BALANCE OF PAYMENTS DEVELOPMENTS JANUARY-AUGUST 2002

11/22/2002 1:41 PM

➢ Overall Position

The BOP reverses to a surplus due mainly to the robust performance of the current account.

The country's balance of payments (BOP) in the first eight months of 2002 yielded a $903 million surplus, a reversal of the $1,133 million deficit posted in the same period last year. The strong performance of the current account was behind the marked improvement in the overall BOP position (Table 1).

Balance of Payments (US$ m)

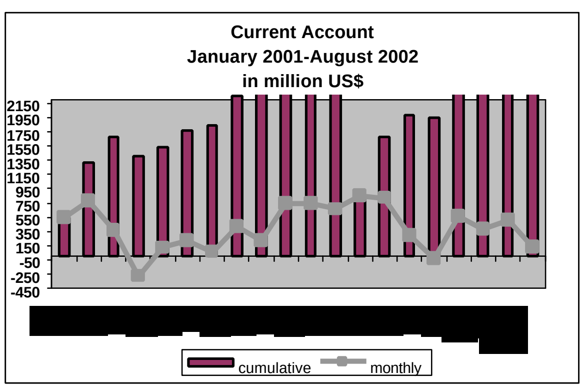
	January-August		
	2002	**2001**	**Growth Rate (%)**
I. Current Account	3532	1780	98.4
II. Capital & Fin'l.	-3093	-2643	-17.0
III. Net Unclassified	464	-270	271.9
IV. Overall BOP *	**903**	**-1133**	**179.7**

* Totals may not add up due to rounding.

➢ Current Account

The current account gains strength in all fronts.

The current account surplus nearly doubled to $3,532 million in January-August 2002, with all the sub-accounts gaining headway. The higher net inflow in the income account, the significantly lower net outflow in the services account and the continued good showing of the trade-in-goods account propped up the current account surplus.



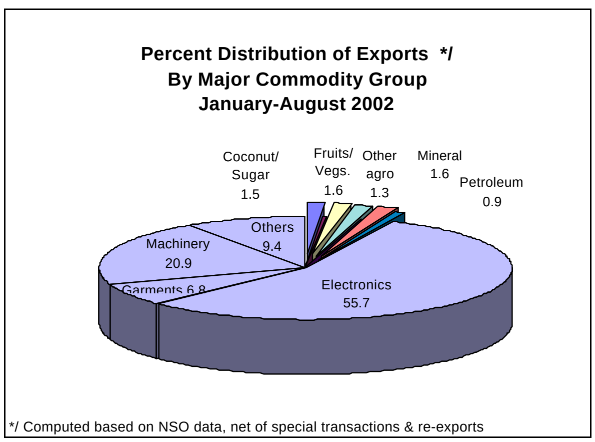
➢ Trade in Goods

Exports of goods post five straight months of double-digit growth.

Exports continued to perform well in August, bringing the year-to-date performance to $22,319 million or 8.3 percent higher than the level a year ago.[1] This was the fifth month in a row that exports recorded a year-on-year double-digit growth after 14 consecutive months of decline. The pick-up in exports reflected largely the recovery in electronics exports. The implementation of a two-pronged strategy in exports—industry clustering to enhance competitive advantages and an aggressive marketing program in both traditional and new markets—also contributed to the improvement in export performance.

Although the U.S. and Japan remained to be the country's traditional export destinations accounting for 25 percent and 15 percent, respectively, of total exports of goods, their market shares had contracted from last year's 28 percent and 17 percent, partly on account of lower demand due, in turn, to their weaker-than-expected economic recovery. Absorbing the slack in demand, however, were Asian countries such as China, Hong Kong, Taiwan, Singapore, Malaysia, South Korea, and Thailand. The aggregate share of these countries to total Philippine exports rose to 35 percent during the first eight months of the year from 31 percent last year.

The country's major export commodity earners during the period in review were electronics, machinery and transport equipment, and garments (Table 2.1).



[1] Per BPM5 concept

Rebound in electronics exports continues in August while exports of machinery and transport equipment help boost export earnings.

a) *Electronics.* Electronic exports for the first eight months of 2002 reverted to a positive growth of 10.0 percent from a contraction of 22.2 percent last year to reach $12,126 million. This developed following the successive double-digit year-on-year expansion in electronic exports since April 2002. The upturn in electronics was in line with the book-to-bill ratio, which climbed to above the unity mark beginning March. However, the ratio, though still above 1, was noted to be trending downward beginning June, foretelling a soft recovery and a possible slowdown in demand for electronics in the months ahead. [2]

Driving the performance of Philippine electronics exports is the strong back-end semiconductors operations, assembly and test centers. It was noted that 70 percent of Digital Signal Processors or DSP (main component of mobile cellular phones) worldwide are manufactured in the Philippines. In addition, the country is one of the major Pentium (brain of computers) and disk drive (memory of computers) centers of the world. Electronic Braking System, which serves as a safety feature of vehicles, as well as the servo controls, which help operate aircraft wings, are also being manufactured in the country.

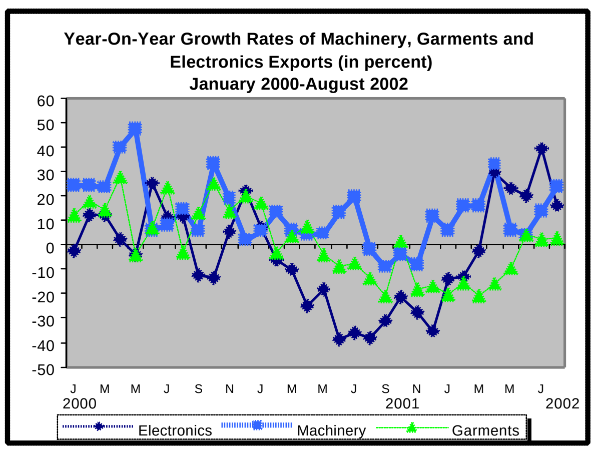
To improve global competitiveness, the Semiconductor and Electronics Industries in the Philippines (SEIPI), an umbrella organization of semiconductor producers in the country, with the aid of the government, hammered out a five-point strategy to make the Philippines a regional center of excellence in selected electronics products and processes. These include: (1) capitalizing on the country's historical edge as a transshipment point in Asia, taking full advantage of the relocation of major logistics and transportation operations in the country like Federal Express and United Parcel Service; (2) improving the industry's supply chain by developing backward linkages; (3) improving research and development to face the China challenge; (4) introducing low-end wafer fabrication? the backbone of the electronics industry? which will require specialized inputs that are available in the Philippines; and (5) cutting power costs to bring down cost of production. The industry predicts that the future growth of electronics will be towards electronic manufacturing services involving primarily contract manufacturing of electronics assemblies and sub-assemblies for original equipment manufacturers such as Compaq, Lucent Technologies, Alcatel,

[2] The book-to bill ratio is the ratio of three-month moving average bookings (demand) to three-month moving average shipments (supply). A ratio of less than one indicates that demand is lower than supply. Conversely, a ratio of one or more indicates that demand exceeds supply.

Ericsson, Nortel Networks, and Philips.

b) *Machinery and Transport Equipment*. Exports of machinery and transport equipment, the only major export commodity group that has showed consistent strength during the year, grew by 14.5 percent to $4,552 million. Major contributory factors were the increased exportation of input/output peripheral units, parts/accessories of automatic data processing and machineries and units as well as other parts and accessories of motor vehicles.

c) *Garments*. Exports of garments continued to recover, recording their third consecutive month of modest growth of 2.8 percent in August. This tempered the year-to-date decline of garment exports to 8.5 percent to reach $1,509 million. The twin strategies to tap the high-end markets in traditional quota-driven countries and the increased penetration of non-quota markets of Japan, United Arab Emirates, Hong Kong and Mexico appeared to be paying off. With the impending quota phase-out in 2004, the garments and textile industry is shifting to high-value items and veering away from traditional markets like the U.S., which has exhibited signs of saturation following the influx of garments and textile items from other countries. The Department of Trade and Industry encourages the industry to continue to re-engineer itself and rethink its business plans and strategies in order to survive and remain competitive beyond 2004.



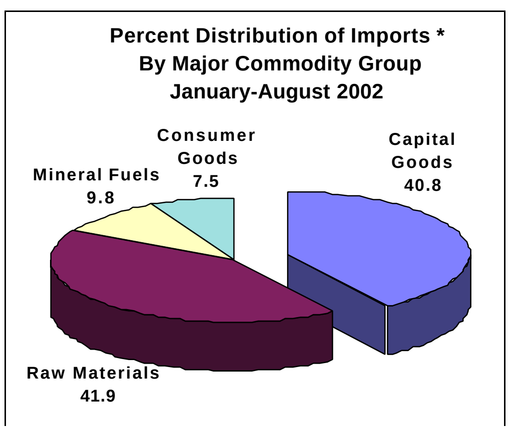
Growth in imports continues. Backed by increased purchases of raw materials for the electronics industry, imports of goods grew for the seventh consecutive month since February, peaking in August at 22.4 percent. This brought the cumulative imports growth to 7.8 percent to reach $21,293 million, a reversal of the

1.2 percent decline registered in the comparable period in 2001 (Table 2.2).[3] The strong import growth reflected, in part, the high import demand for electronic exports and the pick-up in domestic demand.

Imports of raw materials and intermediate goods—which accounted for more than two-fifths of total imports—expanded by 12.1 percent to $8,974 million for the period January-August 2002. Double-digit year-on-year growth rates ranging from 33 to 74 percent were noted in the importation of materials/accessories for the manufacture of electrical equipment during the period February-August 2002.[4]

Meanwhile, capital goods imports reached $8,735 million following increased importations of telecommunication equipment? mainly inputs to electronics production? and office and EDP machines. The 11.4 percent expansion during the first eight months of the year was a reversal of the 3.7 percent decline in 2001.

Among the major import commodity groups, mineral fuels and lubricants posted the only decline at 11.9 percent to reach $2,101 million during the period in review. This developed on account of the twin effect of the contraction in the volume of imports and the drop in price of petroleum crude. The average price of petroleum crude for the first eight months of 2002 declined to $23.29 per barrel from $24.68 per barrel last year. Meanwhile, the fall in the volume of oil imports was attributed mainly to the temporary slowdown in operations of some refinery units of oil companies for various reasons including check-up and maintenance operations and excess capacity.



---

[3] Per BPM5 concept

[4] About half of the imported raw materials needed for electronics production are lodged in the capital goods commodity group, particularly under telecommunication equipment and electrical machinery. Only consigned materials/accessories for the manufacture of electrical equipment are classified as raw materials and intermediate goods. Other electronics parts are classified as capital goods. The combined total of imported inputs to electronics lodged in the capital goods and raw materials categories increased by 27.8 percent during the review period as against the 6.6 percent decline in January-August 2001.

* Computed based on NSO data, net of special transactions

➢ Trade In Services

The deficit in the trade-in-services account narrows.

The trade-in-services account in January-August 2002 posted a lower net outflow of $721 million (Table 3). The 43.4 percent narrowing of the deficit was traced to lower net payments for transportation services and for miscellaneous business, professional and technical services. Moreover, increased net receipts from travel services, which rose by 71.1 percent to $669 million, owing to the higher rate of decline in travel payments relative to that of travel receipts also contributed to the lower net outflow in the services account. The weaker peso and the government's program to promote domestic tourism among local residents could be behind the lower travel payments.

The country's tourism strategy will focus on an aggressive promotion blitz of the government through new international marketing campaigns to showcase the country's tourists attractions. In line with this, the government tourism program? "Visit Philippines" 2003? kicked off on 15 August 2002 and will cover three continents: the North America, Asia (China, Japan and Korea), and Europe (Spain, England and Italy). A strategy to support this program is the "Volunteer 12 Program" which will mobilize and tap all overseas Filipinos to encourage friends, relatives, and associates to visit the country.

➢ Income

Higher OFW remittances and lower interest payments contribute to the income account surplus.

The net inflow in the income account during the period January-August 2002 increased to $2.906 billion, or 54.5 percent higher from the comparable level a year-ago. Underpinning this positive development was the higher remittances from overseas Filipino workers (OFWs), the cumulative amount of which reached $4.832 billion during the period in review. The 22.6 percent expansion from last year's level was partly attributed to the 3.9 percent rise in the number of new hires and rehires OFWs during the review period. Specifically, an increase in OFW deployment was noted in Europe, Africa and the Americas. Increased deployment of skilled workers also contributed to higher OFW remittances. The bulk of remittances from OFWs, which comprised 91.7 percent of gross income receipts, came from the U.S., Saudi Arabia, Japan, Hong Kong and Singapore.[5]

[5] Data may not reflect the actual country of deployment of OFWs due to the common practice of remittance centers in various cities abroad to course their remittances through correspondent banks, which are located mostly in the United States. Since banks attribute the origin of funds to the most immediate source, the U.S., therefore, would appear to be the major source of remittances.

To counter act the emerging trend towards "localization" and the slowdown experienced in some of the economies of countries where Filipino workers are deployed, the government has intensified its marketing of Filipino skills abroad.[6] In the next three years, higher remittances are anticipated with the expanded hiring of developed countries of OFWs in the medical field.

Meanwhile, the net outflow in the investment income account was slightly lower by 6.5 percent relative to the level last year as interest payments on portfolio and other investments fell with the continued drop in global interest rates (Table 4).

➢ Current Transfers

The current transfers account remains in surplus.

The net inflow in the current transfers account for January-August 2002 amounted to $321 million, 5.9 percent higher than year-ago level (Table 5).

➢ Capital and Financial Account

Net inflows of portfolio investments help moderate the net outflow in the capital and financial account.

The net outflow in the capital and financial account expanded by 14.9 percent to $3,037 million during the period in review notwithstanding net inflows of portfolio investments. The reversal of the portfolio investment account to a net inflow of $925 million from a net outflow of $300 million last year, however, helped mitigate the lower net inflow of direct investments and the negative impact of the higher net outflow of other investments.

➢ Capital Account

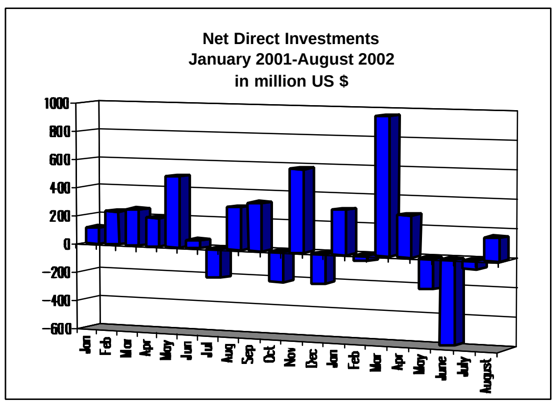
[6] Localization means the preferential hiring by a country of its own residents.

The capital account posts a higher deficit. The capital account for January-August 2002 posted a higher net outflow of $11 million compared to last year's deficit of $4 million, owing mainly to increased net outflow of migrants' transfers (Table 6).[7]

➢ Direct Investments

Higher direct equity investments by non-residents boost the direct investment account. Non-residents' investments in equity capital almost tripled to $815 million during the period in review. The bulk of non-residents' equity investments came from Japan following the investment of $544 million worth of shares by a Japanese firm in a local brewery company in March 2002. Equity funds were also infused in other manufacturing companies, financial institutions and transport and storage services. Major sources of direct investments apart from Japan were the U.S., Singapore, U.K. and the Netherlands (Table 7).

These notwithstanding, direct investments for January-August 2002 registered a lower net inflow of $828 million, 43.3 percent below the year-ago level. Repayment by local subsidiaries of loans granted by their foreign parent companies muted the impact of higher fresh equity investments.



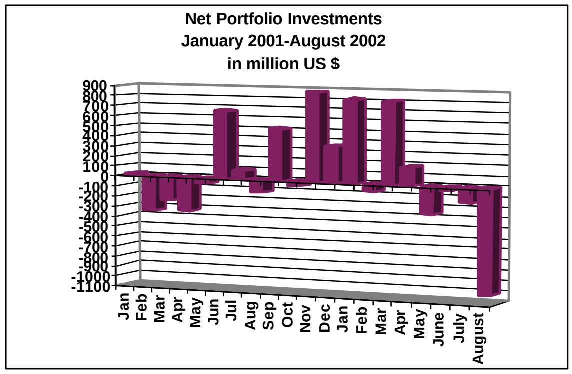
➢ Portfolio Investments

Higher non-residents' Portfolio investments for the first eight months of 2002 reverted to a net inflow of $925 million from a net outflow of $300 million in 2001

[7] The capital account consists largely of capital transfers. Capital transfers are transactions that involve a change in the stocks of assets of one or both parties and therefore relate to investments. By contrast, current transfers involve transactions that affect the level of disposable income and should therefore influence consumption of goods and services.

investments in equity and debt securities turn the portfolio investment account to a net inflow …

following increased non-residents' investments in resident-issued foreign-denominated debt securities, particularly government-issued medium-term bonds. Investments in debt securities posted a net inflow of $682 million from a net outflow of $204 million during the comparable period a year ago.[8] Non-residents' investments in equity securities also rose by 10.2 percent to $367 million, indicating a resurgence of investor confidence in the local equities market and a shift from investments in lower yielding domestic financial instruments to higher yielding equity securities (Table 8).



➢ Other Investments

…while the net outflow of other investments increases.

The net outflow in the other investment account expanded by 27.3 percent to $4.835 billion during the review period. This developed on account mainly of non-residents' withdrawals from their FCDU accounts in local banks and net loan repayments. Increased net deposits abroad by resident non-banks, majority of which were corporations involved in build-operate-transfer schemes, also contributed to the net outflow in other investments (Table 9).

➢ Reserve Assets

NG deposits raise the GIR to $16.1 billion.

As of end-Aug. 2002, the BSP's GIR rose to $16.1 billion, 3.1 percent higher vis-à-vis end-December level of $15.7 billion (Table 11).

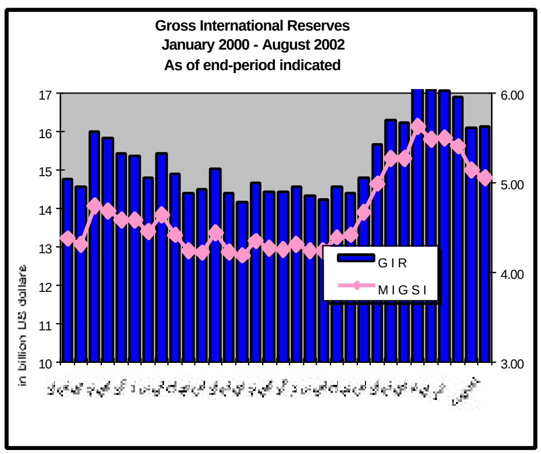
The increase in the GIR during the period was due mainly to foreign exchange inflows mainly in the form of net deposits by the Treasurer of

[8] The government issued $2.04 billion worth of foreign currency-denominated bonds in January, March and June while the BSP issued $250 million worth of fixed rate notes in January. Proceeds are earmarked for budgetary support and international reserve management.

the Philippines. [9] However, these were partly offset by outflows to meet the foreign exchange requirements of the BSP and the National Government.

The BSP's GIR sufficed to cover 5.1 months' worth of imports of goods and payment of services and income. Using other reserve coverage measures, the level of reserves was about 3.0 times the amount of the country's short-term external debt based on original maturity or, alternatively, 1.4 times the amount of short-term external debt based on residual maturity.[10]

During the review period, the bulk of reserves consisted of foreign investments (80.0 percent), while the rest were in gold (16.2 percent), foreign exchange (2.9 percent), and combined SDRs and reserve position in the Fund (0.9 percent). In terms of the currency composition of reserves excluding gold, 93.1 percent were in US dollars, 2.9 percent in Japanese yen, 1.6 percent in pound sterling and the balance of 2.4 percent in other foreign currencies.



➢ Exchange Rate

The peso depreciates compared to the level last year...

The peso-dollar exchange rate averaged ₱50.92:US$1 from January to August 2002, depreciating by 0.6 percent from the P50.64:US$1 average exchange rate for the same period in 2001. The year-on-year depreciation of the peso reflected, in part, swings in sentiment on

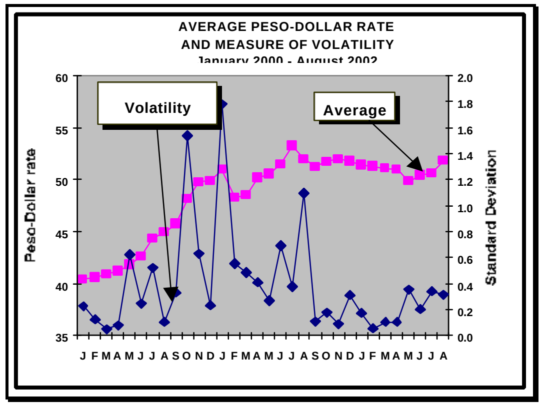
[9] Sources of deposit were mainly from government borrowings, i.e., net proceeds of the RP US Securities Registered Global Bond ($2.042 billion) and JBIC Co-Financing of the Power Sector Loan ($100 million)

[10] Refers to outstanding short-term external debt on original maturity basis plus principal payments on medium- and long-term loans of the public and private sectors falling due in the next 12 months.

regional currencies and steady corporate demand for dollars in tandem with the rise in imports.

...but the peso shows continued stability.

Notwithstanding the weaker peso, exchange rate movements were less volatile as indicated by the declining standard deviation of the daily peso-dollar exchange rate since September last year. In January-August 2002, the standard deviation at ₱0.64 was substantially lower than the ₱1.81 registered for the same period in 2001. The peso-dollar exchange rate ranged from ₱49.336 to ₱52.345 during the period under review.



Higher nominal depreciation and relatively lower domestic inflation strengthen the peso's external competitiveness against currencies of some competitor countries.

Relative to its level in the comparable period last year, the peso's average nominal effective exchange rate index (NEERI)[11] in January-August 2002 was almost unchanged against the currency basket of the country's major trading partners. However, the peso's NEERI depreciated slightly by 4.1 percent against the currency basket of a broad group of competitor countries,[12] and by 5.7 percent against the currency basket of a narrow group of competitor countries.[13] The drop in the peso's NEERI against the currency baskets of both the broad and narrow groups of competitor countries resulted from the larger depreciation of the peso against the US dollar compared to the depreciation of the exchange rates of other currencies in these baskets. In terms of the real effective exchange rate index (REERI),[14] the index increased moderately by 2.9 percent against the currency basket of the country's major trading partners, reflecting the weakened external competitiveness of Philippine goods against those countries in the basket mainly on account of relatively higher domestic inflation. However, in the case of countries in both the broad and narrow baskets, the peso's external competitiveness strengthened as the REERI dropped by 2.8 percent and 9.2 percent,

[11] The NEER index represents the weighted average exchange rate of the peso vis-à-vis a basket of foreign currencies such as the US dollar, the Japanese yen, the Deutsche mark and the British pound. Major trading partners include the U.S., Japan, Germany and the U.K.
[12] The broad basket is composed of the currencies of Singapore, South Korea, Taiwan, Malaysia, Thailand, Indonesia and Hong Kong.
[13] The narrow basket is composed of the currencies of Indonesia, Malaysia and Thailand.
[14] The REER index is derived from the NEER index by adjusting for inflation differentials.

respectively. This developed on account of the higher nominal depreciation of the peso and the relatively lower domestic inflation vis-a-vis those of the countries in the broad and narrow baskets.

EFFECTIVE EXCHANGE RATE INDICES OF THE PESO
For periods indicated

		NEER			REER		
		MIC 1/	CC		MIC 1/	CC	
			Broad[2]	Narrow[3]		Broad[2]	Narrow[3]
2001	Jan	12.80	32.59	65.44	60.39	109.90	171.93
	Feb	13.53	34.46	69.71	63.98	114.69	181.88
	Mar	13.65	35.38	72.46	64.63	117.75	188.96
	Apr	13.29	35.60	74.44	63.04	118.19	192.04
	May	13.17	35.54	74.71	62.41	118.52	195.38
	Jun	12.99	35.00	73.47	61.88	118.10	193.65
	Jul	12.61	33.53	69.64	60.89	114.36	183.81
	Aug	12.76	31.77	62.56	61.70	108.47	166.15
	Sep	12.82	32.50	64.53	61.61	109.93	169.75
	Oct	12.79	33.29	67.42	61.57	111.59	176.25
	Nov	12.79	33.66	69.33	61.84	114.49	179.90
	Dec	12.95	31.04	67.95	63.06	110.46	175.70
Ave.	Jan-Aug	13.10	34.23	69.31	62.36	115.00	184.23
Ave.	Jan-Dec	13.01	33.70	69.31	62.25	113.87	181.28
2002	Jan	13.23	34.05	69.37	64.50	117.01	177.14
	Feb	13.31	33.92	68.75	64.90	113.96	173.53
	March	13.29	33.68	67.61	64.74	113.53	170.88
	April	13.28	33.21	65.91	64.73	111.99	165.41
	May	13.40	33.08	65.30	65.43	112.12	166.68
	June	13.10	31.87	62.60	64.03	108.87 e/	161.06 e/
	July	12.81	31.68	63.09	62.97	109.27 e/	162.79 e/
	Aug	12.57	31.14	61.92	62.15 e/	107.65 e/	160.66 e/
Ave.	Jan-Aug	13.12	32.83	65.57	64.17	111.80	167.27

1/ Major trading countries: USA, Japan, Germany and United Kingdom
2/ Competing countries (broad basket): Hong Kong, Singapore, South Korea, Taiwan, Malaysia, Thailand and Indonesia
3/ Competing countries (narrow basket): Indonesia, Malaysia and Thailand
e/ Estimates using the average inflation rate of the previous two months.