs to the 15-24 age group or the youth (45.5 percent), followed by 25-34 years old (33.2 percent). The number of unemployed youth increased by 6.3 percent during the period.

The quality of employment significantly improved as underemployment rate dropped from 17.2 percent to 13.9 percent. This is equivalent to 1.0 million reduction in the number of employed individuals who wanted more work compared to July 2018. Similar to unemployment rate, this underemployment rate in July 2019 is the lowest achieved by the country for all surveys conducted in the July rounds since 2006. However, other aspects of quality of employment did not improve during the period. This is evidenced by lower share of remunerative work or wage and salary workers (63.4 percent in July 2019 from 65.3 percent a year ago) and the decline in overall mean hours of work (hours per week) from 43.0 in July 2018 to 41.6 in July 2019, which could still indicate slower economic activities in the third quarter of 2019.

To further improve the employment condition in the country, the government recognizes the need to increase employment opportunities, particularly for the youth by continually improving their knowledge and skills through technical vocational training, promoting apprenticeship and on-the-job training.[24]

[24] NEDA (2019), "PH Employment Numbers Continue to Improve in July 2019," 5 September.

II. Monetary and Financial Market Conditions

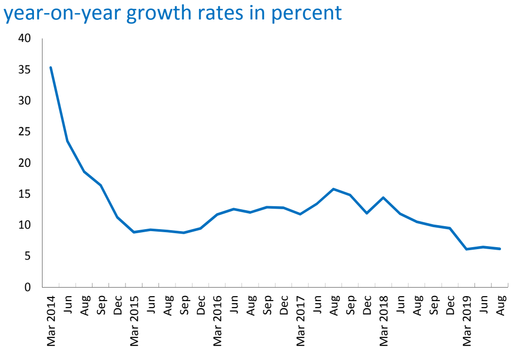
Domestic Liquidity

Domestic liquidity (M3) grew by 6.2 percent y-o-y in August 2019 to ₱11.9 trillion, slightly slower than the 6.5-percent (revised) expansion as of end-Q2 2019.

Domestic liquidity expands

Money supply continued to increase due mainly to sustained demand for credit. Domestic claims grew by 6.2 percent in August, the same rate of expansion posted as of end-Q2 2019 due to the sustained growth in credit to the private sector. Meanwhile, net claims on the central government expanded by 2.1 percent in August, a reversal from the 3.9-percent (revised) contraction in end-Q2 2019.

Chart 21. Domestic Liquidity
year-on-year growth rates in percent



Source: BSP

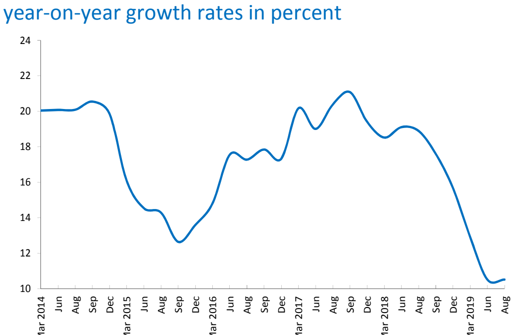
Net foreign assets (NFA) in peso terms grew by 8.9 percent y-o-y in August from a growth of 4.4 percent (revised) in end-Q2 2019 as the NFA position of the BSP and banks improved during the month. The BSP's NFA position continued to expand in August, supported by foreign exchange inflows coming mainly from overseas Filipinos' remittances and business process outsourcing receipts. On the other hand, the NFA of banks increased as their foreign assets grew as a result of higher loans and investments in marketable debt securities.

Outstanding loans of commercial banks, net of reverse repurchase (RRP) placements with the BSP, increased by 10.5 percent y-o-y in August 2019, similar with the 10.5-percent growth rate posted at end-Q2 2019 but slower than the 17.6-percent growth rate recorded in end-Q3 2018.

Bank lending sustains growth

The sustained increase in bank lending was largely due to loans for production activities, which expanded by 9.0 percent y-o-y in August 2019 from 9.8 percent in end-Q2 2019 and 17.4 percent in end-Q3 2018. The expansion in production loans was driven primarily by increased lending to the following sectors: real estate activities; financial insurance activities; electricity, gas, steam and air conditioning supply; construction; and wholesale and retail trade.

Chart 22. Loans Outstanding of Commercial Banks
year-on-year growth rates in percent



Source: BSP

Meanwhile, loans for household consumption grew by 25.4 percent in August 2019, higher than the 15.3-percent growth and 18.2-percent expansion in end-Q2 2019 and end-Q3 2018, respectively.

Monetary Operations

As of end-Q3 2019, majority of the BSP's liquidity-absorbing monetary operations had been through the overnight reverse repurchase (RRP) facility, comprising about 54.1 percent of total outstanding amount of liquidity absorbed in BSP liquidity facilities. Meanwhile, the combined placements in the overnight deposit facility (ODF) and the term deposit facility (TDF) made up the remaining 45.9 percent.

Consistent with the BSP's assessment of prevailing liquidity conditions and taking into account lower NG deposits with the BSP as well as the last tranche of the reserve requirement reduction effective on 26 July 2019, the average weekly total offer volumes for the TDF auctions was higher at about ₱74.6 billion in Q3 2019 relative to the ₱35.4 billion average weekly volume offered in the previous quarter. The average bid-to-cover ratios for the 7-day, 14-day, and 28-day tenors were recorded at 1.4, 1.3, and 1.3 compared to 1.4, 1.5, and 0.8, respectively, in the previous quarter. Meanwhile, the average bid-to-cover ratio for the daily RRP offerings was higher at around 1.1 during the quarter from 0.9 in Q1 2019.

Credit Conditions

Credit Standards. Results of the Q3 2019 Senior Bank Loan Officers' Survey (SLOS) showed that most of the respondent banks continued to maintain their overall credit standards for loans to both enterprises and households during the quarter based on the modal approach.[25]

Majority of banks keep credit standards steady

This is the 42nd consecutive quarter since Q2 2009 that the majority of respondent banks reported broadly unchanged credit standards.

The diffusion index (DI) approach,[26,27] meanwhile, continued to indicate a net tightening of credit standards for loans to enterprises while credit standards for loans to households were unchanged. In the previous quarter, credit standards for loans to both enterprises and households showed a net tightening based on the DI approach.

Lending to Enterprises. Most banks (81.6 percent of banks that responded to the question) indicated that they maintained their credit standards for loans to enterprises during the quarter using the modal approach (Table 13).

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

	2017				2018				2019		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Tightened Considerably	0.0	0.0	0.0	0.0	0.0	3.6	2.3	6.7	2.1	4.8	4.1
Tightened Somewhat	6.7	10.0	7.4	3.7	3.7	10.7	18.6	20.0	22.9	11.9	12.2
Remained Basically Unchanged	**93.3**	**90.0**	**88.9**	**88.9**	**92.6**	**82.1**	**76.7**	**71.1**	**72.9**	**81.0**	**81.6**
Eased Somewhat	0.0	0.0	3.7	7.4	3.7	3.6	0.0	0.0	0.0	0.0	0.0
Eased Considerably	0.0	0.0	0.0	0.0	0.0	0.0	2.3	2.2	2.1	2.4	2.0
Total	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	**6.7**	**10.0**	**3.7**	**-3.7**	**0.0**	**10.7**	**18.6**	**24.4**	**22.9**	**14.3**	**14.3**
Number of Banks Responding	**30**	**30**	**27**	**27**	**27**	**28**	**43**	**45**	**48**	**42**	**49**

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

Meanwhile, results based on the DI approach pointed to a net tightening of credit standards for the quarter, which was attributed by respondent banks largely to their perception of a deterioration in the profile of borrowers, their reduced tolerance for risk, and less aggressive competition from banks and non-bank lenders. In terms of specific credit standards, the net tightening of overall credit standards was reflected in reduced credit line sizes; stricter collateral requirements and loan covenants; shortened loan maturities; and increased use of interest rate floors.

Banks' responses likewise pointed to a net tightening of credit standards across all borrower firm sizes, namely, top corporations, large middle-market enterprises, small and medium enterprises (SMEs) and micro-enterprises based on the DI approach.

Over the next quarter, results based on the modal approach showed that most of the respondent banks expect credit standards to remain unchanged. At the same time, results based on the DI approach indicated expectations of unchanged credit standards given the equal percentages of respondent banks that anticipate tightening and easing of overall credit standards for business

[25] In the modal approach, the results of the survey are analyzed by looking at the option with the highest share of responses.
[26] In the DI approach, a positive DI for credit standards indicates that the proportion of respondent banks that have tightened their credit standards exceeds those that eased ("net tightening"), whereas a negative DI for credit standards indicates that more respondent banks have eased their credit standards compared to those that tightened ("net easing").
[27] During the Q1 2010 to Q4 2012 survey rounds, the BSP used the diffusion index (DI) approach in the analysis of survey results. Beginning in Q1 2013, the BSP used both the modal and diffusion index (DI) approaches in assessing the results of the survey.

loans. Respondent banks attributed their anticipation of unchanged overall credit standards to their stable economic outlook and expectations of no changes in terms of tolerance for risk, among other factors.

Lending to Households. The results of the survey likewise indicated that most respondent banks (81.3 percent) kept their overall credit standards unchanged for loans extended to households during the quarter based on the modal approach (Table 14). Similarly, results based on the DI approach reflected unchanged credit standards for household loans given the equal percentages of respondent banks that reported tightening and easing of overall credit standards during the quarter.

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

	2017				2018				2019		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Tightened Considerably	0.0	0.0	0.0	0.0	0.0	0.0	6.3	10.7	3.3	4.0	3.1
Tightened Somewhat	0.0	9.1	5.0	0.0	15.8	5.9	12.5	7.1	16.7	8.0	6.3
Remained Basically Unchanged	**100.0**	**81.8**	**90.0**	**90.5**	**78.9**	**94.1**	**75.0**	**78.6**	**73.3**	**88.0**	**81.3**
Eased Somewhat	0.0	9.1	5.0	9.5	5.3	0.0	6.3	3.6	3.3	0.0	9.4
Eased Considerably	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	3.3	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
Diffusion Index for Credit Standards	**0.0**	**0.0**	**0.0**	**-9.5**	**10.5**	**5.9**	**12.5**	**14.3**	**13.3**	**12.0**	**0.0**
Number of Banks Responding	**21**	**22**	**20**	**21**	**19**	**17**	**32**	**28**	**30**	**25**	**32**

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

The overall unchanged credit standards for household loans was attributed by respondent banks largely to their steady tolerance for risk and unchanged profile of banks' borrowers.

In terms of respondent banks' outlook for the next quarter, results based on the modal approach showed that the majority of the respondent banks anticipate maintaining their overall credit standards. Meanwhile, DI-based results indicated expectations of overall net tightening of credit standards for household loans as respondent banks anticipate a deterioration in profitability of banks' portfolios and a lower tolerance for risk.

Loan demand. Responses to the survey question on loan demand indicated that the majority of respondent banks continued to see stable overall demand for loans from both enterprises and households during the quarter.

Demand for loans from firms and households remains stable

Meanwhile, results based on the DI approach showed a net increase in overall demand[28] for business loans (across all firm sizes) and household loans (except for housing and auto loans, which showed a net decrease). The overall net increase in loan demand from firms was attributed by banks largely to their customers' higher working capital requirements. Meanwhile, respondent banks attributed the overall net increase in household loan demand to higher household consumption and banks' more attractive financing terms.

Over the next quarter, most of respondent banks expect steady overall loan demand from firms and households. However, DI-based results suggested expectations of a net increase in overall loan demand for both business and household loans. For business loans, the expected net increase in demand was associated largely with corporate clients' higher working capital requirements. Meanwhile, the anticipated net increase in loan demand from households was attributed to expectations of higher household consumption, lower interest rates, and more attractive financing terms offered by banks.

Real Estate Loans. Most of the respondent banks (93.8 percent) reported that overall credit standards for commercial real estate loans were maintained in Q3 2019.

Majority of banks maintain credit standards for real estate loans

The DI approach, however, continued to point to a net tightening of overall credit standards for commercial real estate loans for the 15th consecutive quarter, which was attributed largely to reduced tolerance for risk and deterioration in the liquidity of banks' portfolios. The net tightening of overall credit standards for commercial real estate loans reflected respondent banks' wider loan margins; reduced credit line sizes; stricter collateral requirements and loan covenants; shortened loan maturities; and increased use of interest rate floors. Over the next

[28] The "DI for loan demand" refers to the percentage difference between banks reporting an increase in loan demand and banks reporting a decrease. A positive DI for loan demand indicates that more banks reported an increase in loan demand compared to those stating the opposite, whereas a negative DI for loan demand implies that more banks reported a decrease in loan demand compared to those reporting an increase.

quarter, while most of the respondent banks anticipate maintaining their credit standards for commercial real estate loans, DI-based results point to expectations of continued net tightening of overall credit standards for the said type of loan.

Demand for commercial real estate loans was also unchanged in Q3 2019 based on the modal approach. However, DI-based results showed a net decrease in demand for commercial real estate loans for the third consecutive quarter, which respondent banks attributed to lower working capital requirements and investment in plant or equipment of clients; increase in customers' internally generated funds; deterioration in economic outlook; availability of other sources of funds; banks' less attractive financing terms; and high interest rates. Over the next quarter, although most of the respondent banks anticipated generally steady loan demand, more banks expected demand for commercial real estate loans to increase compared to those expecting the opposite.

For housing loans extended to households, most of the respondent banks (88.5 percent) reported maintaining their credit standards, while the DI approach pointed to a slight net easing of overall credit standards, reflecting a net narrowing of loan margins and net increase in credit line sizes. The slight net easing of overall credit standards for housing loans was attributed to banks' more favorable economic outlook, more aggressive competition from banks and non-bank lenders, and increased tolerance for risk. Over the next quarter, results based on the modal approach showed that respondent banks expect overall credit standards for housing loans to remain unchanged. However, using the DI approach, survey results suggested expectations of a net tightening of credit standards for housing loans in Q4 2019 as respondent banks anticipate a deterioration in the profitability of banks' loan portfolio and a decline in risk tolerance.

Most banks reported unchanged demand for housing loans in Q3 2019 based on the modal approach while DI-based results pointed to a net decrease in demand for housing loans, which was attributed by respondent banks largely to high interest rates and less attractive financing terms offered by banks. Furthermore, banks' responses indicated expectations of a net increase in demand for housing loans over the next quarter supported largely by higher household consumption, lower interest rates, and more attractive financing terms offered by banks.

Interest Rates

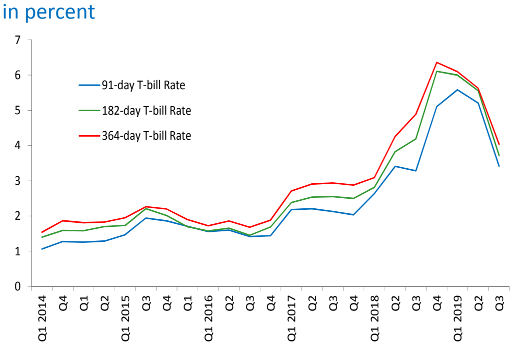
Primary Interest Rates

In Q3 2019, the average interest rates for the 91-, 182- and 364-day T-bills in the primary market decreased to 3.415 percent, 3.723 percent, and 4.040 percent from 5.204 percent, 5.552 percent, and 5.627 percent, respectively.

T-bill rates decrease further

The results of the auctions during the quarter reflected market players' strong demand for government securities amid expectations of policy rate cuts from the BSP and US Fed during the quarter on the back of easing inflation expectations as well as the continuing trade tension between the US and China. The appetite for government notes was driven as well by the three-phased 200-bp reduction in reserve requirements (i.e., 100 bps on 31 May, 50 bps on 28 June and 50 bps on 26 July) and the limited supply of T-bills in Q3 2019.

Chart 23. Treasury Bill Rates
in percent

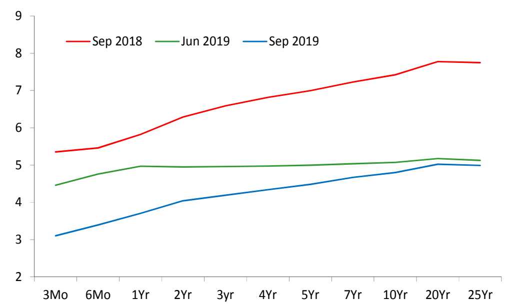


Yield Curve.[29] As of end-September 2019, the secondary market yield for government securities (GS) for all maturities declined relative to the end-June 2019 levels, as market players invested their excess liquidity and serviced their clients' requirements following the reductions in the BSP's key policy interest rates.

Yields for GS decline across all maturities

Debt paper yields were lower by a range of 13.5 bps for the 25-year GS to 136.6 bps for the 6-month GS compared to end-June 2019 levels.

Chart 24. Yields of Government Securities in the Secondary Market
in percent



Source: Bloomberg

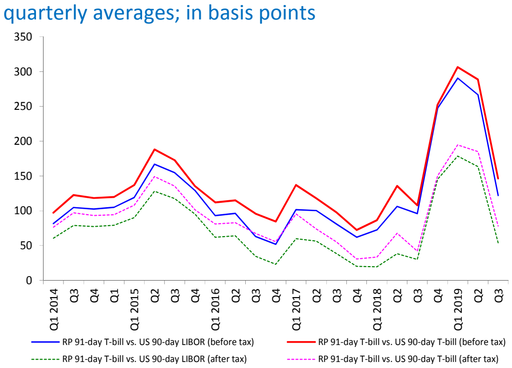
Relative to year-ago levels, the secondary market yields for GS for all maturities likewise decreased by a range of 206.7 bps (for the 6-month GS) to 275.6 bps (for the 25-year GS).

Interest Rate Differentials. The average differentials between domestic and US interest rates, gross and net of tax, narrowed further in Q3 2019 relative to the previous quarter.

Interest rate differentials narrow further in Q3 2019

The average 91-day RP T-bill rate declined q-o-q by 175.5 bps to 3.415 percent in Q3 2019 from 5.170 percent in Q2 2019. Likewise, the average US 90-day LIBOR and the US 90-day T-bill rate declined by 30.7 bps and 33.4 bps, respectively to 2.195 percent and 1.951 percent in Q3 2019. These developments led to narrower positive gross and net of tax differentials between the 91-day RP T-bill rate and US interest rates. Domestic and foreign interest rates fell following the reductions in the BSP's key policy interest and the US federal funds target rate during the quarter.

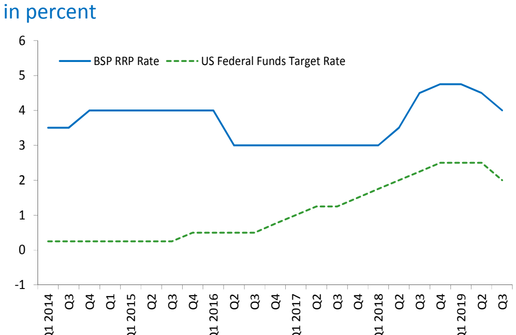
Chart 25. Interest Rate Differentials
quarterly averages; in basis points



Source: Bloomberg, BTr and BSP

The positive differential between the BSP's overnight borrowing or RRP rate and the US Fed funds target rate remained at a range of 200-225 bps in Q3 2019, reflecting the impact of the 50-bp cumulative decline in the BSP's overnight RRP rate to 4.25 percent on 8 August 2019 and 4.00 percent on 26 September 2019 and the 50-bp cumulative decline in the US federal funds target rate to 2.00-2.25 percent on 1 August 2019 and 1.75-2.00 percent on 19 September 2019.

Chart 26. BSP RRP Rate and US Federal Funds Target Rate
in percent

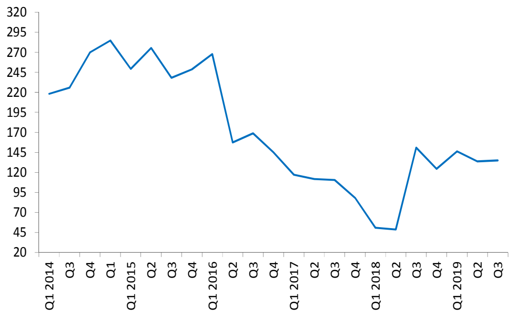


Source: Bloomberg and BSP

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

Meanwhile, the interest rate differential between the BSP's overnight RRP rate and the US Fed funds target rate adjusted for risk[30] widened slightly to 135 bps as of end-September 2019 from 134 bps in end-June 2019.

Chart 27. Risk-Adjusted Differentials
in basis points



Source: Bloomberg and BSP

This development could be traced to the 1-bp decline in the risk premium, following the 34.0-bp and 33.0-bp decline in the interest rates for the 10-year ROP note and the 10-year US Treasury note, respectively. The 10-year ROP note and the 10-year US Treasury note fell amid strong demand for safe-haven government bonds due to the continuing trade tensions between the US and China, expectations of a no-Brexit deal and heightened concerns over a possible global economic slowdown following the release of weaker-than-expected US data on consumer confidence, housing, employment gains, manufacturing and non-manufacturing activities.

Domestic real lending rate[31] rose to 5.1 percent in September 2019 from 3.7 percent in June 2019.

Real lending rate increases

The increase in domestic real lending rate was due to the 180.0-bp and 40.0-bp decline in inflation and actual bank lending rate[32], to 0.9 percent and 6.0 percent, respectively in September 2019.

[30] The difference between the 10-year ROP note and the 10-year US Treasury note is used as proxy for the risk premium.
[31] Real lending rate is measured as the difference between actual bank lending rate and inflation.
[32] The actual bank lending rate for the Philippines is the weighted average interest rate charged by reporting commercial banks on loans and discounts granted during the period.

Chart 28. Philippines' Real Lending Rate
in percent

Source: PSA and BSP

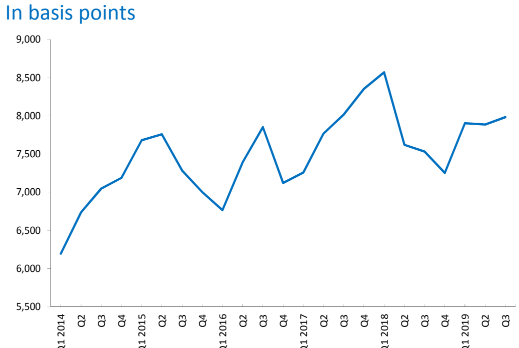
The Philippines' real lending rate at 5.1 percent in September 2019 is the fourth highest in a sample of 10 Asian countries, with Indonesia recording the highest real lending rate at 6.8 percent followed by India at 6.0 percent while Japan posted the lowest at 0.7 percent.

Financial Market Conditions

The domestic financial system remained stable, supported by firm macroeconomic fundamentals during the review quarter.

Stock Market. In the third quarter of 2019, the Philippine Stock Exchange index (PSEi) increased by 1.3 percent, quarter-on-quarter (q-o-q), to average at 7,988.57 index points.

Chart 29. Quarterly Average PSEi
In basis points



Source: Philippine Stock Exchange, BSP

The rise in the main index was supported mainly by the country's benign inflation environment which led to the BSP easing its monetary policy stance. Partly tempering the rally, however, was the slowdown in Philippine GDP growth in Q2 and the subdued global growth outlook arising from the continued trade tensions between the US and China.

Other external risk factors which continued to dampen trading sentiment include the following: potential impact on domestic inflation of the attack on Saudi Arabia's oil processing facilities,[33] rising political risk following the start of an impeachment inquiry against President Trump,[34] and reports that the White House is considering limits on US investment into China that could further aggravate the protracted trade dispute between the two countries.

Meanwhile, total market capitalization declined by 3.0 percent during the review period to close at ₱16.75 trillion in end-September from ₱17.26 trillion in end-June. This downtrend is attributed to the fall in four of the seven sectoral indices, namely industrials, services, property, and SME. Foreign investors also posted net outflows during the period with net sales of ₱16.9 billion, higher than the ₱11.4 net outflows registered in Q2. The price-earnings ratio for listed firms also trended lower from 19.4x in end-June to 17.5x in end-September.

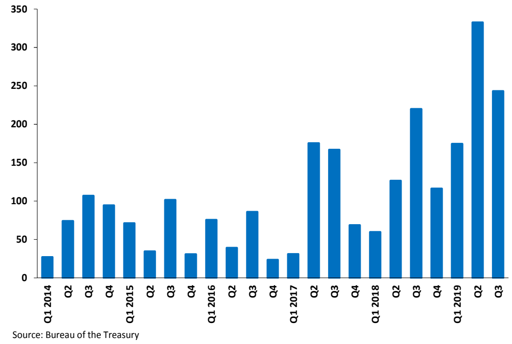
Government Securities. Results of the T-bill auctions conducted in July – September 2019 continued to show robust demand for short-term government securities with total subscription for the quarter amounting to around ₱333.0 billion or about 3.7 times the ₱90.0-billion aggregate offered amount.

Demand for T-bills continues to be strong

The oversubscription for Q3 2019, at ₱243.0 billion, was lower than the ₱332.5-billion oversubscription in the previous quarter. The Bureau of the Treasury (BTr) awarded in full the ₱4.0-billion, ₱5.0-billion and ₱6.0-billion offered amounts for the 91-, 182- and 364-day T-bills in all T-bill auctions during the quarter, except for the auction on 16 September.

[33] Oil prices surged following news of a drone attack on Saudi Arabia's oil facilities during the weekend of 14 September, which was estimated to have cut five percent of the world's oil supply or about 5.7 million barrels per day (mb/d).
[34] House Speaker Nancy Pelosi said on 24 September that the US House of Representatives was moving forward with an official impeachment inquiry on President Trump after his admission that he asked a foreign leader to investigate 2020 rival Joe Biden, am action that seriously violated the Constitution.

Chart 30. Total Oversubscription of T-bill Auctions



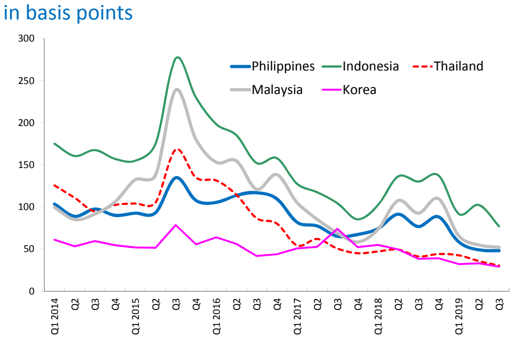
Results of the T-bond auctions during the quarter likewise showed strong demand for T-bonds.

Sovereign Bond and Credit Default Swap (CDS) Spreads. The country's 5-year sovereign CDS spreads as of end-September was at 48 bps, slightly higher from the end-June level of 47 bps.

Debt spreads widen slightly due to uncertainties on the external front

Against other neighboring economies, the Philippine CDS traded lower than Malaysia's 52 bps and Indonesia's 91 bps but was wider compared to Thailand's 29 bps and Korea's 33 bps.

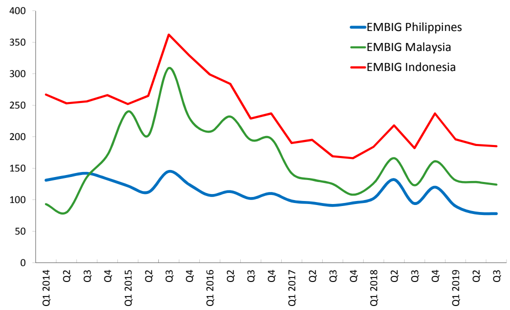
Chart 31. 5-Year CDS Spreads of Selected ASEAN Countries
in basis points



Debt spreads widened given the continued absence of a Brexit deal; imposition of additional duties on some $550-billion worth of targeted Chinese goods by the US; and retaliatory new tariffs imposed by China on $75-billion worth of US goods. On the domestic front, the lower-than-expected Q2 GDP figure of 5.5 percent negatively affected investor sentiment.

Meanwhile, the risk premium from holding a Philippine sovereign bond over a similarly tenured US Treasury bond or the Emerging Market Bond Index Global (EMBIG) for the Philippines declined to 78 bps as of 30 September 2019 from the end-June level of 79 bps.

Chart 32. EMBIG Spreads of Selected ASEAN Countries
in basis points



Source: Bloomberg

Banking System

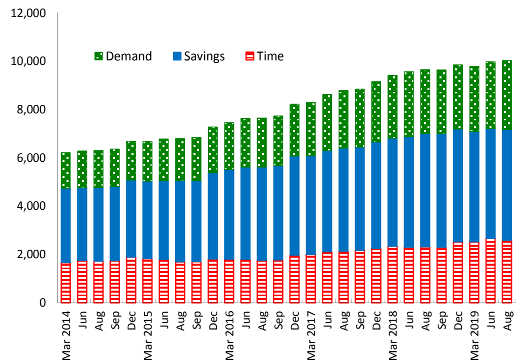
The Philippine banking system continued to lend support to the country's long-term economic growth and stable financial condition. During the second quarter of 2019, banks' balance sheets exhibited sustained growth in assets and deposits.

Philippine banking system exhibits stable growth in assets and deposits

Furthermore, asset quality indicators remained healthy while capital adequacy ratios continued to be above international standards, even with the implementation of the tighter Basel III framework.[35]

Savings Mobilization. Savings deposits remained the primary sources of funds for the banking system. Banks' total deposits as of end-August 2019 amounted to ₱10.0 trillion, 3.9 percent higher than the year-ago level.[36] Relative to the end-June 2019 level, total deposits increased slightly by 0.6 percent.

Chart 33. Deposit Liabilities of Banks
in billion pesos



Source: BSP

Meanwhile, foreign currency deposits owned by residents (FCD-Residents) reached ₱2.0 trillion as of end-August 2019, posting a y-o-y growth of 5.6 percent. With respect to the end-June 2019 level, FCD-Residents grew by 2.2 percent.[37]

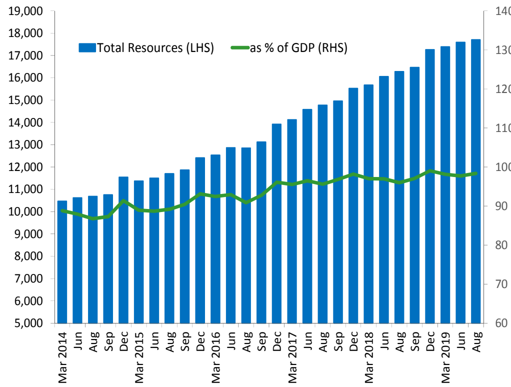
Institutional Developments. The total resources of the banking system grew by 8.8 percent to reach ₱17.7 trillion as of end-August 2019 from ₱16.3 trillion a year ago. Relative to the end-June 2019 level, total resources of the banking system increased slightly by 0.7 percent. As a percent of GDP, total resources stood at 98.4 percent.[38]

Total resources of the banking system continue to grow

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

[36] This refers to the total peso-denominated deposits of the banking system.
[37] FCD-Residents, along with M3, forms part of a money supply measure called M4. Meanwhile, M3 consists of savings deposits, time deposits, demand deposits, currency in circulation, and deposit substitutes.
[38] GDP as of the 2nd quarter of 2019.

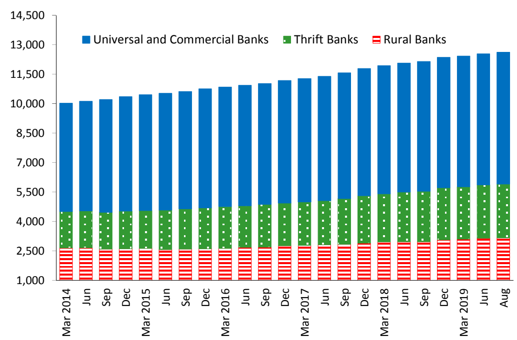
Chart 34. Total Resources of the Banking System
levels in billion pesos; share in percent



Source: BSP

The number of banking institutions (head offices) as of end-August 2019 decreased to 552 offices from 554 last end-June 2019. The banks' head offices are comprised of 46 universal and commercial banks (U/KBs), 50 thrift banks (TBs), and 456 rural banks (RBs).

Chart 35. Number of Banking Institutions



Source: BSP

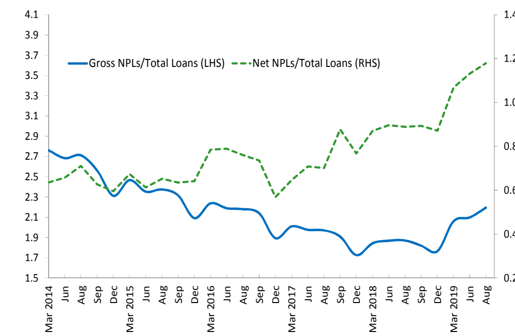
During the same period, the operating network (head offices and branches/agencies) of the banking system expanded to 12,618 offices from 12,543 offices last end-June 2019. The expansion was due mainly to the increase in the branches/agencies led by U/KBs and followed by RBs.

The Philippine banking system's gross non-performing loan (GNPL) ratio increased slightly to 2.2 percent as of end-August 2019 relative to the 1.9 percent registered a year ago and 2.1 percent as of end-June 2019.

Asset quality of Philippine banks remains healthy

Banks' initiatives to improve their asset quality along with prudent lending regulations helped maintain the GNPL ratio below its pre-Asian crisis level of 3.5 percent.[39] Similarly, net non-performing loan (NNPL) ratio grew moderately to reach 1.2 percent as of end-August 2019 from the previous year's ratio of 0.9 percent and the end-June 2019 ratio of 1.1 percent. In computing for the NNPLs, specific allowances for credit losses on Total Loan Portfolio (TLP) are deducted from the GNPLs. Said allowances increased slightly to ₱104.6 billion in August 2019 from ₱99.5 billion posted as of end-June 2019.[40]

Chart 36. Ratios of Gross Non-Performing Loans and Net Non-Performing Loans to Total Loans
in percent



Source: BSP

The Philippine banking system's GNPL ratio of 2.2 percent was higher with respect to that of Malaysia (1.0 percent) and South Korea (0.9 percent) but was lower than that of Indonesia (2.4 percent) and Thailand (3.0 percent).[41]

The loan exposures of banks remained adequately covered with the banking system's NPL coverage ratio at 91.7 percent as of end-August 2019. This was, however, lower than the previous year's and quarter's ratios of 114.2 percent and 93.3 percent, respectively.

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[39] The 3.5 percent non-performing loans (NPL) ratio was based on the pre-2013 definition.

[40] This type of provisioning applies to loan accounts classified under loans especially mentioned (LEM), substandard-secured loans, substandard-unsecured loans, doubtful accounts and loans considered as loss accounts.

[41] Sources: Malaysia (Banking System's Ratio of net impaired loans to net total loans, August 2019); South Korea (Domestic Banks' Substandard or Below Loans [SBLs] ratio, June 2019); Indonesia, IMF and financial stability report (Banks' Nonperforming Loans to Gross Loans Ratio, March 2019); and Thailand (Total Financial Institutions' Gross NPLs ratio, June 2019).

U/KBs' CAR remains above international and regulatory standards

The capital adequacy ratio (CAR) of U/KBs at end-June 2019, on solo basis, increased marginally to 15.3 percent from 15.1 percent as of end-March 2019. Similarly, on a consolidated basis, CAR of U/KBs increased to 16.0 percent from 15.8 percent registered a quarter ago. These figures remained well above the BSP's regulatory threshold of 10.0 percent and international standard of 8.0 percent.

Chart 37. Capital Adequacy Ratio of Universal and Commercial Banks

in percent

Source: BSP

The CAR of Philippine U/KBs, on consolidated basis was higher than that of South Korea (15.3 percent) but lower than those of Malaysia (17.7 percent), Thailand (18.7 percent) and Indonesia (23.3 percent).[42]

Exchange Rate

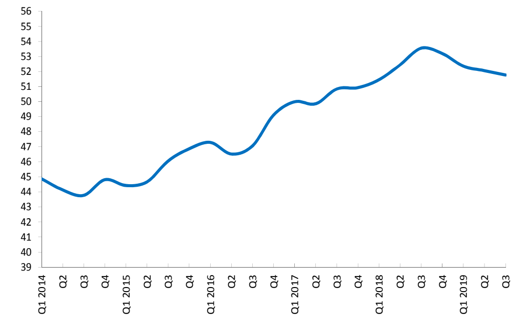
The peso averaged at ₱51.74/US$1 in Q3 2019, appreciating by 0.64 percent from the previous quarter's average of ₱52.07/US$1.

Peso strengthens on expectations of a US Fed rate cut

The peso's appreciation during the period was due mainly to market anticipation of interest rate reduction by the US Federal Reserve. On a y-o-y basis, the peso likewise appreciated by 3.48 percent relative to the ₱53.54/US$1 average in Q3 2018.[43]

Chart 38. Quarterly Peso-Dollar Rate

PHp/US$; average per quarter



Source: Reference Exchange Rate Bulletin, Treasury Department, BSP

In July, the peso averaged at ₱51.14/US$1, 1.29 percent higher than the ₱51.80/US$1 average in June. The peso's appreciation was amid renewed expectation of a US Federal Reserve rate cut following the release of weaker-than-expected US data on housing starts, new jobs and non-manufacturing sector growth for June 2019.

Meanwhile, in August, the peso depreciated to an average of ₱52.05/US$1, 1.75 percent lower than the average in July, amid the lingering trade conflict between the US and China.

In September, the peso depreciated further by 0.10 percent to an average of ₱52.11/US$1 from its average in August. The depreciation of the peso was due partly to safe haven buying following the attack in Saudi Arabia's oil facilities which drove up crude oil prices; market expectation of a policy rate cut by the BSP on its 26 September 2019 policy meeting; and weak business activity data from large European economies.

On a y-t-d basis, the peso appreciated against the US dollar by 1.45 percent to close at ₱51.83/US$1 on 30 September 2019 from the end-December 2018 closing rate of ₱52.58/US$1.[44] The sustained inflows of foreign exchange from overseas Filipino remittances, foreign direct investments (FDI), Business Process Outsourcing (BPO) receipts, as well as the ample level of the

[42] Sources: South Korea (Capital Ratios of Banks and Bank Holding Companies, June 2019); Malaysia (Banking System's Total Capital Ratio, August 2019); Thailand (Commercial Banks' Capital Funds Percentage of Risk Assets, July 2019); and Indonesia, IMF and financial stability report (Commercial Banks, Regulatory Capital to Risk-Weighted Assets Ratio, March 2019).

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

[44] Based on the last done deal transaction in the afternoon.

country's Gross International Reserves (GIR), and the country's firm economic growth provided support to the peso.

Meanwhile, the volatility of the peso's daily closing rates (as measured by the coefficient of variation) stood at 1.01 percent in Q3 2019, slightly higher than the 0.61 percent registered in Q2 2019.[45] The volatility of the peso in the same period was also slightly higher than the volatility of some currencies in the region.

On a real trade-weighted basis, the peso gained external price competitiveness in Q3 2019 against the basket of currencies of all trading partners (TPI) and trading partners in advanced (TPI-A) and developing (TPI-D) countries relative to Q2 2019. This was indicated by the decline in the real effective exchange rate (REER) index of the peso by 0.51 percent, 1.26 percent, and 0.10 percent, against the TPI, TPI-A and TPI-D baskets, respectively.[46,47]

Relative to Q3 2018, the peso meanwhile lost external price competitiveness in Q3 2019 across currency baskets. This developed following the nominal appreciation of the peso and the widening inflation differential, resulting in the increase in the REER index of the peso by 4.42 percent, 4.22 percent and 4.53 percent against the TPI, TPI-A and TPI-D baskets, respectively.

[45] The coefficient of variation is computed as the standard deviation of the daily closing exchange rate divided by the average exchange rates for the period.
[46] The TPI measures the nominal and real effective exchange rates of the peso across the currencies of 14 major trading partners (MTPs) of the Philippines, which includes US, Euro Area, Japan, Australia, China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand. The TPI-A measures the effective exchange rates of the peso across currencies of trading partners in advanced countries comprising of the US, Japan, Euro Area, and Australia. The TPI-D measures the effective exchange rates of the peso across 10 currencies of partner developing countries which includes China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.
[47] The REER index represents the Nominal Effective Exchange Rate (NEER) index of the peso, adjusted for inflation rate differentials with the countries whose currencies comprise the NEER index basket. A decrease in the REER index indicates some gain in the external price competitiveness of the peso, while a significant increase indicates the opposite. The NEER index, meanwhile, represents the weighted average exchange rate of the peso vis-à-vis a basket of foreign currencies.

III. Fiscal Developments

The NG recorded a ₱120.4-billion fiscal deficit for the first eight months of 2019, which is 57.3 percent lower than recorded in 2018 (Table 15).

NG posts a fiscal deficit for January-August 2019

Netting out the interest payments in NG expenditures, the primary surplus amounted to ₱130.2 billion, which is a turnaround from the ₱43.3 billion deficit recorded in January – August 2018.

Table 15. National Government Fiscal Performance
in billion pesos

	2018		2019		Growth Rate (in percent)	
	Aug	Jan-Aug	Aug	Jan-Aug	Aug	Jan-Aug
Surplus/(Deficit)	-2.6	-282.0	-2.5	-120.4	-3.8	-57.3
Revenues	256.9	1,909.2	279.7	2,091.4	8.9	9.5
Expenditures	259.5	2,191.1	282.2	2,211.8	8.8	0.9

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

Revenues increased by 9.5 percent to ₱2,091.4 billion in January – August 2019 compared to ₱1,909.2 billion in the same period last year. The Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) contributed ₱1,452.3 billion and ₱411.2 billion, respectively. Revenue collections by the BIR and BOC were higher by 10.6 percent and 7.2 percent, respectively. Meanwhile, income from the Bureau of the Treasury (BTr) increased by 29.5 percent to ₱107.9 billion.

Expenditures for the period in review amounted to ₱2,211.8 billion, 0.9 percent higher than the expenditures in January – August 2018. Excluding interest payments, expenditures barely went up by 0.4 percent to ₱1,961.2 billion. Meanwhile, interest payment was 5.0 percent higher compared to its year-ago level, reaching ₱250.6 billion in January – August 2019.

IV. External Developments

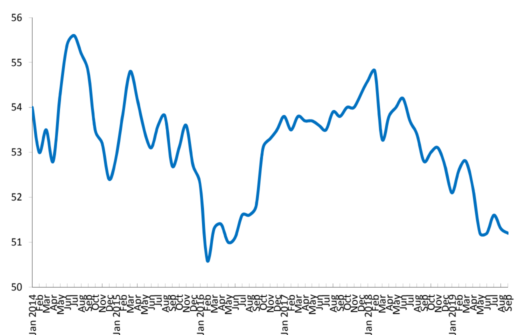
The JP Morgan Global All-Industry Output Index fell to 51.2 in September from 51.3 in August as growth in new business slowed and the downturn in global trade activity continued.

Global economic activity remains subdued in September

During the month, growth improved in the US, Italy, Brazil, and Australia. Meanwhile, rates of expansion slowed in France, Spain, Russia, and Ireland, while downturns were recorded for Germany and the UK.[48]

Chart 39. JP Morgan Global All-Industry Output Index

index points



Source: Markit Economics

US. Real GDP expanded by 2.0 percent on a seasonally-adjusted q-o-q basis in Q2 2019, slower than the 3.1-percent growth rate in Q1 2019. On a y-o-y basis, real output grew by 2.3 percent in Q2 2019 from the 2.7-percent expansion in the previous quarter. The increase in real GDP in the second quarter reflected positive contributions from personal consumption expenditures, federal government spending, and state and local government spending. These movements were partly offset by negative contributions from private inventory investment, exports, nonresidential fixed investment, and residential fixed investment. [49]

[48] JP Morgan Global Manufacturing & Services PMI, http://www.markiteconomics.com/

[49] US Bureau of Economic Analysis, "Gross Domestic Product: Second Quarter 2019 (Third Estimate)," news release, 26 September 2019. https://www.bea.gov/system/files/2019-09/gdp2q19_3rd_0.pdf

US economy cools in Q2 2019

Meanwhile, the manufacturing PMI decreased to 47.8 percent in September from 49.1 percent in August as new orders declined amid weak market confidence owing to global trade concerns.[50]

The unemployment rate fell to 3.5 percent in September from 3.7 percent in August. Total nonfarm payroll employment increased by 136,000 during the month. Employment gains occurred in health care as well as in professional and business services. Meanwhile, on a y-o-y basis, inflation was at 1.7 percent in September, unchanged from the rate in August.

The Conference Board Consumer Confidence Index fell to 125.1 in September from 134.2 in August.[51] Consumers' assessment of current business and labor market conditions and their expectations regarding the short-term outlook weakened amid continued uncertainty due to the escalation in trade and tariff tensions. By contrast, the Thomson-Reuters/University of Michigan Index of Consumer Sentiment rose to 93.2 in September from 89.8 in August.[52]

Euro Area. On a q-o-q basis, real GDP growth in the euro area declined to 0.2 percent in Q2 2019 from 0.4 percent in Q1 2019. On a y-o-y basis, real GDP expanded by 1.2 percent in Q2 2019 from 1.3 percent in Q1 2019.[53] Meanwhile, the composite PMI for the euro area decreased to 50.1 in September from 51.9 in August as demand for goods and services declined at the fastest rate in over six years.[54]

Inflation in the euro area decreased to 0.8 percent in September from 1.0 percent in August. The decline in inflation was due to the slower inflation for food, alcohol & tobacco; energy; and non-energy industrial goods. Meanwhile, the seasonally adjusted unemployment rate fell to 7.4 percent in August from 7.5 percent in July.

[50] Institute for Supply Management, https://www.instituteforsupplymanagement.org

[51] The Conference Board, http://www.conference–board.org/

[52] University of Michigan Survey of Consumers, http://www.sca.isr.umich.edu/

[53] Eurostat news release 137/2019 dated 6 September 2019

[54] Markit Eurozone PMI, http://www.markiteconomics.com/

The European Commission's Economic Sentiment Indicator in the euro area fell to 101.7 in September from 103.1 in August due to weaker confidence in industry and retail trade, while confidence improved among consumers and remained broadly steady in services and construction.

Japan. On a q-o-q basis, real GDP grew by 0.3 percent in Q2 2019 from 0.5 percent (revised) in Q1 2019. Meanwhile, on a y-o-y basis, real GDP expanded by 1.0 percent in Q2 2019, unchanged from Q1 2019 as public demand improved during the quarter.[55]

Manufacturing eases in Japan, improves in China

Meanwhile, the seasonally-adjusted manufacturing PMI fell to 48.9 in September from 49.3 in August as both output and new orders declined, reflecting weaker domestic and foreign demand.[56]

Inflation decreased to 0.3 percent in August from 0.5 percent in July due to lower inflation for food; fuel, light, and water charges; medical care; as well as education. Meanwhile, the seasonally adjusted unemployment rate was 2.2 percent in August, the same figure recorded in the previous month.

China. Real GDP in China expanded by 6.2 percent y-o-y in Q2 2019, slower than the 6.4 percent growth in Q1 2019. The slower expansion in Q2 2019 was attributed largely to the impact of the country's trade dispute with the US.

Meanwhile, the seasonally-adjusted manufacturing PMI rose to 51.4 in September from 50.4 in August, driven partly by a faster rise in overall new work amid firmer domestic demand.[57]

Inflation rose to 3.0 percent in September from 2.8 percent in August due mainly to higher food inflation during the month.

[55] Second Preliminary Estimate. Department of National Accounts, Economic and Social Research Institute, Cabinet Office. http://www/esri.cao.go.jp/
[56] Flash estimate. Jibun Bank Japan Manufacturing PMI, http://www.markiteconomics .com/
[57] Caixin China General Manufacturing PMI, http://www.markiteconomics.com/

India. Real GDP in India expanded by 5.0 percent y-o-y in Q2 2019 from 5.8 percent in the previous quarter. Albeit slower, the latest GDP expansion was driven mainly by growth in electricity, gas, water supply, and other utility services; trade, hotels, transport, communication and services related to broadcasting; and public administration, defense, and other services.[58]

Economic activity in India expands at a weaker pace

Meanwhile, the composite PMI fell to 49.8 in September from 52.6 in August, reflecting weaker manufacturing production growth and a decline in service sector activity.

Inflation was nearly unchanged at 3.21 percent in August from 3.15 percent in the previous month. The slightly faster August inflation reading was due to higher inflation for food and beverages as well as pan, tobacco, and intoxicants.

ASEAN Region. The Nikkei ASEAN Manufacturing PMI remained in contraction as it posted a reading of 49.1 in September from 48.9 in August due to a decline in production and new orders.

Overall manufacturing conditions in ASEAN region continue to weaken

Manufacturing conditions continue to improve in Myanmar, Philippines, Thailand, and Vietnam. Meanwhile, the manufacturing sectors of Indonesia, Malaysia, and Singapore remained in contraction territory.[59]

Policy Actions by Central Banks. On 2 July 2019, the Reserve Bank of Australia decided to lower the cash rate by 25 bps to 1.0 percent to further support employment growth and ensure that inflation will be consistent with the medium-term target.

[58] Ministry of Statistics and Programme Implementation. http://mospi.nic.in/
[59] Nikkei ASEAN Manufacturing PMI, http://www.markiteconomics.com/

Central banks ease their monetary policy settings

Similarly, on 18 July 2019, the Monetary Policy Board of Bank of Korea decided to reduce the benchmark interest rate by 25 bps to 1.50 percent based on the assessment that the pace of global economic growth has continued to weaken due mainly to the US-China trade dispute.

On 7 August 2019, the Reserve Bank of India (RBI) cut the policy repo rate by 35 bps to 5.40 percent as it expects domestic economic activity to continue to be weak, with the global growth slowdown and escalating trade tensions posing as downside risks.

During their 7 August monetary policy meeting, the Bank of Thailand (BOT) also reduced their policy rate by 25 bps to 1.50 percent based on the view that the Thai economy would expand at a slower rate than previously assessed owing to a contraction in merchandise exports which started to affect domestic demand.

The Reserve Bank of New Zealand (RBNZ) also decided to cut the official cash rate by 50 bps to 1.0 percent during its 7 August monetary policy meeting. The decision was based on the assessment that there is a need for further stimulus to meet inflation and employment objectives.

On 18 September 2019, the Federal Open Market Committee (FOMC) of the US Federal Reserve decided to lower the target range for the federal funds rate by 25 bps to 1.75-2.0 percent, in light of the implications of global developments on the economic outlook as well as muted inflation pressures. The FOMC also reduced the target range for the federal funds rate by 25 bps to 2.0-2.25 percent during its 31 July policy meeting amid muted inflation pressures and uncertainties in the economic outlook given recent global developments.

Similarly, on 19 September 2019, Bank Indonesia (BI) reduced the 7-day reverse repo rate by 25 bps to 5.25 percent to stimulate the domestic economy amid sluggish global economic activity. During its policy meetings on 22 August and 18 July, BI also lowered the BI 7-day reverse repo rate by 25 bps each to boost domestic economic activity and ensure adequate market liquidity.

Meanwhile, the Reserve Bank of New Zealand, Bank of Thailand, Bank of England (BOE), Central Bank of the Republic of China (Taiwan), Bank of Japan (BOJ), the European Central Bank (ECB), Bank Negara Malaysia, Reserve Bank of Australia, and Bank of Canada kept their respective policy rates steady during their monetary policy meetings in September.

However, on 12 September, the ECB reduced the interest rate on the deposit facility by 10 bps to -0.50 percent from -0.40 percent and decided to re-introduce net purchases under its asset purchase programme (APP). The APP will involve the purchase of €20 billion worth of bonds every month starting November until such a period when inflation expectations come sufficiently close to, but below, 2 percent.

The People's Bank of China (PBOC) did not announce any adjustment in its benchmark one-year lending rate during the quarter. However, on 9 September 2019, the PBOC announced that it would reduce the RR ratio (RRR) for large banks by 50 bps to 13 percent from 13.5 percent, effective 16 September. An additional 100-bp phased reduction in the reserve requirement ratio (RRR) will also be implemented on qualified city commercial banks that operate within provincial-level regions, effective 15 October and 15 November. The phased reduction is expected to inject about RMB900 billion in liquidity and lend support to China's slowing economy.

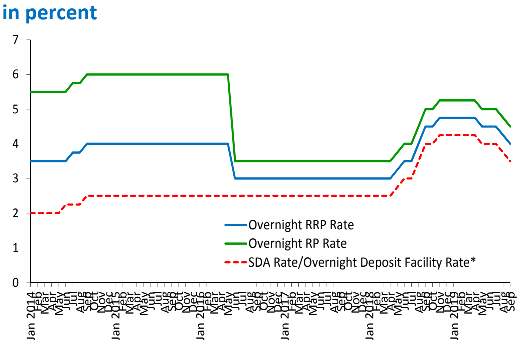
V. Monetary Policy Developments

At its monetary policy meeting on 8 August, the BSP lowered the key policy rate by 25 bps to 4.25 percent for the overnight reverse repurchase or RRP facility. Similarly, in the 26 September meeting, the BSP decided to reduce the policy rate anew by another 25 bps to 4.00 percent. The interest rates on the overnight lending and deposit facilities were likewise reduced accordingly.

The BSP reduces the key policy rate twice during the quarter

In deciding to reduce the key policy interest rate twice during the review quarter, the BSP noted that price pressures have continued to ease in Q3 2019.

Chart 40. BSP Policy Rates
in percent



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

Latest baseline inflation forecasts presented then continued to indicate that inflation is likely to settle within the lower half of the target band of 3.0 ± 1 percentage point for 2019 up to 2021. Inflation expectations also remained well-anchored based on the BSP's survey of private sector economists.

Moreover, the BSP noted that the balance of risks to the inflation outlook has shifted toward the upside for 2020, while it is seen to tilt to the downside for 2021. Upside risks to inflation over the near term were seen to emanate mainly from volatility in oil prices due to geopolitical tensions in the Middle East as well as the potential impact of the ASF outbreak on food prices.

Meanwhile, subdued pace of global economic activity is considered to continue to temper the inflation outlook.

At the same time, the BSP was of the view that prospects for global economic growth were likely to remain weak owing mainly to uncertainty over trade policies. Nevertheless, firm domestic spending and progress on policy reforms could serve as buffers against global headwinds.

Given these considerations, the BSP believed that the benign inflation outlook provided room for a 50-bp reduction in the policy rate in Q3 2019 to support economic growth and reinforce market confidence.

At its meeting on 27 September 2019, the MB decided to reduce the reserve requirements for U/KBs, TBs, and RBs by 100 bps (or one ppt). The reduction will be effective on the reserve week 1 November 2019 and will apply to the deposits and deposit substitute liabilities in local currency of U/KBs (from 16 percent to 15 percent), TBs (from 6 percent to 5 percent), and RBs (from 4 percent to 3 percent).

The RR cut is in line with the BSP's broad financial sector reform agenda to promote a more efficient financial system by lowering financial intermediation costs. At the same time, the adjustment in RR ratios is aimed at increasing domestic liquidity in support of credit activity.

Going forward, the BSP emphasized that it will continue to monitor emerging price and output developments to ensure that monetary policy setting remains consistent with price stability while being supportive of sustained non-inflationary economic growth over the medium term.

VI. Inflation Outlook

BSP Inflation Forecasts

The latest baseline forecasts indicate that inflation will settle within the 3.0 percent ± 1.0 percentage point target range for 2019 to 2021. Inflation is projected to stay low in October 2019 due primarily to base effects as oil and rice prices peaked during the same period in 2018, but is expected to revert back to the target range by December 2019 and settle close to the midpoint of the target range for 2020 and 2021.

The decline in the forecast path compared to the previous report can be attributed primarily to lower electricity rates and easing food prices which contributed to the lower-than-expected inflation outturns in Q3 2019 along with the decline in global oil prices.

The risks to the inflation outlook appear to be on the upside for 2020, but are tilted to the downside in 2021. Petitions for electricity rates and transport fare adjustments, the proposed increase in the excise taxes of alcoholic beverages, the impact of ASF on meat prices, and higher global oil prices are the main upside risks to inflation.

Meanwhile, slower global economic growth due to the escalation of protectionist policies in advanced economies as well as geopolitical tensions continue to be the main downside risks to inflation.

Inflation is projected to settle within the target range for 2019 – 2021

Demand Conditions. Domestic growth prospects continue to be firm despite the deceleration in Q2 2019. Domestic economic activity slowed down to 5.5 percent in Q2 2019 from the 5.6 percent growth in Q1 2019 and 6.2 percent expansion in Q2 2018. On the expenditure side, growth was driven by sustained growth in household consumption. On the production side, the industry and services sectors continue to be the primary drivers of the expansion.

Economic activity in H2 2019 could be boosted by the continued rebound in tourism-related sectors as well as the expected government spending catch up with the implementation of its social programs and infrastructure projects.

Looking ahead, prospects for the domestic economy remains respectable. Domestic growth could be supported by the services sector and public construction. Private demand is expected to remain robust, aided mainly by sustained remittance inflows and lower inflation. Private capital formation should likewise contribute to economic growth with construction and investments in durable equipment likely to remain positive as the government projects and other infrastructure programs get underway. Domestic economic activity would need to grow by 6.4 percent in H2 2019 to reach the low-end of the government's target of 6.0 to 7.0 percent.

High-frequency real sector indicators also point to firm growth prospects in the near term. Capacity utilization for the manufacturing sector suggests that more than half of all major manufacturing sectors are operating at or above 80.0 percent. The composite PMI also remains above the 50-point mark as of August 2019, suggesting sustained expansion across all sectors. Moreover, results of the BSP expectations surveys indicated improved consumer confidence in Q3 2019.

Supply Conditions. Food inflation could decline further over the near term due to the implementation of non-monetary measures to ease import requirements, such as the passage of the Rice Tariffication Law.

Improved domestic food supply conditions have contributed to decelerating price pressures

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The deceleration in global non-fuel prices is expected to continue over the medium term. Heightened trade tensions have affected global trade and investments thereby dampening global demand for commodities. Prices of agricultural commodities and metals could remain stable in the near term due to subdued demand conditions. Commodity prices have started to decline in the H2 2018 with the trade barriers imposed by the US and China. Similarly, metal prices have fallen following the effects of tariffs on consumer and capital goods.

In the domestic front, based on standing crop estimates by the PSA, *palay* production could decrease by 4.7 percent in Q3 2019. The projected drop in *palay* production could be attributed to a decline in harvest areas from 2018 levels. Meanwhile, corn production could increase by 25.0 percent in Q3 2019 due to increase in harvest areas.[60]

Nonetheless, the reforms in rice importation have significantly lowered food prices in 2019. With the implementation of the Rice Tariffication Law and the accelerated issuance of certifications for the private sector's out-quota rice importation by the NFA, domestic rice prices could decline to levels similar to that of major import sources of rice, such as Thailand and Vietnam.

Despite the recent attack on Saudi Arabia's production facilities, international crude oil prices declined in Q3 2019 relative to the previous quarter's level due to concerns of weaker demand amid uncertainties surrounding the external environment. Global crude oil prices eased sharply in August and the first week of September 2019 due to concerns on global demand with the recent round of tariff increases between the US and China. In addition, the production level of the Organization of the Petroleum Exporting Countries (OPEC) increased in August 2019, the first production expansion registered for the year. However, global crude oil prices rose markedly in the third week of September following the attacks on Saudi Arabia's oil facilities. Nonetheless, the release of strategic reserves by the US and Saudi Arabia and the expected resumption of operations by the end of the month cushioned the impact on crude oil futures over the forecast horizon. Uncertainties surrounding the oil market could further emanate from supply dynamics and extent of trade dispute between the US and China as well as the production cut by OPEC and other non-OPEC countries.

The latest futures prices indicate that global crude oil prices could remain subdued in 2019-2021. This is in line with projections of the EIA along with other international agencies for crude oil prices to remain broadly steady in the near term.

[60] PSA, Updates on July - September 2019 Palay and Corn Estimates, October 2019, available online at http://www.psa.gov.ph

Domestic economic activity remains broadly in line with potential growth

The balance of demand and supply conditions as captured by the output gap (or the difference between actual and potential output), provides an indication of potential inflationary pressures in the near term.[61]

Given the latest GDP data, estimates by the BSP show that the output gap remains broadly neutral and stable relative to the previous quarter.[62]

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

1) BSP's overnight RRP rate at 4.0 percent from October 2019 to December 2021;

2) NG fiscal deficits for 2019 to 2021, which are consistent with the DBCC-approved estimates;

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

4) Increase in nominal wage in November 2019, November 2020 and November 2021 consistent with historical wage increases;

5) Real GDP growth is endogenously determined; and

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

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

Risks to the Inflation Outlook

The risks to the inflation outlook may be presented graphically through a fan chart. The fan chart depicts the probability of different inflation outcomes based on the central projection (corresponding to the baseline forecast of the BSP) and the risks surrounding the inflation outlook.

Compared to the previous inflation report, the latest fan chart shows a downward shift in the inflation projections. The decline in the forecast path compared to the previous report can be attributed primarily to lower electricity rates and easing food prices which contributed to the lower-than-expected inflation outturns in Q3 2019 along with the decline in global oil prices.

Lower projected inflation path is due to deceleration in electricity, oil, and food prices

The BSP's review of current inflation dynamics suggests that the risks surrounding the inflation outlook appear to be on the upside for 2020, but are tilted to the downside in 2021.

Various petitions for rate adjustments by Meralco and PSALM are considered as upside risks to inflation and are not part of the baseline scenario. Meralco's petitions include generation and transmission charges, system loss, lifeline subsidy, the December 2013 rate adjustment, which is the subject of Supreme Court temporary restraining order, and the ₱0.65/ kWh adjustment for the January 2014 billing period that is subject to the ERC's approval. PSALM's petitions cover adjustments for fuel and foreign exchange costs.

Higher excise taxes for alcoholic beverages present an additional upside risk to inflation. The House of Representatives approved H.B. 1206 on 20 August 2019 to raise the sin taxes of alcoholic beverages (0.7 percent of the CPI basket). Under the proposed bill, the specific taxes of distilled spirits, wines, and fermented liquor specified in the Sin Tax Reform Act of 2012 (Republic Act No. 10351) will be raised in addition to the higher annual indexation of 7.0 percent from 4.0 percent previously.

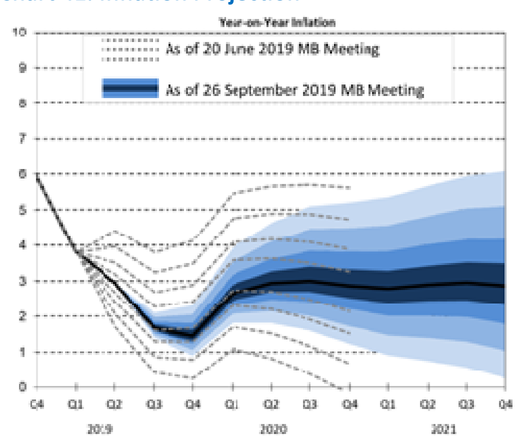
The recent ASF outbreak could also lead to an uptick in meat prices over the near term. Meat products account for 6.2 percent of the CPI basket, of which 4.8 percent is from fresh or frozen meat and 1.4 percent from canned and processed meat. The outbreak of ASF is expected to lower domestic hog supply and also temper demand.

Consequently, consumers could substitute away from pork products, resulting in possible increased demand and higher prices of chicken and beef products. However, the Department of Agriculture (DA) has assured the public that the situation is under control and that only a small percentage of total hog supply in two provinces, i.e. Bulacan and Rizal, was affected by ASF.

Heightened geopolitical tensions in the Middle East following the drone strike on Saudi Arabia present upside risks over the near term. The oil facilities targeted in Saudi Arabia, which represent 5.0 to 6.0 percent of global production, are expected resume its operations by the end of the month. However, the increased geopolitical tension within the region and the likelihood of further attacks could result in supply disruptions, raising global oil prices.

The balance of risks to the inflation outlook is on the upside for 2020, but is tilted to the downside in 2021

Chart 41. Inflation Projection



Source: BSP estimates

The slower global economic outlook and the escalation of trade tensions remain as downside risks. The continued trade tensions between the US and China, risk-off episodes from long-standing global financial vulnerabilities, global disinflationary pressures, and geopolitical risks are the primary downside risks to global growth over the medium term. The escalation of trade tensions between the US and China and other countries on global trade and investments could result in further downward adjustments to world growth. The imposition of additional trade barriers would raise consumer prices and the cost of capital goods, thereby dampening momentum from consumption and investment. The expected slowdown in global demand is seen to dominate the impact of higher prices of commodities in the US and China due to the increased tariff rates.

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

The shaded area, which measures the range of uncertainty, is based on the forecast errors from the past years. In greater detail, it can be enhanced by adjusting the level of skewness of the downside and upside shocks that could affect the inflationary process over the next two years in order to change the balance of the probability area lying above or below the central projection.

Implications for the Monetary Policy Stance

With the sustained downtrend in domestic inflation during the quarter, the BSP saw room to reduce the policy rate by 25 bps each on 8 August 2019 and 26 September 2019. The MB recognized the benign inflation outlook and well-anchored inflation expectations over the policy horizon, with baseline projections continuing to indicate that inflation would likely settle within the lower half of the inflation target range of 3.0 percent ± 1.0 percentage point in 2019-2021. The balance of risks to the inflation outlook also shifted toward the upside for 2020, while it continued to tilt to the downside for 2021. Upside risks to inflation over the near term would emanate mainly from volatility in global oil prices and from the potential impact of the African Swine Fever outbreak on domestic food prices.

At the same time, while prospects for domestic economic growth remained firm due to steady domestic spending and progress on various macroeconomic policy reforms, the outlook for global economic growth had weakened further owing mainly to sustained trade tensions among major economies. The cumulative 50-bp reduction in the policy rate during the quarter was therefore aimed at reinforcing market confidence.

Furthermore, following the reduction in RR ratios in May 2019, the MB decided to reduce RR ratios by another 100 bps on 27 September 2019, effective on the first reserve week of November 2019. The cut in reserve requirements is expected to support credit activity by lowering financial intermediation costs, in line with the BSP's broad financial sector reform agenda.

Going forward, the BSP will continue to monitor and assess the impact of its previous policy actions in conjuction with the evolving outlook for prices and output to determine if there is any need for further monetary adjustments to uphold the BSP's mandate of price stability. Future decisions on the monetary policy stance will remain data-dependent.

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

Summary of Monetary Policy Decisions

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

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

www.bsp.gov.ph/monetary/inflation.asp

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