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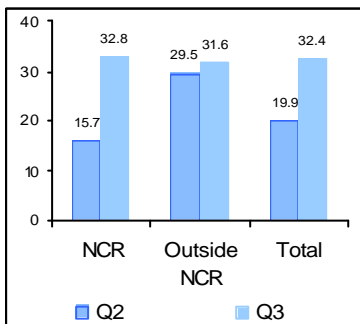
**Business Optimism Continues  
For the Second and Third Quarters of 2004\***

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**Overall business outlook**

*Business outlook show continuing optimism for the second and third quarters of 2004.*

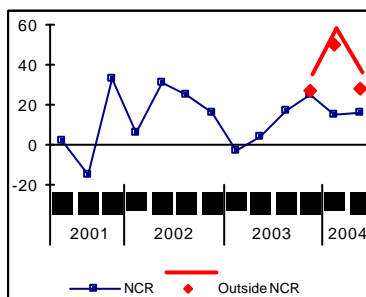
Overall Business Outlook  
Diffusion Index: 2004 Q2 and Q3



In the survey conducted during the whole month of April 2004, business sentiment showed increasing confidence in the economy in the next two quarters of 2004. For these two quarters, the overall business outlook diffusion indices (DI) were recorded at 19.9 percent and 32.4 percent, respectively (Table 1).<sup>1</sup>

The overall outlook index for second quarter of 2004 remained positive but declined to 19.9 percent from 26.0 percent in the first quarter of 2004. This was due mainly to the decline in business sentiment in areas outside the National Capital Region (NCR), which went down to 29.5 percent from a high of 50.5 percent in the previous quarter. Business outlook in the NCR, however, improved slightly from 15.1 percent to 15.7 percent during the same period (Table 2).

Current Quarter Business Outlook  
Q2: 2004



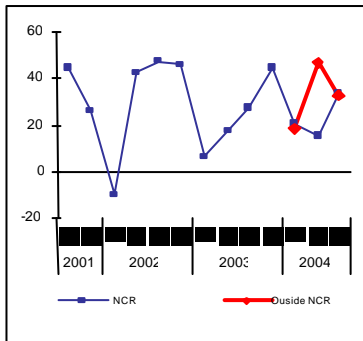
While the expected increase in consumer demand contributed to the more positive business outlook in the first quarter of 2004, the growing political uncertainty on the election results dampened the business outlook for the second quarter. Business outlook of firms in areas outside NCR was affected more by political uncertainty than those in the NCR.

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\* This survey covers respondents from the NCR and Regions I, VII and XI.

<sup>1</sup> The diffusion Index (DI) is computed as the percentage share of firms that answered in the affirmative less percentage share of firms that answered negative in a given indicator. A positive DI indicates a favorable view, except for the average inflation rate and the average peso-borrowing rate, where a positive DI indicates the opposite. Please note that all index figures are diffusion indices.

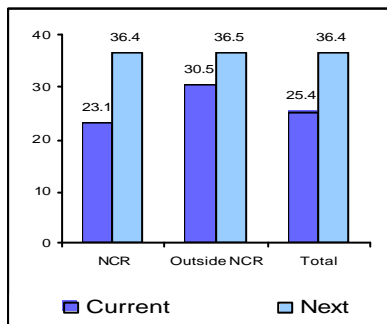
**Current Quarter Business Outlook  
Q2: 2004**



For the third quarter of 2004, the overall business outlook diffusion index increased to 32.4 percent compared to the 25.2 percent recorded in the previous quarter. The DIs for the third quarter of 2004 for the NCR respondents increased to 32.8 percent from 15.7 percent during the previous quarter, but respondents outside NCR projected a lower index of 31.6 percent compared to 46.6 percent for the same periods. The increases in the diffusion indices for the third quarter indicate that respondents expect growth to accelerate after the elections.

**Business-related factors**

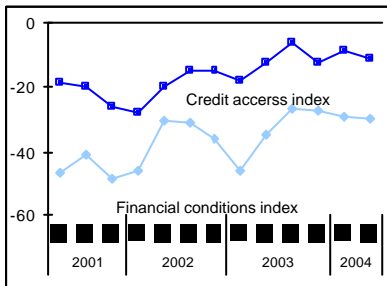
**Volume of Business Activity**



Expectations of accelerating growth in the economy were further confirmed as majority of the firms projected brisk volume of business in the second quarter, and more so in the third quarter of 2004, with indices of 25.4 percent and 36.4 percent, respectively. This sentiment is reflected particularly in the volume of business activity index for NCR respondents, which increased to 23.1 percent in the second quarter from 2.3 percent in the first quarter, and then accelerated to 36.4 percent in the third quarter of 2004. The corresponding index outside NCR likewise increased to 30.5 percent in the second quarter from 16.0 percent in the first quarter, then continuing its momentum in the third quarter at 36.5 percent (Table 2).

**Access to Credit**

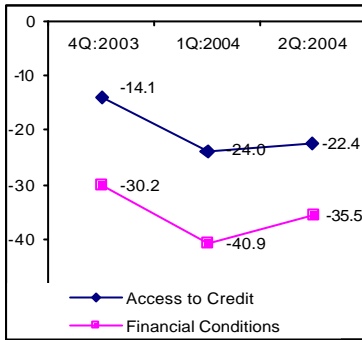
**NCR**



Indices for business-related factors showed more tightening financial conditions in the NCR. More respondent firms anticipate financing problems, with the credit access index declining to -11.1 percent from -8.7 percent in the previous quarter.<sup>2</sup> Likewise, the financial conditions index, which is an indicator of the internal financial prospects of firms, declined slightly to -29.6 percent from -29.2 percent in the previous quarter (Table 2).<sup>2</sup>

<sup>2</sup> The financial conditions index reflects the respondents' judgment on their general cash position, taking into account the level of cash and other cash items and repayment terms on loans. The access to credit index refers to the environment external to the firm, particularly the availability of credit from the banking system or other financial institutions.

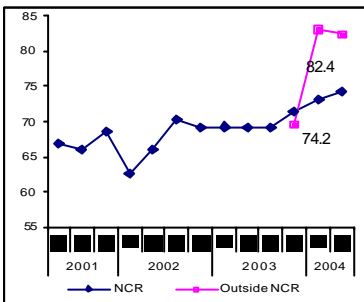
## Outside NCR



In areas outside NCR, more respondent firms anticipate easier access to credit and better financial conditions compared to the previous quarter. The credit access index for non-NCR respondents improved to -22.4 percent from -24.0 percent, while the financial conditions index also increased to -35.5 percent from -40.9 percent (Table 2).

## Capacity Utilization

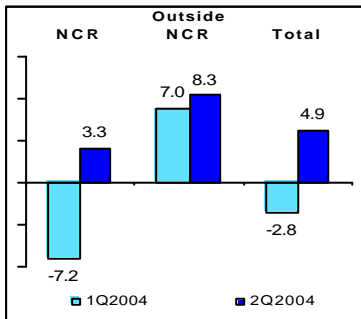
Q2 2004



Consistent with positive expectations in the next two quarters, the average capacity utilization in the industry sector improved slightly to 76.7 percent for the second quarter from 76.2 percent in the previous quarter. This was due largely to the increase in capacity utilization of firms in the NCR from 73.0 percent in the first quarter to 74.2 percent in the second quarter. Meanwhile, average capacity utilization for firms outside NCR remained higher than that for NCR firms but decreased slightly to 82.4 percent from 83.2 percent for the same periods (Table 2).<sup>3</sup>

## Employment Outlook

Q2: 2004



The overall employment outlook index entered positive territory at 4.9 percent for the second quarter of 2004 from -2.8 percent in the previous quarter. The increase in employment index is consistent with the anticipated increase in business activity in the next two quarters. The index for NCR climbed to 3.3 percent from -7.2 percent in the previous quarter. Likewise, the index outside NCR increased to 8.3 percent in the second quarter from 7.0 percent in the first quarter (Table 2).

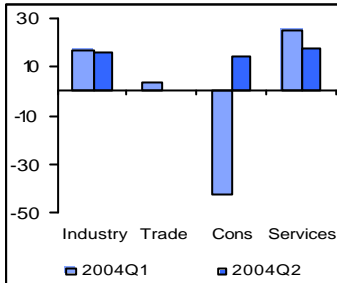
Only 15.6 percent of the respondent firms in the industry sector indicated plans for expansion in the third quarter of 2004. This could be due to the uncertainty of election results and the still ample spare production capacity in the sector. NCR firms however, were more optimistic with 18.3 percent indicating expansion plans compared to 12.4 percent among non-NCR respondents (Table 3).

<sup>3</sup> The average capacity utilization of 76.7 percent in the second quarter 2004 of the BES sample firms from the industry sector in Metro Manila and the three selected regions differs from the average capacity utilization figures of 78.4 percent from January-February 2004 of the National Statistics Office (NSO), which were computed based on a sample of large manufacturing firms nationwide.

## Confidence indicators

*Strong business confidence in industry, construction and services*

Business Confidence Index  
Q2 2004



Consistent with the optimistic business outlook for the next two quarters, business confidence showed positive indices in the second quarter. The confidence index for the services sector was most optimistic at 17.7 percent, followed by the industry sector at 16.8 percent and the construction sector at 14.5 percent. The index for the wholesale and retail trade was weak but still positive at 0.1 percent (Table 4).

## Sub-sector outlook

*Manufacturing remains as the major source of optimism in the industry sector for the second and third quarters of 2004.*

The industry sector continued to show positive expectations with diffusion indices of 22.3 percent in the second quarter and 30.6 percent in the third quarter of 2004. The manufacturing sub-sector remains as the major contributor to the optimistic industry expectations, with indices at 22.9 percent in the second quarter and improving to 31.2 percent in the third quarter. The positive outlook came particularly from firms outside NCR, which recorded indices of 30.4 percent and 39.1 percent, for the second and third quarters, respectively (Table 1).

*Business services and hotels and restaurants drive business optimism in the services sector for the second and third quarters of 2004.*

The services sector maintained its optimistic outlook with overall diffusion indices of 26.7 percent and 39.6 percent in the second and third quarters of 2004, respectively. The services sector in the NCR recorded a 24.7 percent DI in the second quarter and improved considerably to 41.4 percent in the third quarter. The services sector in areas outside NCR posted a 46.6 percent DI in the second quarter but this decelerated to 20.5 percent in the next quarter. Main contributors to this optimism are firms engaged in business services with 45.6 percent and 71.0 percent diffusion indices; and hotels and restaurants with 40.0 percent and 26.1 percent diffusion indices for the second and third quarters, respectively (Table 1).

## Business constraints

*Stiff competition and low demand continue to constrain business activities in the second quarter of 2004.*

Around 67 percent of respondent firms cited stiff competition while 57 percent mentioned low demand as the major factors that constrain production and business activity in the second quarter. Other major factors cited by respondent firms were unclear economic laws, high interest rates, financial problems and limited access to credit (Table 5).

## Expectations on key economic indicators

*A higher peso borrowing rate, a higher inflation rate and a stronger peso is expected in the third quarter of 2004.*

Survey respondents anticipate a higher peso-borrowing rate in the second quarter of 2004 as the corresponding diffusion index registered 38.7 percent. They likewise expect a relatively higher inflation rate with an index of 52.0 percent and a weaker peso to US\$ rate with an index of -1.5 percent. Expectations for the third quarter of 2004 likewise indicated higher interest rates and inflation rates, but respondents anticipate a strengthening of the peso with a positive diffusion index of 0.2 percent. The anticipated strengthening of the peso could be attributed to the expectations of more stable political conditions and increased economic activity after the elections (Table 6).

## TECHNICAL NOTES

Beginning in the fourth quarter of 2003, to provide a regional dimension to business prospects, the BES survey coverage was expanded to include regions outside the NCR. The expanded BES coverage consists of firms in SEC's Top 5000 Corporations in 2002 which are based in NCR and three selected regions: Region I, Region VII and Region XI. From each of these regions, a stratified random sample of 650 firms was selected across four major economic groups and 12 sub-groups namely: Group 1: Industry, which consists of manufacturing, mining and quarrying, electricity gas and water and agriculture fishery and forestry; Group II: Construction; Group III: Wholesale and Retail Trade and Group IV: Services Sector, which consists of financial intermediation, real estate, renting and business activities, hotels and restaurants, transport, storage and communication and community, social and personal services. The combined survey response rate for this quarter is 66 percent. The response rate is 77 percent for NCR and 39 percent for the selected regions outside NCR. It is worth noting that 31.8 percent of respondents belong to the small-firm category employing less than 100 workers. The distribution of sample size by region is found below.

SECTOR	Population					Sample				
	NCR	I	VII	XI	Total	NCR	I	VII	XI	Total
<b>Industry</b>	<b>1121</b>	<b>6</b>	<b>127</b>	<b>22</b>	<b>1276</b>	<b>143</b>	<b>6</b>	<b>49</b>	<b>22</b>	<b>220</b>
Agriculture, Fisheries and Forestry	38	0	5	14	57	7	0	2	14	23
Mining and Quarrying	18	0	1	1	20	2	0	0	1	3
Manufacturing	974	5	117	7	1103	129	5	45	7	186
Electricity, Gas and Water Supply	39	1	4	0	44	5	1	2	0	8
<b>Construction</b>	<b>142</b>	<b>1</b>	<b>8</b>	<b>3</b>	<b>154</b>	<b>19</b>	<b>1</b>	<b>3</b>	<b>3</b>	<b>26</b>
<b>Wholesale and Retail Trade</b>	<b>1051</b>	<b>24</b>	<b>63</b>	<b>12</b>	<b>1150</b>	<b>140</b>	<b>24</b>	<b>25</b>	<b>12</b>	<b>201</b>
<b>Services</b>	<b>1199</b>	<b>12</b>	<b>59</b>	<b>10</b>	<b>1280</b>	<b>158</b>	<b>12</b>	<b>23</b>	<b>10</b>	<b>203</b>
Hotels and Restaurant	110	4	4	0	134	15	4	2	0	21
Transport, Storage and Communications	199	1	13	5	210	26	1	5	5	37
Financial Intermediation	347	1	13	1	356	45	1	5	1	52
Real Estate	172	3	14	1	180	23	3	5	1	32
Renting and Business Activities	245	0	8	1	216	32	0	3	1	36
Community, Social and Personal Services	126	3	7	2	140	17	3	3	2	25
<b>TOTAL NUMBER OF FIRMS</b>	<b>3513</b>	<b>43</b>	<b>257</b>	<b>47</b>	<b>3860</b>	<b>460</b>	<b>43</b>	<b>100</b>	<b>47</b>	<b>650</b>

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**Table 1. INDICES OF OVERALL BUSINESS OUTLOOK BY SECTOR <sup>1/</sup>**

Second and Third Quarters of 2004

Sectors	Number of Respondents			Index Points					
				Current Quarter April - June			Next Quarter July - September		
	NCR	Outside NCR	Total	NCR	Outside NCR	Total	NCR	Outside NCR	Total
<b>All Sectors</b>	<b>354</b>	<b>75</b>	<b>429</b>	<b>15.7</b>	<b>29.5</b>	<b>19.9</b>	<b>32.8</b>	<b>31.6</b>	<b>32.4</b>
<b>Industry</b>	<b>111</b>	<b>26</b>	<b>137</b>	<b>16.4</b>	<b>29.0</b>	<b>22.3</b>	<b>22.9</b>	<b>39.4</b>	<b>30.6</b>
of which:									
Manufacturing	99	23	122	16.2	30.4	22.9	24.2	39.1	31.2
<b>Construction</b>	<b>13</b>	<b>2</b>	<b>15</b>	<b>-23.1</b>	<b>0.0</b>	<b>-17.4</b>	<b>15.4</b>	<b>50.0</b>	<b>23.9</b>
<b>Wholesale and Retail Trade</b>	<b>93</b>	<b>25</b>	<b>118</b>	<b>9.7</b>	<b>24.0</b>	<b>13.3</b>	<b>35.5</b>	<b>16.0</b>	<b>30.5</b>
<b>Services</b>	<b>137</b>	<b>22</b>	<b>159</b>	<b>24.7</b>	<b>46.6</b>	<b>26.7</b>	<b>41.4</b>	<b>20.5</b>	<b>39.6</b>
of which:									
Financial Intermediation	45	5	50	17.8	20.0	18.0	35.6	20.0	34.0
Business Activities	25	1	26	40.0	100.0	45.6	68.0	100.0	71.0
Community & Social Services	17	5	22	5.9	60.0	19.2	29.4	60.0	36.9
Hotel and Restaurants	15	5	20	40.0	40.0	40.0	33.3	0.0	26.1

1/ The diffusion index is weighted based on the distribution of the 2002 Top 5000 Corporations: (a) across the twelve economic sectors grouped as follows: Industry-manufacturing, electricity, gas and water, agriculture, fishery and forestry, and mining and quarrying; Construction, Wholesale and Retail Trade and Services Sector - finance, real estate, transport, storage & communication, hotels & restaurant, renting & business activities and community, social & personal services; and (b) beginning 4th Quarter 2003, between those firms based in the National Capital Region (NCR) and those based outside NCR, particularly Regions I, VII and XI.

**Table 2. SELECTED INDICATORS OF BUSINESS EXPECTATIONS**  
 First and Second Quarters 2004

INDICATORS	First Quarter 2004			Second Quarter 2004		
	NCR	Outside NCR	Total	NCR	Outside NCR	Total
Business Outlook Index						
Current Quarter	15.1	50.5	26.0	15.7	29.5	19.9
Next Quarter	15.7	46.6	25.2	32.8	31.6	32.4
Volume of Business Activity Index						
Previous Quarter	17.8	33.8	22.7	13.1	19.2	15.0
Current Quarter	2.3	16.0	6.5	23.1	30.5	25.4
Next Quarter	26.4	39.9	30.6	36.4	36.5	36.4
Volume of Total Order Book Index						
Previous Quarter	12.7	31.6	18.5	12.4	15.6	13.4
Current Quarter	0.0	12.1	3.8	18.6	16.8	18.0
Credit Access Index						
Current Quarter	-8.7	-24.0	-13.4	-11.1	-22.4	-14.6
Financial Conditions Index						
Current Quarter	-29.2	-40.9	-32.8	-29.6	-35.5	-31.4
Ave. Capacity Utilization (Industry Sector)						
Current Quarter	73.0	83.2	76.2	74.2	82.4	76.7
Employment Outlook Index						
Next Quarter	-7.2	7.0	-2.8	3.3	8.3	4.9

**Table 3. DISTRIBUTION OF COMPANIES WITH AND WITHOUT EXPANSION PLANS  
FOR THE INDUSTRY SECTOR**  
Second Quarter 2004

Industry Group	Number of Respondents			Percent Share								
				With Expansion Plans			No Expansion Plans			No Answer		
	NCR	Outside NCR	Total	NCR	Outside NCR	Total	NCR	Outside NCR	Total	NCR	Outside NCR	Total
<b>Industry Sector</b>	111	26	137	18.3	12.4	15.6	66.1	48.2	57.8	15.6	39.4	26.6
Mining & Quarrying	2	1	3	50.0	0.0	39.1	50.0	100.0	60.9	0.0	0.0	0.0
Manufacturing	99	23	122	17.2	13.0	15.2	69.7	47.8	59.4	13.1	39.1	25.3
Electricity, Gas & Water	4	0	4	0.0	0.0	0.0	0.0	0.0	0.0	100.0	0.0	100.0
Agriculture, Fishery & Forestry	6	2	8	50.0	0.0	25.0	50.0	50.0	50.0	0.0	50.0	25.0



**Table 4. CONFIDENCE INDICATORS AND DIFFUSION INDICES**

Second Quarter 2004

In percent

SECTORS	Confidence Indicator <sup>1/</sup>			Diffusion Index		
	NCR	Outside NCR	Total	NCR	Outside NCR	Total
1. Industry	15.6	18.2	16.8			
Volume of Total Order Book ( Current Quarter)				27.1	15.4	21.6
Volume of Stocks of Finished Goods (Current Quarter)				11.8	6.6	9.4
Volume of Production (Next Quarter)				31.5	45.8	38.1
2. Construction	19.2	0.0	14.5			
Volume of Total Order Book ( Current Quarter)				0.0	0.0	0.0
Number of People Employed (Next Quarter)				38.5	0.0	29.0
3. Wholesale and Retail Trade	2.9	-8.0	0.1			
Volume of Stocks of Finished Goods (Current Quarter)				23.7	16.0	21.7
Business Conditions (Current Quarter)				1.1	-8.0	-1.2
Business Conditions (Next Quarter)				31.2	0.0	23.2
4. Services	17.9	15.5	17.7			
Business Conditions (Current Quarter)				13.1	14.4	13.2
Business Conditions (Next Quarter)				36.8	26.9	35.9
Number of People Employed (Next Quarter)				3.9	5.3	4.1

<sup>1/</sup> The confidence indicators were computed as the averages of the diffusion indices of the variables in each sector. However, volume of stocks of finished goods were inverted (subtracted) rather than added. Discrepancies between diffusion index and confidence indicator figures are due to rounding-off.

**Table 5. FACTORS LIMITING PRODUCTION/BUSINESS ACTIVITY BY SECTOR**  
Second Quarter 2004

Sectors	No. of Respondents	Percent Share										
		High Interest Rate	Unclear Economic Laws	Lack of Equipment	Insufficient Demand	Access to Credit	Financial Problems	Competition	Labor Problems	Lack of Materials	Others <sup>1/</sup>	None
<b>All Sectors</b>	<b>429</b>	<b>33.1</b>	<b>35.2</b>	<b>21.5</b>	<b>57.2</b>	<b>25.4</b>	<b>31.1</b>	<b>66.8</b>	<b>20.8</b>	<b>24.2</b>	<b>19.0</b>	<b>6.2</b>
<b>NCR</b>	354	32.7	34.4	17.0	56.3	26.3	31.1	67.2	15.5	15.2	20.0	6.6
Industry	111	32.5	36.9	23.5	57.0	29.3	28.1	63.5	25.7	28.8	24.5	10.9
Of which:												
Manufacturing	99	33.3	34.3	21.2	56.6	27.3	27.3	68.7	24.2	30.3	24.2	8.1
Construction	13	38.5	15.4	0.0	61.5	15.4	15.4	61.5	7.7	0.0	30.8	0.0
Wholesale and Retail Trade	93	34.4	34.4	12.9	64.5	29.0	35.5	73.1	18.3	17.2	3.2	6.5
Services	137	30.6	34.5	16.8	47.8	22.5	30.0	66.1	4.9	3.1	29.4	3.8
Of which:												
Financial Intermediation	45	24.4	42.2	6.7	53.3	20.0	26.7	60.0	6.7	6.7	100.0	6.7
Business Activity	25	36.0	48.0	28.0	52.0	28.0	40.0	68.0	1.2	1.4	1.1	1.7
Community & Social Services	17	23.5	5.9	5.9	29.4	11.8	29.4	64.7	11.8	0.0	0.0	0.0
Hotel and Restaurants	15	26.7	46.7	20.0	46.7	20.0	53.3	80.0	13.3	6.7	0.0	13.3
<b>Outside NCR</b>	75	34.0	36.8	31.6	59.3	23.3	31.1	65.6	32.6	44.4	17.0	5.3
Industry	26	22.8	39.4	35.2	62.2	18.7	25.4	60.1	33.2	49.8	17.2	8.9
Of which:												
Manufacturing	23	21.7	39.1	34.8	60.9	17.4	26.1	60.9	30.4	47.8	13.0	4.3
Construction	2	50.0	0.0	50.0	50.0	50.0	50.0	100.0	0.0	50.0	0.0	0.0
Wholesale and Retail Trade	25	60.0	44.0	28.0	56.0	36.0	44.0	84.0	28.0	40.0	12.0	0.0
Services	22	35.0	21.9	18.5	54.5	16.5	29.8	51.7	44.4	28.1	27.6	0.0
Of which:												
Financial Intermediation	5	20.0	20.0	0.0	20.0	20.0	0.0	40.0	0.0	0.0	100.0	0.0
Business Activity	1	0.0	0.0	0.0	0.0	0.0	0.0	100.0	0.0	0.0	0.0	0.0
Community & Social Services	5	0.0	0.0	0.0	20.0	0.0	20.0	80.0	40.0	40.0	0.0	0.0
Hotel and Restaurants	5	40.0	40.0	40.0	60.0	40.0	40.0	80.0	40.0	40.0	20.0	0.0

<sup>1/</sup> Other factors that limit production or business activities are political and economic climate, lack of investors' confidence and government regulations.

**Table 6. INDICES OF EXPECTATIONS ON SELECTED ECONOMIC INDICATORS BY SECTOR**  
 Second and Third Quarters of 2004  
 In Index Points

Sectors	Current Quarter (April - June)			Next Quarter (July - September)		
	Average Peso Borrowing Rate	Average Inflation Rate	Average Peso/US \$ Rate	Average Peso Borrowing Rate	Average Inflation Rate	Average Peso/US \$ Rate
<b>Total</b>	<b>38.7</b>	<b>52.0</b>	<b>-1.5</b>	<b>31.8</b>	<b>42.2</b>	<b>0.2</b>
NCR	37.6	48.7	-4.1	34.4	39.9	-4.2
Industry	41.2	45.3	-7.9	28.6	35.5	-7.7
Construction	23.1	53.8	15.4	23.1	53.8	38.5
Wholesale & Retail Trade	29.0	40.9	-3.2	35.5	41.9	1.1
Services	43.4	58.3	-3.6	40.7	40.7	-10.7
Outside NCR	41.2	59.4	4.5	25.9	47.4	10.0
Industry	43.4	68.3	12.3	22.7	53.8	8.2
Construction	50.0	50.0	0.0	-50.0	0.0	50.0
Wholesale & Retail Trade	36.0	44.0	-8.0	40.0	40.0	12.0
Services	35.4	32.2	-34.2	35.4	32.8	-15.0

**Table 7. AVERAGE NUMBER OF EMPLOYEES**  
Second Quarter 2004

Sectors	No. of Respondents	Current Number of Employee (in percent)					No Response
		Small <100	Medium		Large >500		
			101-300	301-500			
<b>Total</b>	<b>429</b>	<b>31.8</b>	<b>24.6</b>	<b>11.5</b>	<b>15.6</b>	<b>16.5</b>	
NCR	354	34.7	24.7	7.0	14.4	19.1	
Industry	111	29.7	26.9	11.0	16.2	16.2	
Construction	13	46.2	30.8	0.0	0.0	23.1	
Wholesale and Retail Trade	93	41.9	24.7	4.3	6.5	22.6	
Services	137	31.6	22.1	6.6	21.4	18.2	
Outside NCR	75	25.4	24.2	21.6	18.3	10.5	
Industry	26	18.7	21.3	24.8	24.8	10.4	
Construction	2	0.0	0.0	50.0	0.0	50.0	
Wholesale and Retail Trade	25	36.0	32.0	12.0	12.0	8.0	
Services	22	41.3	28.6	17.8	5.5	6.9	