BALANCE OF PAYMENTS DEVELOPMENTS
JANUARY-JUNE 2003

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➢ Overall Position

BOP for the first half of 2003 in deficit due to geopolitical concern and fears of SARS epidemic.

The geopolitical uncertainty and the SARS outbreak particularly in Asia had a significant adverse effect on the external accounts. The cumulative balance of payments (BOP) for the first half of the year yielded a $616 million deficit, a turnaround from the $1,729 million surplus registered in the comparable period last year. Nonetheless, the current account position has considerably improved in June posting a surplus of $587 million. Consequently, the resulting $114 million deficit for the second quarter of this year was significantly lower than $502 million deficit in the first quarter. (Table 1).

Balance of Payments (US$ m)

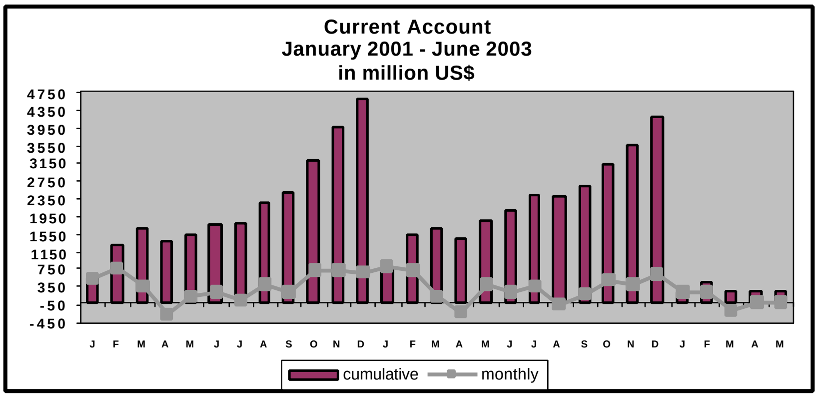
	January-June		
	2003	**2002**	**Growth Rate (%)**
I. Current Account	868	2084	-58.3
II. Capital & Fin'l.	-2439	1682	-245.0
III. Net Unclassified	955	-2037	146.9
IV. Overall BOP *	**-616**	**1729**	**-135.6**

* Totals may not add up due to rounding.

➢ Current Account

The current account remains in surplus.

The continued strength of the income account brought the current account to a $868 million surplus in January-June, albeit, lower compared to the $2,084 million surplus posted in the comparable period last year. Contributing to the lower current account inflow was the reversal of the trade-in-goods account into a deficit and the further weakening in the services account.



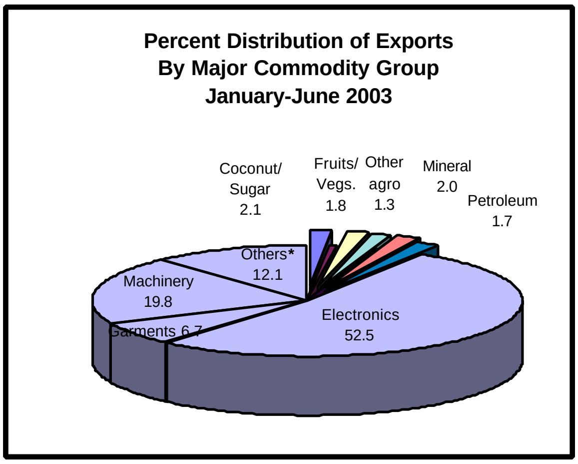
➢ Trade-in-Goods

The surge in imports causes the trade-in- goods deficit.

The trade-in-goods balance for the first semester reversed to a deficit of $1,309 million from a surplus of $116 million in the same period last year, underpinned by the frontloading of imports in the first three months of the year as the U.S.-Iraq conflict escalated. Total imports of goods at $17,949 million accelerated to 10.9 percent growth, in stark contrast to the slowing pace in exports.[1]

Export growth tapers off.

Exports continued to exhibit mixed trend, climbing up during the first three consecutive months of 2003 then sliding down in April and May before rebounding in June at 4.2 percent year-on-year. This resulted in a modest cumulative growth of 2.1 percent that ended the first semester with $16,640 million export earnings. This growth was lower compared to 5.1 percent posted same period last year.



* Includes special transactions & re-exports net of returned goods and temporary exports

[1] Based on BPM5

Electronics exports decline.

a) *Electronics.* As SARS continued to dampen global economic outlook, exports of electronics, which comprised 52.6 percent of total exports, remained sluggish, declining by 2.5 percent in the first six months. (Table 2.1). However, the electronics industry is confident of a modest comeback towards the second half of the year with the expectation of recovery in business and consumer confidence particularly in the U.S. The book-to-bill ratio tended to support the industry's optimism with the ratio inching up towards the unity mark, from 0.90 in May to 0.93 in June.[2]

Machinery and transport equipment at standstill .

b) *Machinery and Transport Equipment*. Exports of machinery and transport equipment—the second largest export earner next to electronics— posted a flat growth in the first semester to $3,287 million. The weak performance was influenced in part by the softening demand for electronics exports since nearly 60 percent of exports from this commodity group consisted of input/output peripheral units of computers. Exports of other major product lines of machinery transport and equipment such as parts and accessories of motor vehicles also slowed down from the level posted in the comparable period last year.

Garments exports rebound.

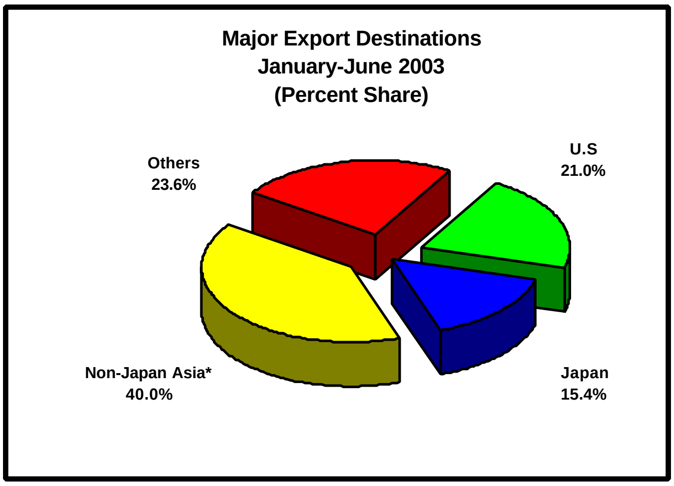
c) *Garments.* Exports of garments representing 6.7 percent of total exports for the first half of 2003, sustained a strong growth path that started late last year to post a 9.1 percent growth in the first semester. This compared favorably with last year's contraction of 12.9 percent. The industry attributed the strong performance to the almost full utilization of the annual quota (largely to the U.S. market) in the initial months. A better long-term outlook rests on the implementation of the twin strategies of tapping the high-end segment in traditional quota-driven markets and increasing access to non-quota markets such as Japan, United Arab Emirates, Hong Kong and Mexico. Along with these strategies set in the Garments Industry Transformation Plan (GITP) is a comprehensive program that focuses on cost reduction, productivity enhancement, market and product development, trade facilitation and the re-engineering of the garments industry to improve competitiveness and meet the challenges of the quota phase-out in 2005.

Intra-Asian trade continues with Hong Kong as the top Non-Japan export market.

Non-Japan Asia continued to corner the biggest share of Philippine exports at 41.6 percent, picking up the slack in demand from major traditional markets such as US and Japan. Hong Kong emerged as the top non-Japan export market in the first semester as it overtook Singapore and Taiwan, the economies that ranked highest in the comparable period a year ago. Shipments to Hong Kong increased by 51.2 percent. However, the People's Republic of China remained the most dynamic market, as it consistently increased its demand for Philippine products at double-digit pace, which in the first semester was

[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.

recorded at 44.9 percent. This could be explained by the intracompany shipments largely of electronics products in which the production and marketing processes have been relocated in many parts of Asia, with China hosting most of the newly established companies.



' Comprised of China, Hong Kong, South Korea, Singapore, Taiwan, Malaysia and Thailand.

Imports grow at decelerating pace.

Imports of goods in the first semester posted a 10.9 percent expansion, characterized by a first quarter surge arising from the U.S.-Iraq war concerns, and a dip in the second quarter as the geopolitical tension eased up. The first semester performance, at $17,949 million, was a turnaround from the 4.0 percent contraction last year.(Table 2.2).[3]

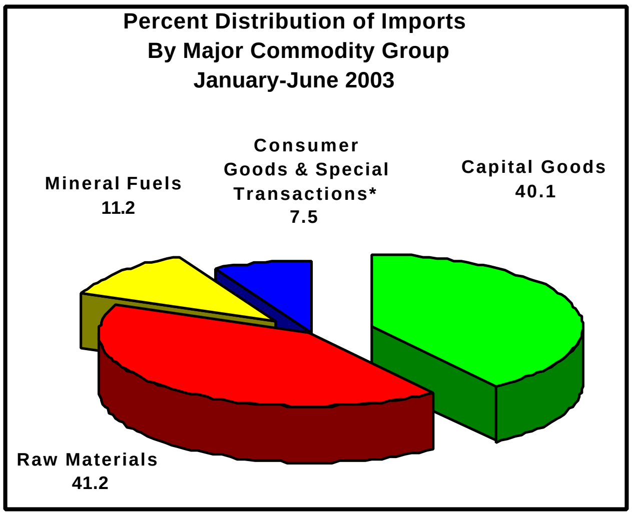
Imports of raw materials and intermediate goods—which comprised almost 41 percent of total imports—grew by 1.4 percent to $7,396 million. This was a reversal from the 10.4 percent contraction last year. The commodities that primarily contributed to growth of this group were chemicals, particularly chemical compounds and artificial resins, and manufactured goods such as iron and steel, non-ferrous metals and paper and paper products.

Imports of capital goods, comprising about 40 percent of total imports, climbed by 14.2 percent (from only 6.3 percent last year) during the first semester of 2003 to reach $7,197 million. The expansion was influenced largely by imports of telecommunications equipment and land transport

[3] Based on BPM5 concept

equipment excluding passenger cars and motorized cycles.

Imported mineral fuels and lubricants, comprising 11.2 percent of total imports, posted a robust growth of 30.7 percent to reach $2,006 million during the period in review, due to the combined effects of the increase in both the volume and price of petroleum crude. The volume of petroleum crude imports grew by 17.9 percent to 50.7 million barrels in the first semester from 43.0 million barrels in the comparable period last year. The stock build-up was mostly in the first quarter when the government directed oil companies to maintain at least 30-day oil inventory for big oil players and 15 days for small oil players to ensure continued domestic oil supply.[4] The average price of petroleum crude during the review period rose sharply to $27.69 per barrel from $22.51 per barrel during the same period last year, with the average price peaking at $30.06 per barrel in February. Price of petroleum crude has gradually eased up, settling at $25.86 per barrel in June.



* Computed based on NSO data, net of special transactions

➢ Trade In Services

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

The decline in net travel receipts and the rise in import-related freight payments brought the trade-in-services account to a net outflow of $827 million in the first semester. This represented a 56.3 percent increase from the level in the comparable period in 2002. Net inflows from travel dropped by 37.2 percent to $322 million following geo-political uncertainty and the SARS outbreak. Tourist arrivals dropped by 11.5 percent consequently bringing down travel receipts by 27.6 percent to $712 million in the review period. The drop in the number of tourist arrivals was most evident in countries such as the U.S., Japan, Korea, Hong Kong, Taiwan, Singapore and Australia.

Meanwhile, the increase in the net outflow of transportation services was

[4] On 7 April 2003, the government announced the reduction of the minimum oil inventory to 7-15 days following the easing of hostilities in the Middle East.

due to higher freight expenditures following the increase in imports of goods. Moreover, with domestic shipping companies having pulled out of international routes due to high maintenance costs, importers have increased their reliance on foreign carriers for shipment of their goods (Table 3).

➢ Income

OFW remittances remain strong.

The income account grew by 18.7 percent at $2,698 million as Overseas Filipino Workers' (OFWs) remittances in the first semester rose by 8.0 percent while the net outflow in investment income dipped by 10.4 percent. Despite the 5.1 percent decline in deployment, OFW remittances grew to $3,880 million during the first half of the year from $3,592 million in the comparable period last year on account of the increasing share of higher-paid professionals among the deployed (i.e., engineers, caregivers, performing artists, clerks and sales workers). The decline in total deployment to 459,260 in the first semester from 484,169 last year was attributed to SARS outbreak, the temporary suspension of deployment in Hong Kong because of the minimum wage cut issue and the first quarter threat of war? all of which contributed to the 7.8 percent decline in the deployment of land-based workers.[5] However, these developments had not affected the deployment of sea-based workers as their number increased by 4.3 percent.

Considered to be one of the drivers of economic growth, the government continues to pursue programs that will enhance the competitiveness of OFWs. In line with this, the government is promoting technical education and training programs for OFWs such as foreign language instruction for Filipino nurses; specialized training for household workers and performing artists; and skills proficiency schemes for information technology (IT) professionals. Furthermore, government initiatives/efforts are underway to improve/facilitate overseas remittances particularly from the United States.

Likewise, the government addresses the emerging trend towards "localization" and the economic slowdown in host economies by exploring and expanding access by Filipino overseas workers to other economies.[6]

Meanwhile, the $1,182 million net outflow in the investment income account was 10.4 percent lower than the $1,319 million recorded in the comparable period a year ago. The slowdown in non-resident foreign direct investments reduced income payments on equity investments and other investments. Meanwhile, notwithstanding decline in global interest rates, interest payments on debt increased due to higher level of external liabilities. (Table 4)

[5] Of the total number of Filipino workers deployed abroad for the period January-June 2003, 349,114 were land-based workers and 110,146 were sea-based workers.
[6] Localization means the preferential hiring by a country of its own residents.

➢ Current Transfers

The surplus in current transfers increases.

Net current transfers for the first semester amounted to $306 million, 36.6 percent higher than the level posted in the same period last year (Table 5). The improvement was accounted for by the transfer of income by migrant workers as well as receipts in the form of gifts, grants and donations from individuals and non-governmental institutions.

➢ Capital and Financial Account

The capital and financial account reverses to a deficit.

The capital and financial account reversed to a net outflow of $2,439 million for the first semester from a net inflow of $1,682 million posted in the same period in 2002. Investors continued to stay in the sidelines, awaiting forecast of a better economic outlook. During the review period, both the direct investment account and the portfolio investment account posted substantially lower net inflows.

➢ Capital Account

The capital account registers a higher net outflow.

The capital account for the first semester posted a higher net outflow of $11 million relative to a net outflow of $7 million in the comparable period last year owing to the increase in the net outflow of migrants' transfers (Table 6).[7]

➢ Direct Investments

Direct investments slow down due to fragile global economic outlook.

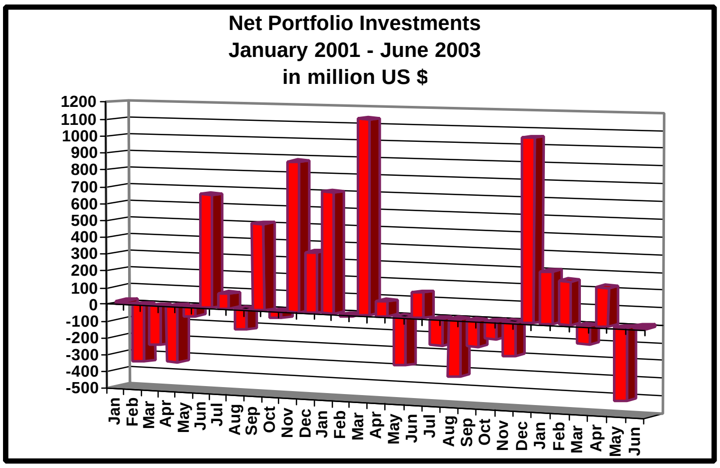
The infusion of fresh equity capital in June buoyed up the direct investment account to end the first semester at a surplus of $10 million, a slight turnaround from the net outflow for the first five months of 2003. However, this was significantly lower from last year's surplus of $847 million as investors wait for firmer indications of a global recovery. Non-residents' investments in equity capital dipped to $121 million for the first semester 2003 compared to $730 million in the same period last year, with the biggest drop in investments posted in the manufacturing sector. The bulk of the equity capital inflows were channeled mainly to the manufacturing and construction industries as well as financial intermediation services and real estate. The $60 million net outflow in other capital representing net repayment of intra-company loans however, pared down net inflows in foreign equity capital in the Philippines (Table 7).

➢ Portfolio Investments

[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 influence consumption of goods and services.

The portfolio investment account declines but remains in surplus.

The portfolio investment account in the review period managed to post a $258 million surplus despite the persistently subdued investment climate. However, this was substantially below the $1,451 million surplus realized in the same period last year. The lower surplus was due to the substantial increase in residents' investments abroad, particularly local banks' holdings of non-residents' debt instruments. Another factor was the 66.4 percent contraction in non-residents' investments in equity securities on account of weak corporate profit that had driven the market towards investments in fixed-income debt instruments, which grew by 14.1 percent in the period under review (Table 8).



➢ Other Investments

The net outflow of other investments increases.

During the review period, the net outflow in the other investment account at $2,696 million was significantly higher than the level posted in the comparable period last year. Largely accounting for the increase in net outflow was the net repayment of loans by the National Government and the increase in banks' net loans receivables from foreign banks (Table 9).

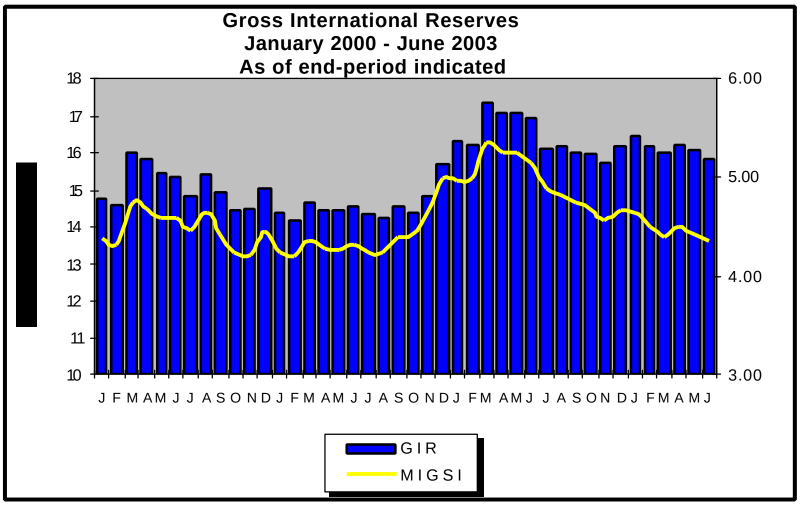
➢ Reserve Assets

International reserves remain adequate at $15.9 billion.

The BSP's gross international reserves (GIR) stood at $15.9 billion as of end-June 2003. This was lower than the end-December 2002 level of $16.2 billion. The decline in reserves during the period was due mainly to drawdown from reserves to service debt requirements of the National Government and the BSP.

The BSP's GIR were adequate to cover 4.4 months' worth of imports of goods and payment of services and income. Using other reserve coverage measures, the level of reserves was 2.5 times the amount of the country's short-term external debt based on original maturity or, alternatively, 1.3 times the amount of short-term external debt based on residual maturity.[8]

During the quarter in review, the bulk of reserves consisted of foreign investments (76.4 percent), while the balance was in the form of gold (19.1 percent), foreign exchange (3.7 percent), and combined SDRs and reserve position in the Fund (0.8 percent). In terms of the currency composition of reserves excluding gold, 83.7 percent were in US dollars, 9.5 percent in Euros, 3.9 percent in Japanese yen, 1.7 percent in pound sterling and the balance of 1.3 percent in other foreign currencies.



➢ Exchange Rate

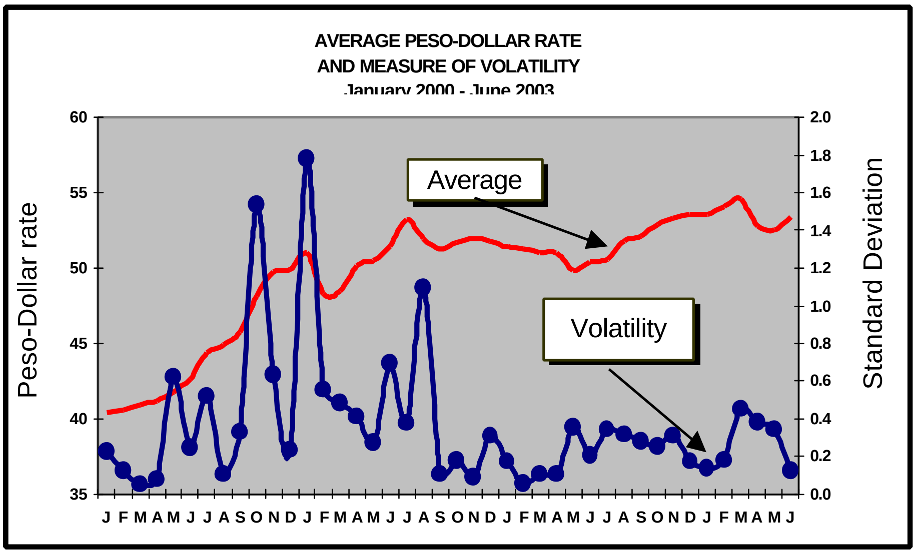
The peso depreciates relative to the previous year's level.

The nominal peso-dollar exchange rate averaged ₱53.49/US$1 in January-June 2003, depreciating by 5.2 percent from the ₱50.83/US$1 average exchange rate in January-June 2002. The depreciation of the peso reflected mainly the increase in corporate demand in the first quarter following the surge in imports due in turn to the conflict in Iraq and fears of the lower dollar supply ahead due to the SARS outbreak in the second quarter. The persisting concerns over the budget deficit and domestic security also negatively affected the sentiment on the peso.

The peso is more volatile.

The peso was more volatile in the first half of 2003, as shown by higher standard deviation of ₱0.77 compared with the year-ago level of only ₱0.59. To address the excessive peso volatility arising from speculative demand particularly in March and pre-empt possible impact on inflationary expectation, the BSP introduced a number of measures.[9] Following these measures, the peso stabilized considerably. The peso-dollar exchange rate ranged from ₱52.021/US$1 to ₱55.075/US$1 during the period.

[8] 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.
[9] Among the measures implemented by the BSP were: a) the reduction of the allowable overbought position of banks to 2.5 percent of unimpaired capital or US$5 million, whichever is lower, b) limiting the tenor of forward contracts to a maximum of 6 months, c) imposing appropriate sanctions against banks violating BSP foreign exchange regulations, d) raising the liquidity reserve requirement by one percentage point from 7 percent to 8 percent; and e) removing the tiering scheme for banks' short-term deposits under BSP's Reverse Repurchase Facility and Special



Higher nominal depreciation and relatively lower domestic inflation strengthen the peso's external competitiveness.

Relative to the previous year's level, the peso's average nominal effective exchange rate (NEER) index[10] for the first six months of 2003 depreciated by 12.5 percent against the currency basket of the country's major trading partners, 9.6 percent against the currency basket of a broad group of competitor countries,[11] and by 11.2 percent against the currency basket of a narrow group of competitor countries.[12] This was due to 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 (REER) index,[13] the peso gained external price competitiveness as the REER depreciated by 11.7 percent against the currency basket of the country's major trading partners. Relative to the currencies of countries in both the broad and narrow baskets, the peso's external competitiveness improved as the REER depreciated by 8.7 percent and 12.2 percent, respectively, due mainly to the higher nominal depreciation of the peso and the relatively lower domestic inflation vis-à-vis those of the countries in the broad and narrow baskets.

Deposit Accounts.

[10] 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 euro and the British pound. Major trading partners include the U.S., Japan, European Monetary Union and the U.K.

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

[12] The narrow basket is composed of the currencies of Indonesia, Malaysia and Thailand.

[13] The REER index is derived from the NEER index by adjusting for inflation differentials.

		NEER			REER		
EFFECTIVE EXCHANGE RATE INDICES OF THE PESO For periods indicated							
		MIC 1/	**CC**		**MIC 1/**	**CC**	
			Broad2	**Narrow3**		**Broad2**	**Narrow3**
2001	Jan	114.35	32.59	64.78	62.13	109.90	171.13
	Feb	15.24	34.46	69.00	65.96	114.69	181.02
	Mar	15.37	35.38	71.71	66.42	117.75	187.98
	Apr	15.01	35.60	73.65	64.74	118.19	191.46
	May	14.95	35.54	73.91	64.38	118.52	194.50
	Jun	14.82	35.00	72.67	64.37	118.10	192.44
	Jul	14.35	33.53	68.91	62.91	114.36	182.79
	Aug	14.39	31.77	62.11	63.14	108.47	165.76
	Sep	14.45	32.50	63.90	63.39	109.93	168.92
	Oct	14.42	33.29	66.77	63.40	111.59	175.46
	Nov	14.48	33.66	68.61	63.98	114.49	178.93
	Dec	14.61	31.04	65.60	64.87	110.46	170.57
Ave.	**Jan-Dec**	**14.70**	**33.70**	**68.47**	**64.14**	**113.87**	**180.08**
2002	Jan	14.74	32.99	65.99	65.88	113.22	174.31
	Feb	14.87	32.88	65.42	66.31	110.28	170.85
	Mar	14.84	32.69	64.38	66.01	109.93	168.33
	April	14.81	32.28	62.80	65.65	108.74	163.48
	May	14.87	32.17	62.40	66.02	108.92	165.15
	June	14.45	31.02	59.78	64.29	106.01	159.66
	July	14.06	30.81	60.27	62.78	106.30	161.19
	Aug	13.83	30.28	59.10	61.92	104.80	159.11
	Sep	13.76	30.27	58.92	61.60	103.94	157.23
	Oct	13.63	30.25	58.88	60.90	102.75	155.39
	Nov	13.38	29.77	58.19	59.84	102.05	152.14
	Dec	13.29	29.54	57.49	59.68	100.80	150.05
Ave.	**Jan-June**	**14.76**	**32.34**	**63.46**	**65.69**	**109.52**	**166.96**
Ave.	**Jan-Dec**	**14.21**	**31.24**	**61.13**	**63.41**	**106.48**	**161.41**
2003	Jan	13.02	29.24	57.14	58.35	100.72	147.64
	Feb	12.87	29.05	56.61	57.92	98.83	146.17
	Mar	12.74	29.03	56.18	57.07	98.62	145.53
	April	13.17	29.94	57.68	59.03	101.68	148.22
	May	12.95	29.42	56.27	58.13	100.71	147.23
	June	12.71	28.65	54.36	57.56	99.48	144.37
Ave.	**Jan-June**	**12.91**	**29.22**	**56.37**	**58.01**	**100.01**	**146.53**

1/ Major trading countries: USA, Japan, European Monetary Union (EMU) 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.