BALANCE OF PAYMENTS DEVELOPMENTS
SECOND QUARTER 2006

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➢ Overall Position

BOP position in the second quarter of 2006 reverses to a deficit due to the net outflow in the capital and financial account, even while current account remains in surplus.

The balance of payments (BOP) posted a deficit of US$81 million in the second quarter of 2006 as the capital and financial account reversed to a net outflow in light of the country's net repayment of external obligations, including prepayment of some Brady bonds and the BSP's term loan facility ahead of their maturities. The settlement occurred against the backdrop of gains in the current account following the strong inflows from remittances of overseas Filipino workers (OFWs), goods and services exports, and income receipts. Given the solid BOP surplus achieved during the first quarter of 2006, the overall BOP surplus for the first half of 2006 still came out strong at US$2.040 billion (Table 1).

Balance of Payments (US$ m)

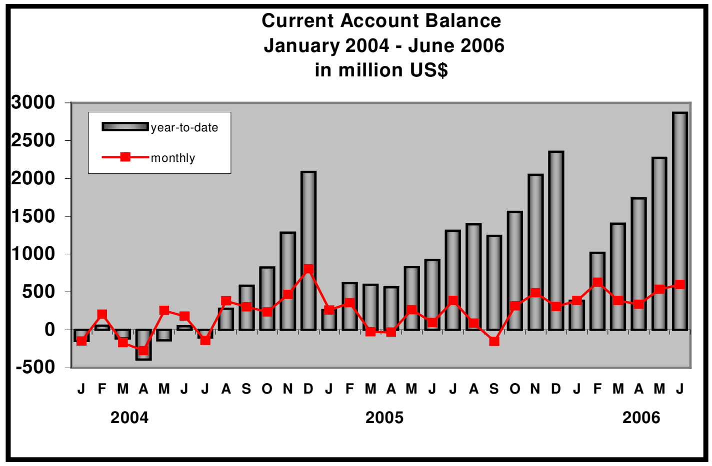
	Q2 2006	Q2 2005	Growth Rate (%)	Q1-Q2 2006	Q1-Q2 2005	Growth Rate (%)
I. Current Account	1469	-44	3438.6	2869	621	362.0
II. Capital & Fin'l Account	-1735	2247	-177.2	-1139	3906	-129.2
III. Net Unclassified Items	185	-1006	118.4	310	-2548	112.2
IV. Overall BOP	**-81**	**1197**	**-106.8**	**2040**	**1979**	**3.1**

*Details may not add up to totals due to rounding off.

➢ Current Account

The current account gains strength in the second quarter boosted by higher remittances from OFWs, stronger goods and services exports and higher net income receipts.

The current account (CA) surplus in the second quarter of 2006 surged to US$1.469 billion (5.3 percent of GDP), a reversal from the US$44 million deficit a year ago. The significant improvement was traced to higher inflows in current transfers from OFW remittances, higher net income receipts, and lower deficit in the trade-in-goods and services accounts. This favorable outturn led the cumulative six-month current account surplus to rise to US$2.869 billion (5.3 percent of GDP) compared to the US$621 million (1.3 percent of GDP) posted in the comparable period in 2005.

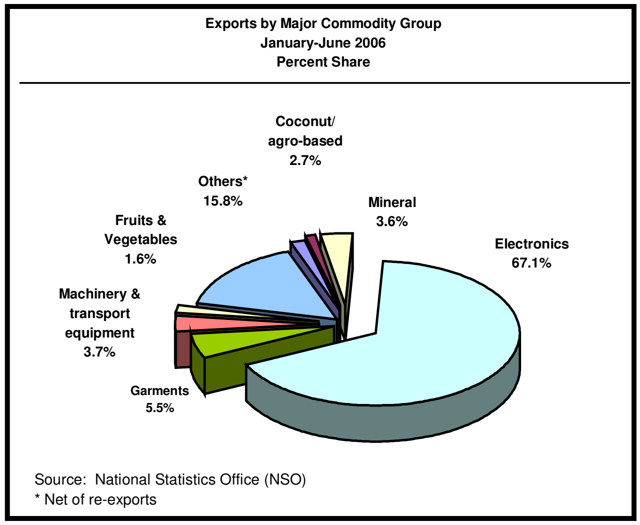


▪ Trade-in-Goods

The trade-in-goods account improves in the second quarter.

The trade-in-goods account registered a lower deficit of US$1.953 billion in the second quarter of 2006 compared to the US$2.541 billion deficit posted a year ago as the expansion in exports at 19.8 percent exceeded the growth in imports at 10.9 percent. Total export revenues during the quarter in review reached US$11.608 billion, driven mainly by higher shipments in manufactured goods specifically electronics and garments. The other commodities which also contributed to the double-digit export growth were minerals, petroleum, chemicals, wood manufactures, iron and steel, and fruits and vegetables. Meanwhile, purchases of foreign goods amounted to US$13.561 billion, traced primarily to increased procurement in mineral fuels and lubricant and raw materials and intermediate goods, notably imports of materials/accessories for the manufacture of electronics exports. These developments resulted in the 11.1 percent narrowing of the trade-in-goods deficit to US$3.471 billion in the first half of the year, as the export growth of 17.1 percent edged over the rise in imports at 12.3 percent (Table 2.2).[1]

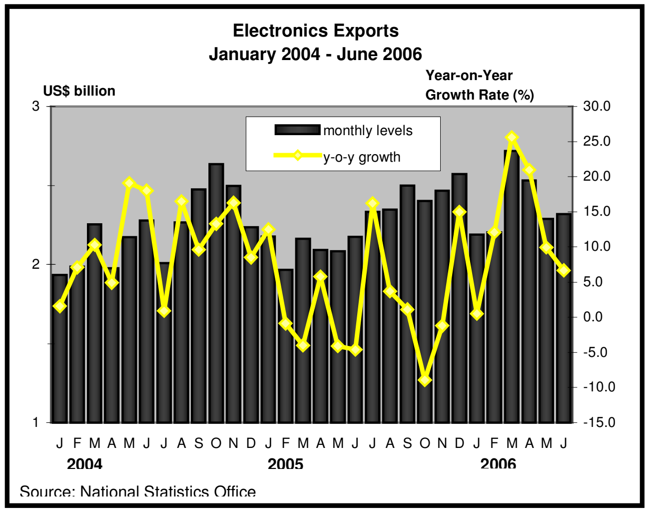
[1] Based on BPM5 concept (i.e., excluding from the National Statistics Office (NSO) foreign trade figures, those goods that did not involve change in ownership).



Growth in electronics exports posts double-digit growth in the second quarter.

a) *Electronics*. Exports of electronics (comprising electronic products, equipment and parts) in the second quarter of the year reached US$7.787 billion, up by 16.8 percent from the year-ago level of US$6.665 billion. Demand in the global IT market remained at a steady pace despite the current geopolitical issues in the Middle East and continuing rise in the world oil price. This strong second quarter export performance led to the acceleration of electronics shipments in the first six months of 2006 to US$15.248 billion. The 14.8 percent year-on-year growth for the period January-June 2006 was spurred primarily by higher shipments of semiconductor components/devices, automotive electronics, office equipment, and telecommunication. Exports of semiconductors garnered about 71.8 percent of total electronics (including electronic equipment and parts) with aggregate export earnings reaching US$10.955 billion during the six-month period. Demand was enhanced by increasing semiconductor content for a broad range of consumer electronics products and communications applications (e.g., third-generation (3G) phones, personal computers, digital cameras and televisions, and MP3 players). This strong performance, in turn, reflected the sustained global demand for electronics with the monthly book-to-bill ratios exceeding the unity mark since February 2006 at 1.01 and further to

1.14 in June.[2] The healthy industry outlook is expected to drive electronics firms to continuously upgrade production capabilities and move up the production ladder in the coming years.



Exports of garments continue to expand.

b) *Garments*. Garments exports in the second quarter of 2006 expanded by 22.6 percent to reach US$624 million from the year-ago level of US$509 million. This was in contrast with the 1.4 percent contraction in the same period last year. This positive outcome translated in the two-digit growth (18.6 percent) in garments exports in the first six months of 2006 to US$1.246 billion. The garments industry seemed to have benefited from its strategy of shifting to the production of higher-end garments integrating professional design expertise that catered to the clothing product lines of international brands such as JC Penney, GAP, Old Navy, Ann Taylor, among others. In particular, exports of garments such as knitted/crocheted shirts/shirt-blouses of synthetic fibers; brassieres; women's/girls' trousers, bibs & brace overalls, breeches & shorts of synthetic fibers recorded high growth rates during the six-month period.

With the lifting of the quota, garments exports have been continuously struggling to face up with fierce competition from other supplier countries, particularly China. However, the Garments Industry Transformation Plan

[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.

which was launched prior to the removal of the quota access, provided industry players with support programs to enhance productivity and technology skills; granted access to financing; and helped develop and promote diversified markets and products. Moreover, the industry has also taken advantage of the safeguard mechanism under the World Trade Organization that allowed importing countries such as the U.S. and the European Union to impose restraints/limits on China's textile and clothing exports to prevent domination of cheap Chinese produce in the world market. In particular, restrictions were imposed by the U.S. and the E.U. to China's exports of seven garments categories (e.g., cotton knit shirts and blouses, cotton trousers, slacks and shorts, among others), which partly contributed to the increase in Philippine exports of these wearing apparels.

Exports of machinery and transport equipment contract in the second quarter of the year.

c) *Machinery and Transport Equipment.* Exports of machinery and transport equipment declined by 15.4 percent in the second quarter of the year to US$412 million, in contrast to the 25.3 percent growth achieved in the same period last year. This led to the 8.9 percent contraction in shipments of this commodity group during the first half of 2006. The decline can be traced to the lower demand for products such as other gear boxes for motor vehicles and non-photosensitive diodes which more than offset the increase in other parts/accessories of motor vehicles (21.5 percent) and ceramic dielectric and multilayer paper or plastic fixed capacitors (148.3 percent). Despite the slack during the first six months of the year, the government remains optimistic that the industry will recover as initiatives to enhance the industry's competitiveness and harness its potentials have been continuously undertaken with the view to acquire a bigger market share in Japan, U.S., the ASEAN and Europe. The strategy focuses on: i) product and market development; ii) price competitiveness; and iii) improvement of management systems, use of new technologies, development of strategic marketing approaches and heightening of productivity levels.

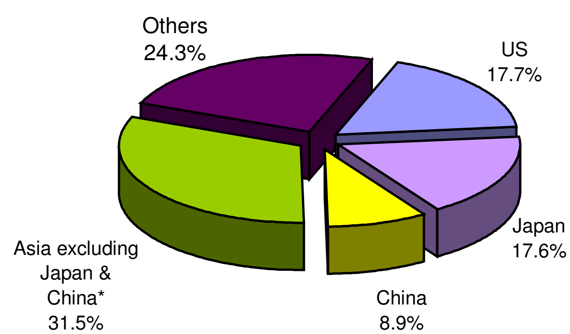
Intra-Asian trade remains healthy.

The country's intra-regional trade sustained its rise with non-Japan/China Asian economies[3] garnering a combined market share of 31.5 percent in the first six months of 2006, almost approximating the 32.7 percent

[3] Countries include Singapore, Hong Kong, Malaysia, South Korea, Thailand, Taiwan and Indonesia.

share in the same period in 2005. China continued to be the most dynamic export market as export shipments expanded at an annual average of about 45 percent for the last five years, with the highest growth recorded at 71.0 percent in 2002. In the first six months of 2006, exports to China rose by 10.8 percent to US$2.019 billion, representing 8.9 percent of total exports. China ranked fourth as the country's biggest export market next to the U.S., Japan and Netherlands. With the anticipated growth of China's production activities, the growth in the country's export shipments is expected to continue.

Major Export Destinations
January-June 2006
(Percent Share)



* Comprised of Hong Kong, South Korea, Singapore, Taiwan, Malaysia, Indonesia and Thailand
Source: NSO

Total imports post hefty growth in the second quarter due to higher procurement of raw materials and mineral fuel and lubricants.

Imports of goods in the second quarter of 2006 grew by 10.9 percent to US$13.561 billion as purchases of imported raw materials and mineral fuels and lubricant posted higher levels compared to the same quarter last year. This brought the first semester's total imports to US$25.772 billion, or an expansion of 12.3 percent, comparing favorably with the 4.0 percent growth in same period last year. Imports of all commodity groups grew during the semester, with purchases of mineral fuel and lubricants recording the highest rate of increase at 34.4 percent (Table 2.2).[4]

[4] Based on BPM5 concept (i.e., excluding from the National Statistics Office (NSO) foreign trade figures, those goods that did not involve change in ownership). Imports per BOP also reflect: a) upward adjustments on the valuation of consigned raw materials for electronics and garments exports; b) OFW remittances in kind; and c) military imports, etc.

Capital goods imports decline in the second quarter of the year.

Imports of capital goods declined marginally by 1.2 percent to US$2.168 billion in the second quarter of 2006 due to the lower procurement of office and EDP machines, land transport equipment excluding passenger cars and motorized cycle, and aircraft, ships and boats. Total imports of capital goods in the first half of 2006, however, still managed to expand by 1.5 percent, a turnaround from the 6.7 percent decline in the same period a year ago. Expansion was traced largely to higher purchases of power generating and specialized machines, telecommunication equipment and electrical machines, and aircraft, ships & boats.

Imports of raw materials and intermediate goods also increase.

Imports of raw materials and intermediate goods grew by 11.1 percent in the second quarter of 2006 to reach US$8.070 billion. The expansion was due mainly to higher procurement of semi-processed raw materials, primarily raw material inputs for the manufacture of electronics products. This led to the 11.9 percent growth in the first half of the year as total raw materials procured stood at US$15.484 billion compared to US$13.836 billion a year ago. Among the commodities which contributed to the strong growth in this commodity group were raw material inputs for electronics production; artificial resins; textile yarn and fabrics; chemical compounds and non-ferrous metals.

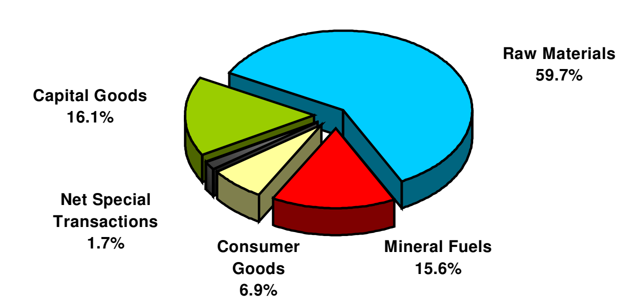
Imports of mineral fuels and lubricants rise due to continuing increase in the world market price of oil.

Imports of mineral fuels and lubricants in the second quarter of 2006 grew by 30.7 percent to US$2.235 billion, posting the highest growth among all major commodity groups. This was on account of the higher import bill on petroleum crude and other petroleum products owing to the continually rising international oil prices. In particular, imports of petroleum crude rose by 42.1 percent to US$1.462 billion as the average crude oil price increased to US$64.72 per barrel during the second quarter from US$48.58 per barrel during the second quarter last year, while volume rose to 22.59 million barrels from 21.18 million barrels during the quarter in review. Other petroleum products, on the other hand, reached US$704 million, up by 10.9 percent from last year's level. Consequently, this brought the import bill for this commodity group in the first six months of the year to climb by 34.4 percent from the year-ago level.

Lower purchases of non-durable goods drag down consumer goods imports in the second quarter.

Imports of consumer goods declined by 3.6 percent to US$930 million in the second quarter of the year caused mainly by the contraction in purchases of non-durable goods, notably rice (which benefited from good domestic production/harvest), fish and fish preparation, and dairy products. Non-durable goods contracted by 11.3 percent to US$540 million during the quarter in review which offset the 9.6 percent improvement in durable goods. This notwithstanding, imports of consumer goods in the first half of 2006 managed to post a growth of 2.1 percent as imports of durable goods increased by 9.1 percent with higher purchases of passenger cars and motorized cycle (14.3 percent) and miscellaneous manufactures (10.2 percent).

Imports by Major Commodity Group
January-June 2006
(Percent Share)



Source: National Statistics Office (NSO)

▪ Trade-in-Services

The trade-in-services account in the second quarter of 2006 ends with a lower deficit.

The deficit in trade-in-services account during the second quarter of 2006 narrowed significantly to US$3 million from US$418 million a year ago. The 99.3 percent improvement compared favorably with the 5.0 percent growth a year ago. During the quarter in review, transactions in travel, communication, financial and other business services resulted in higher net inflows while transportation and insurance services as well as royalties and fees posted lower net outflows. Combined with the surplus recorded in the first quarter of the year, the substantial narrowing of the deficit in the second quarter resulted in the reversal of the services account to a net inflow of US$149 million in the first half of 2006 from a net outflow of US$784 million in the same period last year. Net travel receipts grew by 52.0 percent to reach US$631 million during the six-month period. The Department of Tourism (DOT) continued to promote inbound travel to the country with intensified marketing campaigns including participation in international consumer events. In gearing up the country for the expected surge of foreign tourists, the DOT has set a training program to upgrade the country's frontline services to achieve a high level of professionalism and quality in the provision of tourism services. For the first six months of the year, tourist arrivals registered a 10.4 percent increment to reach 1.42 million. Meanwhile, the gains in communication and other business services, specifically miscellaneous business, professional and technical services reflected increasing revenues from business process outsourcing (BPO) activities notably contact centers, medical transcription, software development, animation and backroom operations, among others. These positive developments were complemented by the lower net outflows for transportation services particularly freight, royalties and fees, financial and insurance services.

- **Income**

The income account registers a higher surplus.

The income account in the second quarter of 2006 posted a higher surplus of US$117 million compared to year-ago level of US$31 million. This was attributed mainly to the lower deficit in investment income due, in turn, to increased reinvested earnings from direct investments coupled with decreased net outlays for dividends and profits. Meanwhile, remittances from resident OFWs during the quarter in review contracted by 9.1 percent to US$681 million from the year-ago level of US$749 million as the implementation of Japan's new immigration rules continued to take its toll on the number of deployed resident OFWs, specifically overseas performing artists.[5] The effect was, however, moderated by the 16.9 percent increase in the deployment of sea-based OFWs in the second quarter of the year. As a result of the higher surplus in the second quarter, the income account for the first semester posted a lower net outflow of US$78 million compared to US$113 million a year ago. The improvement was traced primarily to the 14.0 percent narrowing of the deficit in investment income to US$1.395 billion which negated the 12.8 percent decline in remittances from resident OFWs to US$1.317 billion during the review period. The

[5] Under the BPM5, the residency of seasonal workers such as OFWs is classified according to the length of their stay in the host economy. OFWs who are working for less than one year are classified as resident OFWs and their gross earnings are reflected under the Income account. Meanwhile, OFWs who are working for one year or more in the host economy are classified as non-resident OFWs and their remittances are reflected under the Current Transfers account. Gross earnings of performing artists and sea-based workers, who generally enter into contracts of less than one year are reflected under the Income account. Meanwhile, remittances of all land-based workers, except performing artists, are included under the Current Transfers account.

lower deficit in investment income was due, in turn, to higher reinvested earnings as well as increased net investment income on bonds and notes held by the monetary authority which rose by 133.6 percent to reach US$292 million during the first half of the year (Table 4).

▪ Current Transfers

Strong OFW remittances steer the current transfers account.

Net current transfers in the second quarter of 2006 expanded to US$3.308 billion from the year-ago level of US$2.884 billion. This developed on account of the strong remittances from non-resident OFWs which reached US$3.074 billion during the quarter in review. The 13.7 percent rise was due mainly to the combined impact of rising demand for highly skilled and higher-paid Filipino workers and increased access of a greater number of overseas Filipinos to commercial banks and private remittance agents. A large part of remittances was coursed through commercial banks because of a) better-offered rates to clients; b) intensified bank product endorsements; c) strengthened tie-ups with foreign money transfer agents and non-bank channels; and d) enhanced electronic banking.[6] Moreover, the government and private sector initiatives to enhance workers' competence through skills upgrading, technical training and better education have contributed largely to the increasing preference for the Philippines as a source of skilled labor. Meanwhile, net current transfers from foreign government institutions as well as gifts and donations from migrants also contributed to the 14.7 percent improvement of the current transfers account during the quarter in review. These positive developments drove the current transfers in the first six months of the year to grow by 15.6 percent to reach US$6.269 billion with expansion traced mainly to higher net receipts from: a) non-resident OFWs (13.9 percent); b) foreign government (21.5 percent); and c) other transfers (79.8 percent) (Table 5).

➢ Capital and Financial Account

The capital and financial account reverses to a deficit in the second quarter.

The capital and financial account yielded a deficit of US$1.735 billion in the second quarter of 2006, a reversal from the US$2.247 billion surplus in the same quarter last year. This developed on account of the net outflows registered in both portfolio and other investments, mostly repayment of loans and

[6] Based on the National Statistics Office's Survey on Overseas Filipinos (NSO-SOF) in 2004, 81 percent of the total inflows of OFW remittances passed through the banking system, which was higher compared to 73 percent in 2003. The NSO-SOF is a nationwide survey that gathers information on overseas workers who left abroad during the last five years using the past six months reference period. The SOF is a rider survey to the October round of Labor Force Survey every year.

bonds, which negated the effect of higher net inflows posted by both direct and financial derivatives. As a result, the capital and financial account balance from January to June 2006 likewise reverted to a net outflow of US$1.139 billion from a net inflow of US$3.906 billion.

▪ Capital Account

The capital account surplus improves.

The capital account surplus rose to US$9 million during the second quarter of 2006 from US$4 million in the same quarter last year. This developed as net capital transfers from general government increased to US$12 million. This brought the January-June 2006 capital account to a surplus of US$18 million, matching the level a year ago. Net capital transfers from the general government grew by 33.3 percent to US$24 million which more than compensated for the net outward transfers by migrants and other sectors (Table 6).[7]

▪ Direct Investment

Direct investment flows higher with increased non-residents' investments.

The direct investment account surplus widened to US$636 million in the second quarter of 2006, more than five times the year-ago level of US$117 million. Non-residents' investments surged to US$633 million compared to US$136 million in the same quarter in 2005 as the other capital account— representing primarily inter-company accounts between investee companies and their corresponding foreign direct investors— reversed to a net inflow of US$433 million. This more than offset the net outflow of US$42 million in the reinvested earnings account. Net equity capital placements also improved by 19.2 percent to US$242 million during the quarter in review.

These favorable developments brought the net inflows in direct investments to US$967 million in the first half of 2006, 53.5 percent increase from the year-ago net inflow of US$630 million. Foreign direct investments in the Philippines rose to US$996 million, up by 47.6 percent from last year's level. The rising net FDI flows mirrored the positive sentiment of investors on the country's economic climate following the news on sustained GDP growth, increasing GIR, surplus fiscal position from April-June and easing inflation rate.

[7] The capital account consists largely of capital transfers. Capital transfers are transactions that involve the change in the stocks of assets of one or both counter parties and are linked to the acquisition and disposal of fixed assets. By contrast, current transfers involve transactions that affect the level of disposable income and influence consumption of goods and services.

During the first six months of the year, the "other capital" account reversed to a surplus of US$656 million from a net outflow of US$106 million in the same period in 2005. These intercompany account transactions largely involved automotive and electronic firms. The improvement in the "other capital" account more than offset the net outflow of US$25 million in reinvested earnings in the first six months of the year. Meanwhile, net equity capital remained in surplus at US$365 million from January to June 2006, albeit lower than the year-ago level. Major investors during the six-month period were U.S., Japan, United Kingdom, Federal Republic of Germany, Switzerland and Taiwan. Bulk of the capital placements were infused to the manufacturing (chemicals, health-care, electronics, airconditioning system and steel products); services (medical research, resort facilities, information/technology, engineering, construction and facilities management); financial intermediation and real estate sectors.

- **Portfolio Investments**

Second quarter portfolio investments reverse to a net outflow.

The portfolio investment account reversed to a net outflow of US$1.104 billion in the second quarter of 2006 from a net inflow of US$2.056 billion a year ago. The deterioration was due to the combined effects of increased residents' investments abroad both in equity and debt securities and the net repayments of maturing bonds and notes as well as the prepayment by NG of Brady bonds originally maturing in 2017. The decline in the second quarter resulted in the contraction of the net portfolio investment inflows in the first half of the year to US$460 million, lower by 85.8 percent compared to the US$3.245 billion net inflow a year ago. The major contributory factors were: a) lower net investments in equity securities by non-resident private corporations due, in turn, to lower amount of initial public offerings (IPOs) issued this year compared to last year, and the insufficient treasury instruments available for investments by non-residents; and b) lower net bond availments by the public sector (US$1.425 billion)[8] combined with the net bond repayments by the private sector (US$374 million); and c) net purchase by residents of the NG and monetary authority's foreign currency-denominated debt papers, previously issued to non-residents amounting to US$648 million and US$91 million, respectively.

[8] Includes US$411 million pretermination by NG of Brady bonds originally maturing in 2017.

▪ Financial Derivatives

Financial derivatives post higher surplus.

The trading of financial derivatives in the second quarter of 2006 yielded a net gain resulting in a surplus of US$37 million compared to last year's US$16 million. However, losses incurred in the trading of financial derivatives in the first quarter led to a higher deficit of US$35 million in the first six months of 2006 compared to US$26 million in the same period a year ago.

▪ Other Investments

The other investment account reverses to a deficit due mainly to higher loan repayments by local banks and private corporations.

The other investment account reversed to a deficit of US$1.313 billion in the second quarter of 2006 from a surplus of US$54 million a year ago. The turnaround was due mainly to lower loan borrowings, and higher net loan repayments of US$1.307 billion, arising largely from higher outlays by the domestic banks, private corporations, and the monetary authority. The BSP preterminated in April 2006 US$200 million worth of foreign loan, representing the offshore portion of the US$395.5 million term loan facility, originally maturing in October 2006.[9] This led the other investment account to revert to a net outflow of US$2.549 billion during the six-month period from a net inflow of US$39 million in 2005. The reversal was traced mainly to higher net loan repayments by local banks (US$1.212 billion), public and private corporations (US$495 million), the NG (US$327 million) and monetary authority (US$251 million).

➢ Reserve Assets

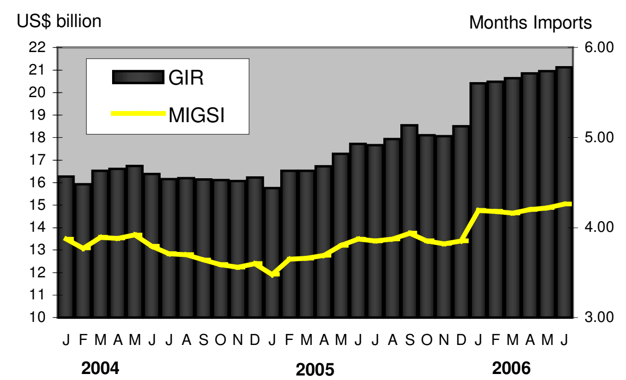
Gross international reserves remain at comfortable level.

The BSP's gross international reserves (GIR), including reserve position in the IMF, reached an all time high of US$21.123 billion as of end-June 2006 (Table 12). This was 14.2 percent higher compared to the end-December 2005 level of US$18.494 billion. At this level, GIR remained comfortable and was equivalent to 4.3 months' worth of imports of goods and payment of services and income (MIGSI). In terms of short-term debt coverage, the reserve level was 3.4 times the amount of the country's short-term external liabilities based on original maturity and 1.8 times based on residual maturity.[10]

[9] This pertains to the US$500 million term loan facility, of which US104.5 million were converted to Floating Rate Notes.
[10] Residual maturity refers to outstanding short-term debt based on original maturity plus principal payments on medium- and long-term loans of the public and private sectors falling due in the next 12 months.

A large part of reserves was in the form of foreign investments (83.6 percent), with the balance in gold (13.7 percent), foreign exchange (2.1 percent) and combined SDRs and reserve position in the Fund (0.6 percent). By currency composition, reserves (excluding gold) were in US dollars (87.0 percent), Euros (7.2 percent), Japanese yen (3.0 percent), pounds sterling (1.4 percent) and the balance (1.4 percent) in other foreign currencies.

Gross International Reserves
2004 - June 2006
As of end-periods indicated



MIGSI - Months of imports of goods and payment of services and income

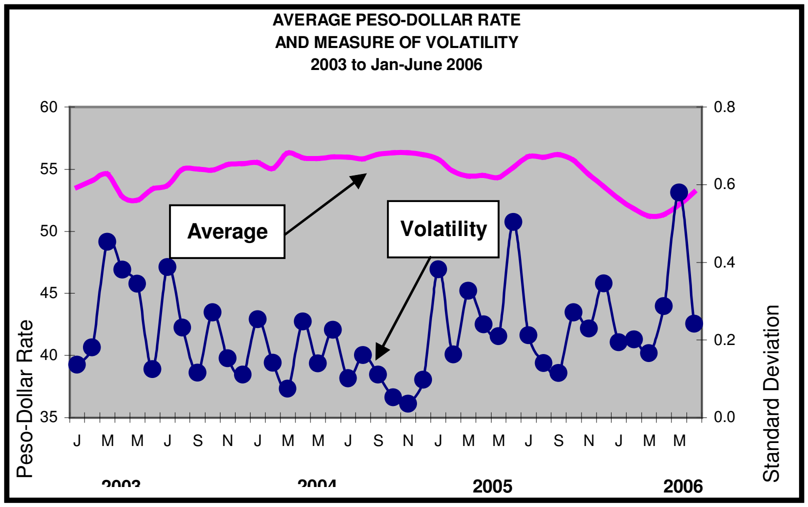
➢ Exchange Rate

Strong foreign exchange inflows boost the peso's strength.

The nominal peso-dollar exchange rate averaged ₱52.22/US$1 in the second quarter of 2006, appreciating by 4.7 percent from ₱54.67/US$1 level in the same quarter in 2005. The strength of the peso was boosted by sustained foreign exchange inflows from OFW remittances, foreign direct and portfolio investments, and higher earnings from exports of goods and services. Thus, in the first six months of 2006, the nominal peso-dollar exchange rate averaged ₱52.05/US$1, appreciating by 5.4 percent from ₱54.84/US$1 level in the comparable period in 2005.

Peso more volatile in the second quarter.

The peso's volatility in the second quarter of the year at a standard deviation of ₱0.83 was higher than the ₱0.50 in the same quarter last year. For the first half of the year, the peso likewise showed more volatility with a standard deviation of ₱0.75 compared to ₱0.60 in January-June 2005. It was noted, however, that in terms of the average of the monthly volatilities, the peso fluctuated less at ₱0.28 for the first half of 2006 compared to ₱0.30 in the same period a year ago.[11] The peso-dollar exchange rate ranged from ₱51.00/US$1 to ₱53.59/US$1 during the six-month period.



Peso external competitiveness weakens. Compared with the previous year's level, the peso's average nominal effective exchange rate (NEER) index in the second quarter of 2006 appreciated by 6.4 percent against the currency basket of the country's major trading partners.[12] Relative to currency baskets of the broad group of competitor countries, the peso's average NEER also appreciated by 1.0 percent but depreciated by 0.1 percent relative to the narrow group of competitor countries.[13] In terms of the real effective exchange rate (REER) index,[14] the peso's competitiveness weakened as the REER appreciated by 11.0 percent against the currency basket of the country's major trading partners, by 2.7 percent against the currencies in the broad basket, but depreciated by 3.2 percent against the currencies in the narrow basket. The peso's nominal appreciation combined with the widening inflation differentials between the Philippines and its major trading partners as well as its competitor countries in the broad basket resulted in the decline in the peso's external competitiveness. However, it should be noted that the REER for the second quarter did not vary much from the levels in 2000 when economic indicators such as GDP, exports and inflation showed improvement.

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[11] Similar trend was noted in the first quarter of 2006 at ₱0.19 compared to ₱0.29 in the first quarter of 2005.
[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 euro and the British pound. Major trading partners include the U.S., Japan, European Monetary Union and the U.K.
[13] The broad basket is composed of the currencies of Singapore, South Korea, Taiwan, Thailand, Indonesia and Hong Kong while 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.

EFFECTIVE EXCHANGE RATE INDICES OF THE PESO For periods indicated December 1980=100							
		NEER			REER		
			CC			CC	
		MIC 1/	Broad 2/	Narrow 3/	MIC 1/	Broad 2/	Narrow 3/
2004	Jan	11.32	27.68	52.85	53.71	96.99	137.80
	Feb	11.19	27.36	52.55	53.03	95.55	136.06
	Mar	11.30	27.46	52.94	53.38	96.28	137.86
	Qtr 1	**11.27**	**27.50**	**52.78**	**53.37**	**96.27**	**137.24**
	Apr	11.43	27.60	53.46	54.15	96.43	137.51
	May	11.55	28.26	55.18	54.83	99.66	144.86
	Jun	11.41	28.58	56.65	54.92	103.61	152.36
	Qtr 2	**11.47**	**28.15**	**55.10**	**54.63**	**99.90**	**144.91**
	Jul	11.38	28.26	55.39	55.52	104.18	150.85
	Aug	11.46	28.58	56.33	56.08	105.73	154.68
	Sep	11.38	28.26	55.77	55.96	103.67	152.20
	Qtr 3	**11.41**	**28.37**	**55.83**	**55.85**	**104.53**	**152.58**
	Oct	11.25	28.05	55.31	55.30	102.16	149.77
	Nov	11.02	27.61	54.82	54.66	102.56	148.72
	Dec	10.92	27.63	55.41	54.67	102.56	151.07
	Qtr 4	**11.06**	**27.76**	**55.18**	**54.88**	**102.43**	**149.85**
Ave	**Jan-Dec**	**11.30**	**27.94**	**54.72**	**54.68**	**100.78**	**146.14**
2005	Jan	11.05	27.74	55.76	55.79	102.97	150.32
	Feb	11.32	28.14	56.70	57.10	103.77	152.13
	Mar	11.34	28.36	57.61	57.01	104.60	153.95
	Qtr 1	**11.24**	**28.08**	**56.69**	**56.63**	**103.78**	**152.13**
	Apr	11.45	28.70	58.54	57.60	105.67	154.78
	May	11.53	28.64	58.41	58.27	106.43	157.94
	Jun	11.56	28.49	58.33	58.88	107.89	160.19
	Qtr 2	**11.52**	**28.61**	**58.43**	**58.25**	**106.66**	**157.64**
	Jul	11.51	28.47	58.35	59.00	108.89	160.70
	Aug	11.42	28.51	58.74	58.64	109.20	162.54
	Sep	11.39	28.83	58.58	58.37	109.00	163.02
	Qtr 3	**11.44**	**28.60**	**58.89**	**58.67**	**109.03**	**162.09**
	Oct	11.65	29.02	59.52	59.80	107.21	155.34
	Nov	12.06	29.56	60.54	62.78	111.43	158.03
	Dec	12.26	29.74	60.80	64.05	117.76	159.77
	Qtr 4	**11.99**	**29.44**	**60.29**	**62.21**	**110.13**	**157.71**
Ave	**Jan-Dec**	**11.55**	**28.68**	**58.57**	**58.94**	**107.40**	**157.39**
2006	Jan	12.33	29.50	60.20	64.76	110.75	156.47
	Feb	12.64	29.61	60.09	67.00	111.69	156.28
	Mar	12.75	29.80	60.13	67.42	112.66	156.51
	Qtr 1	**12.57**	**29.64**	**60.14**	**66.39**	**111.70**	**156.42**
	Apr	12.62	29.24	58.74	66.40	109.74	150.70
	May	12.14	28.69	57.89	63.88	108.41	151.61
	June	12.01	28.75	58.48	63.67	110.49	155.36
	Qtr 2	**12.26**	**28.89**	**58.37**	**64.65**	**109.55**	**152.56**

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.