

BALANCE OF PAYMENTS DEVELOPMENTS JANUARY-JUNE 2002

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➤ Overall Position

The BOP yields a surplus due to the continued strength of the current account and lower net outflows in the capital and financial account.

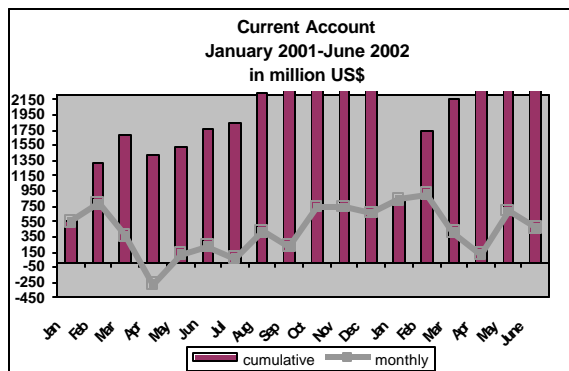
The country's balance of payments (BOP) in the first half of 2002 yielded a \$1,729 million surplus, a reversal of the \$606 million deficit recorded a year ago as both the current account and the capital and financial account continued to record strong performances (Table 1).

Balance of Payments (US\$ m)			
	Jan-June		Growth Rate (%)
	2002	2001	
I. Current Account	3445	1448	137.9
II. Capital & Fin'l.	-1488	-2249	33.8
III. Net Unclassified	-228	195	-216.9
IV. Overall BOP *	1729	-606	385.3
* Totals may not add up due to rounding.			

➤ Current Account

Stronger balances in merchandise trade and services as well as higher income receipts result in a higher current account to GNP ratio.

The current account surplus more than doubled to \$3,445 million in January - June 2002. This positive development stemmed mainly from the improved trade-in-goods balance, and the lower net outflow in the services account. The combined balance of these two accounts amounted to a net inflow of \$469 million. This compared favorably to the \$81 million net outflow in 2001. The more than twofold increase in the surplus in the income account to \$2,750 million also boosted the current account performance. The current account to GNP ratio for the first semester of 2002 reached 8.8 percent, more than twice the 4.0 percent level of a year ago.

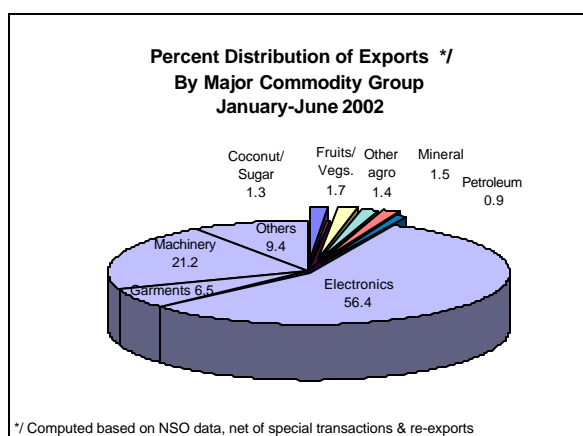




> Trade in Goods

Merchandise exports post consecutive double-digit growths from April to June, after more than a year of decline. The pick-up in global demand coupled with the government's two-pronged strategy in the new export plan—industry clustering to enhance competitive advantage and an aggressive marketing program in both old and new markets—helped push exports to record the third consecutive month of double-digit growth for 2002 after more than a year of decline.¹ This favorable development brought the year-to-date exports to \$16,260 million, 4.8 percent higher than year-ago level.² The strong export performance explained in part the increase in the volume of production index of key manufacturing enterprises for the first semester 2002.

In January-June 2002, the country's major export commodity earners remained to be electronics, machinery and transport equipment, and garments (Table 2.1).



- Electronics exports continue to rebound in June, while exports of machinery and transport equipment help boost export earnings.*
- a) *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 13.0 percent to \$3,287 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.
- b) *Electronics.* Electronic exports for the first half of 2002 rose by 5.0 percent to \$8,948 million, after posting three consecutive months of year-on-year increases since April 2002. The strong recovery in electronics exports was expected as the book-to-bill ratio continued to breach the demand-supply unity mark since March

¹ Industry clustering is a strategy aimed at strengthening the domestic base of an industry by putting and linking together similar businesses so as to ensure a steady supply chain. Industry clusters are usually privately-led initiative but the Government extends support to enhance the trade and investments environment.

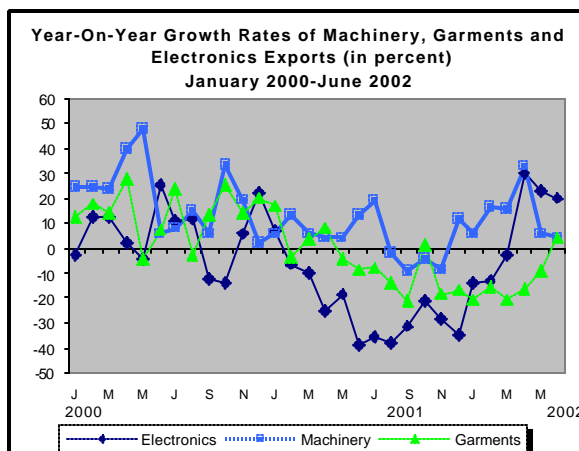
² Per BPM5 concept



2002, to reach 1.26 in June.³ Expanding Asian markets and the continued rebuilding of inventory for semi-conductors and electronic products provided the much-needed push of electronic exports.

To improve competitiveness and brace for stiffer market competition abroad, the leading electronic exporters groups with the aid of the government are hammering out a survival blueprint which will lay down an industry road map that will set the Philippines as a regional center for production design and as a transshipment point for testing and quality check for mass-assembled electronic goods from China that are in transit to Western markets.

- c) *Garments.* Exports of garments rebounded in June, posting a modest growth of 4.2 percent after months of year-on-year declines. This slowed down the year-to-date decline of garment exports to 12.9 percent to reach \$1,029 million. The twin strategies to tap the high-end markets from traditional quota-driven markets and the increased penetration of non-quota markets of Japan, United Arab Emirates, Hong Kong and Mexico have appeared to be paying off. The garments industry is gearing up for the worldwide full phase out of the quota system in 2004.



Growth in imports continues. Imports of goods went up for the fifth month in a row since February at 10.3 percent in June 2002 after peaking in April at 18.8 percent and tapering off in May at 3.9 percent. As a result, January-June imports reached \$15,308 million, 4.4 percent higher vis-à-vis last year's level and a reversal of the 0.9 percent decline registered in 2001.⁴ The rise in imports boosts expectations of sustained growth in exports in the coming months despite indications of tentative recovery in the U.S., the country's major trading partner. As a leading indicator, the positive import growth augurs well for the manufacturing sector in the second half of 2002. (Table 2.2).

³ 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 indicated that demand exceeds supply.

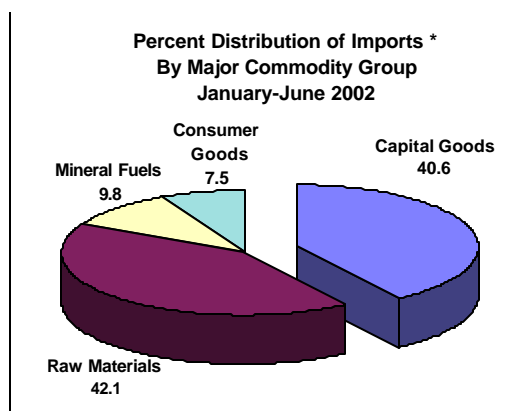
⁴ Per BPM5 concept



Capital goods imports grew by 5.5 percent to \$6,259 million, a reversal of the 3.1 percent decline in 2001. The expansion was traced to increased importations of telecommunication equipment? mainly inputs to electronics production? and office and EDP machines.

Meanwhile, imports of raw materials and intermediate goods—which accounted for more than two-fifths of total imports—expanded by 9.2 percent to \$6,493 million. Double-digit year-on-year growths ranging from 32 to 49 percent were noted in the importation of materials/accessories for the manufacture of electrical equipment starting February - June 2002.⁵ The increase in imported inputs for electronics exports and the growth in imports of capital goods for electronics production lend support to market expectations of an upturn in the electronics industry.

By contrast, imports of mineral fuels and lubricants performed the weakest among the major import commodity groups, falling by 12.8 percent to reach \$1,510 million during the period in review. This developed on account of the twin effect of the decline in the volume of imports and the price of petroleum crude. The average price of petroleum crude for the first half of 2002 dropped to \$22.51 per barrel from \$24.48 per barrel last year. Meanwhile, the decline in the volume of oil imports was attributed mainly to the: i) shutdown of some refinery units of oil companies because of excess capacity and for check-up and maintenance; and ii) high oil stockpile in 2001 following relatively weak domestic demand.



* Computed based on NSO data, net of special transactions

➤ Trade In Services

⁵ 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 22.0 percent during the review period as against the 8.5 percent decline in January-June 2001.



The deficit in the trade-in-services account narrows. The trade-in-services account in January-June 2002 posted a net outflow of \$482 million, 48.4 percent lower than the level in the comparable period in 2001 (Table 3). The narrowing of the deficit was triggered by lower net payments for transportation services and for miscellaneous business, professional and technical services. Meanwhile, increased net receipts from travel services, which rose by 36.4 percent to \$513 million, helped trim the net outflow in the services account during the period in review. This was due to the higher rate of decline in travel payments relative to that of travel receipts. The lower travel payments reflected in part the weaker peso and the government program to promote domestic tourism among local residents. The country's tourism industry is expected to regain lost ground following the aggressive promotion blitz of the government through new international marketing campaigns to showcase the country's tourism attractions. The government will also launch soon the "Visit Philippines 2003" in selected markets abroad. The programs are intended to target tourists from Japan, Taiwan, the U.S., Singapore, Australia, People's Republic of China, the United Kingdom, Hong Kong, South Korea and Germany. Recently, the governments of Thailand and the Philippines signed an agreement on tourism marketing strategies, which is expected to translate to a 25 percent increase in tourist traffic between the two countries in the next two years.

➤ Income

Higher OFW remittances and lower interest payments contribute to the income account surplus. The surplus in the income account for the first semester of the year increased by more than twofold to reach \$2.750 billion. Overseas Filipino workers' (OFWs) remittances, which continued to be a significant source of foreign exchange earnings, expanded by 43.2 percent to \$4.143 billion in January-June 2002 relative to the year-ago level. Contributing to this development was the increase in the number of deployed new hires and rehires OFWs, which rose by 4.1 percent during the review period. The growth in OFW deployment was noted in Europe, Africa and the Americas. By skills, the increase in deployed workers was noted mainly for transport equipment operators as well as professional, technical and related workers. The bulk of remittances from OFWs, which comprised about 92 percent of gross income receipts, came from the U.S., Saudi Arabia, Japan, Hong Kong and Singapore.⁶ The government continues to step up marketing missions to sell Filipino skills abroad. Prospects are bright, with the expanded hiring of the United Kingdom of OFWs in the medical field in the next three years. This development is expected to offset the impact of the trend towards "localization" and the economic slowdown experienced in some of the countries where Filipino workers are deployed.⁷

Meanwhile, the investment income account yielded a net outflow that was lower by

⁶ 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.

⁷ Localization means the preferential hiring by a country of its own residents.



12.4 percent relative to the level last year as interest payments on portfolio and other investments fell with the continued drop in global interest rates. The low global interest rate environment had a greater impact on the payment side than on the income side, thus affecting favorably the country's external transactions (Table 4).

➤ Current Transfers

The surplus in current transfers drops slightly. The net inflow from the current transfers account for January-June 2002 amounted to \$226 million, only \$1 million lower than the previous year's level (Table 5).

➤ Capital and Financial Account

Net inflows of portfolio investments help reduce the net outflow in the capital and financial account. The net outflow in the capital and financial account narrowed by 33.8 percent to \$1,488 million during the period in review. The reversal of the portfolio investment account to a net inflow of \$1,439 million from a net outflow of \$271 million last year dampened the negative impact of the higher net outflow of other investments and the lower net inflow of direct investments.

➤ Capital Account

The capital account posts a deficit. The capital account for January-June 2002 posted a net outflow of \$7 million compared to a balanced position for same period last year, reflecting mainly the net outflow of migrants' transfers (Table 6).⁸

➤ Direct Investments

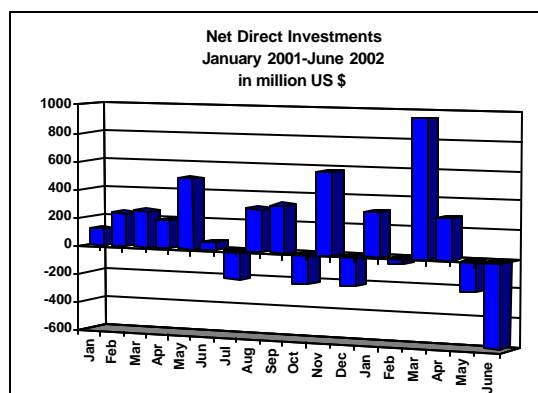
Higher direct equity investments by non-residents boost the direct Non-residents' investments in equity capital more than tripled to \$730 million during the period in review. The bulk of non-residents' equity investments came from Japan following the investment of \$544 million worth of shares by a Japanese firm in a local brewery company in March 2002. The rest was directed to other manufacturing companies, financial institutions and transport and storage services. Other major

⁸ 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.



*investment sources of direct investments were the U.S., U.K and Taiwan. (Table 7).
account.*

This notwithstanding, direct investments for January-June 2002 registered a lower net inflow of \$726 million compared with the year-ago level. The 46.7 percent drop was due mainly to repayments on intercompany loans, particularly in June and residents' placements of equity capital abroad.

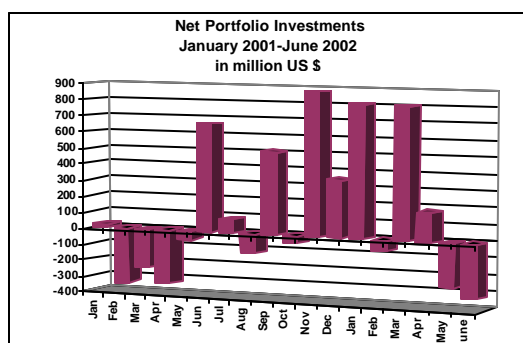


➤ Portfolio Investments

Higher non-residents' investments in equity and debt securities turn the portfolio investment account to a net inflow ...

From a net outflow of \$271 million in January-June 2001, portfolio investments for the first semester of 2002 reversed to a net inflow of \$1.439 billion due to increased non-residents' investments in resident-issued foreign denominated debt securities, particularly government-issued medium-term bonds.⁹ Non-residents' investments in equity securities also rose by 18.5 percent to \$339 million, indicating resurgence of investor confidence in the local equities market and as investors shifted investments to equity securities following relatively lower yield on bonds and other domestic financial instruments (Table 8).

⁹ 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.



➤ Other Investments

...while net outflow of other investments increases. The net outflow in the other investment account expanded by 9.2 percent to \$3.646 billion during the review period. This developed on account mainly of the higher net deposits abroad by resident banks to cover their clients' import payments and to diversify their portfolio (Table 9).

➤ Reserve Assets

NG deposits raise the GIR to \$16.9 billion. As of end-June 2002, the BSP's GIR rose to \$16.9 billion, 8.0 percent higher vis-à-vis end-December level of \$15.7 billion (Table 11).

The increase in GIR during the period was due mainly to foreign exchange inflows mainly in the form of net deposits by the Treasurer of the Philippines.¹⁰ However, these were partly offset by outflows to meet the foreign exchange requirements of the BSP and the National Government to service in part the obligations of the National Power Corporation.

The BSP's GIR were adequate to cover 5.4 months' worth of imports of goods and payment of services and income. Using other reserve coverage measures, the level of reserves was 3.2 times the amount of the country's short-term external debt based on original maturity or, alternatively, 1.5 times the amount of short-term external debt based on residual maturity.¹¹

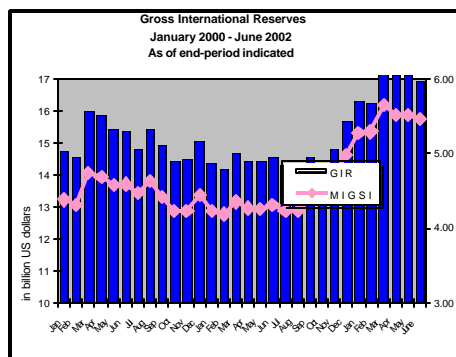
During the review period, the bulk of reserves consisted of foreign investments (79.9 percent), while the rest were in gold (15.5 percent), foreign exchange (3.9 percent), and combined SDRs and reserve position in the Fund (0.7 percent). In terms of the currency composition of reserves excluding gold, 94.1 percent were in US dollars, 2.4 percent in Japanese yen, 1.5 percent in pound sterling and the balance of 2.0 percent in

¹⁰ Sources of deposit were mainly from government borrowings, i.e., net proceeds of the RP US Securities Registered Global Bond (\$2042 billion) and JBIC Co-Financing of the Power Sector Loan (\$100 million)

¹¹ 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.



other foreign currencies.

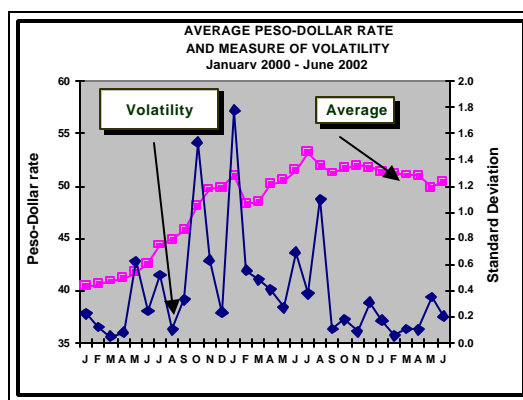


➤ Exchange Rate

The peso depreciates compared to the level last year... The peso-dollar exchange rate averaged ₱50.83:US\$1 in the first half of 2002, depreciating by 1.7 percent from the ₱49.99:US\$1 average exchange rate for the same period in 2001. The year-on-year depreciation of the peso reflected partly swings in sentiment on 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-June 2002, the standard deviation at ₱0.59 was substantially lower than the ₱1.50 registered for the same period in 2001. The peso-dollar exchange rate ranged from ₱49.336 to -₱51.72 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)¹² for the first semester of 2002 appreciated slightly by 0.2 percent against the currency basket of the country's major trading partners. However, the peso's NEERI depreciated by 4.2 percent against the currency basket of a broad group of competitor countries,¹³ and by 7.1 percent against the currency basket of a narrow group of competitor countries.¹⁴ 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),¹⁵ the peso appreciated by 3.2 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 owing mainly to the lower nominal depreciation of the peso relative to currencies of the countries in the basket during the review period. However, in the case of countries in both the broad and narrow baskets, the peso's external competitiveness strengthened as the REERI depreciated by 2.8 percent and 9.7 percent, 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 basket.

¹² 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.

¹³ The broad basket is composed of the currencies of Singapore, South Korea, Taiwan, Malaysia, Thailand, Indonesia and Hong Kong.

¹⁴ The narrow basket is composed of the currencies of Indonesia, Malaysia and Thailand.

¹⁵ The REER index is derived from the NEER index by adjusting for inflation differentials.



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-June	13.24	34.76	71.71	62.72	116.19	187.31
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 e/	108.93 e/	161.06 e/
Ave.	Jan-June	13.27	33.30	66.59	64.71	112.90	169.12

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.

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