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HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 21 MARCH 2019[1]

I. Monetary Policy Decision

The Monetary Board decided to:

a) maintain the overnight RRP (borrowing) rate at 4.75 percent; and

b) maintain the current overnight deposit and overnight lending rates at 4.25 percent and 5.25 percent, respectively.

II. Key Considerations in the Formulation of the Monetary Policy Stance

- The Monetary Board (MB) deemed the prevailing monetary policy settings to be appropriate, with latest baseline inflation forecasts settling within the target range of 3.0 percent ± 1.0 percentage point for both 2019 and 2020, and inflation expectations continuing to stabilize within the target band. Inflation pressures have eased further since the previous monetary policy meeting, reflecting mainly the decline in food prices amid improved supply conditions.

- The MB also noted that the risks to the inflation outlook remained broadly balanced for 2019, even as it observed that further risks could emerge from prolonged El Niño weather conditions and higher-than-expected increases in global oil and food prices. For 2020, the risks lean toward the downside as tighter global financial conditions and geopolitical risks could temper global economic activity and potential upward pressures on commodity prices.

- Meanwhile, the MB observed that overall prospects for domestic activity continued to be firm, supported by a projected recovery in household spending and the implementation of the government's infrastructure program. However, there are downside risks to economic growth in 2019 if the current budget impasse in Congress is not resolved soon.

- Given these considerations, the MB is of the view that the within-target inflation outlook and firm domestic growth support keeping monetary policy settings steady. The MB also emphasized that the BSP remains vigilant against developments that could affect the outlook for inflation and is prepared to take appropriate policy action as necessary to safeguard its price stability objective.

[1] The discussions herein reflect the assessment made by the Monetary Board based on a comprehensive set of economic information available at the time of the policy meeting. The highlights of the discussions during the 21 March 2019 monetary policy meeting were approved by the Monetary Board during its regular meeting held on 11 April 2019. The next meeting of the Monetary Board on the monetary policy stance is scheduled on 9 May 2019.

III. Recent Developments and Inflation Outlook

The MB considered the following developments in deciding on the monetary policy stance:

A. Domestic price conditions

- Inflation momentum eased further in February 2019, reflecting weaker supply-side pressures. Headline inflation decelerated for the fifth consecutive month in February to 3.8 percent (from 4.4 percent in January, 5.1 percent in December, 6.0 percent in November, and 6.7 percent both in October and September) as both food and non-food inflation registered lower outturns. Heavily-weighted food items posted slower inflation amid improved supply conditions. Meanwhile, month-on-month inflation for both non-seasonally-adjusted and seasonally-adjusted data were steady relative to the previous month's levels.

- Core inflation—which excludes selected volatile food and energy items to measure underlying price pressures—also decreased to 3.9 percent in February from 4.4 percent in the previous month. Likewise, all four alternative measures of core inflation computed by the BSP pointed to moderating inflation pressures in February.

- The diffusion index of price changes and the number of CPI items above threshold were also lower in February.

B. Inflation expectations

- Results of the BSP's March 2019 survey of private sector economists showed lower mean inflation forecasts for 2019 and 2020 at 3.3 percent (from 3.5 percent in the February 2019 survey round) and 3.4 percent (from 3.5 percent), respectively. Meanwhile, the mean inflation forecast for 2021 was unchanged from the previous month's reading at 3.4 percent.

C. Inflation outlook

- The latest baseline inflation forecasts showed that inflation will continue to ease, with average inflation for 2019 and 2020 projected to settle within the 3.0 percent ± 1.0 percentage point target range. The slightly lower forecast path for 2019 can be attributed largely to the lower-than-projected inflation outturn for February 2019. Meanwhile, the inflation forecast for 2020 remained broadly unchanged at 3.0 percent as the potential impact of higher crude oil prices was offset by the effect of the peso's appreciation and slower domestic liquidity growth.

Baseline Inflation Forecasts

	7 February 2019 MB Meeting	21 March 2019 MB Meeting
2019	3.1	3.0
2020	3.0	3.0

- The risks to future inflation were seen to remain evenly balanced for 2019 while downside risks to the outlook were projected to dominate in 2020. Petitions for electricity rates and transport fare adjustments, the proposed increase in the excise taxes of alcohol beverages, and the potential impact of a weak El Niño episode are the main upside risks to inflation. Meanwhile, slower global economic growth due to protectionist policies in advanced economies as well as geopolitical tensions and the potential renegotiation for lower tariff rates on meat products continue to be the main downside risks to inflation.

D. Demand conditions

- Domestic demand conditions continued to be firm in 2018 despite some moderation. Philippine GDP grew by 6.1 percent in Q4 2018, bringing annual GDP growth in 2018 to 6.2 percent. The pace of economic growth in 2018 is lower than the National Government (NG) target of 6.5-6.9 percent for 2018 as well as the 6.7-percent expansion recorded in 2017.

- Nonetheless, the Philippine economy is expected to remain resilient with the NG's target GDP growth at about 6.0-7.0 percent in 2019 and at 6.5-7.5 percent in 2020, supported by sustained private demand and the scaling up of public investment spending.

- Meanwhile, the preliminary composite purchasing managers' index (PMI) rose in February to 57.0 from 54.9 in January due to the faster expansion of the manufacturing and services sectors.

E. Supply-side indicators

Developments in Agriculture

- Domestic rice prices declined further in February due to the continued arrival of rice imports of both the government and the private sector.

- President Rodrigo R. Duterte's signing of Republic Act No. 11203, or the "Act Liberalizing the Importation, Exportation, and Trading of Rice, Lifting for the Purpose the Quantitative Import Restriction on Rice, and for Other Purposes" on 14 February 2019 is expected to further promote lower domestic rice prices. The Implementing Rules and Regulations (IRR) of the rice tariffication law is expected to be drafted and to have undergone public consultation within March 2019.

- The onset of the El Niño phenomenon presents a potential upside risk to food inflation in the near term. On 20 February 2019, the Philippine Atmospheric, Geophysical and Astronomical Services Administration (PAGASA) announced the presence of weak El Niño condition in the country which could lead to droughts in the first semester of 2019 and subsequently affect domestic production of rice and other agricultural commodities.

Oil Price Developments

- Global crude oil price rose above US$65.00 per barrel in mid-March 2019 due to a confluence of factors limiting crude oil supply in the international market, namely, the ongoing production cuts of the Organization of the Petroleum Exporting Countries (OPEC) member countries and allies; Saudi Arabia's pronouncement that it would reduce production by more than the pledged cut; US imposition of sanctions against Venezuela state-owned oil company Petroleos de Venezuela; government-mandated production cuts in Canada; and production disruptions in Libya. Nevertheless, international crude oil prices are expected to remain backwardation due to excess global supply and muted demand.

Developments in the Utilities Sector

- The overall electricity rate increased in February 2019 due mainly to higher generation charges contracted by parties under the Power Supply Agreements (PSAs) and those registered in the Wholesale Electricity Spot Market (WESM). Following the reduction in PSA charges in January due to the early completion of annual capacity fee payments for the previous year, capacity fees this month increased to levels prescribed in the PSAs approved by the Energy Regulatory Commission. At the same time, charges from the WESM went up due to tighter supply conditions in Luzon as several large power plants went on scheduled maintenance outage.

F. Financial market developments

- The peso appreciated against the US dollar in the first half of March 2019 amid lower-than-expected inflation outturn in February, dovish monetary stance of the US Federal Reserve (US Fed) for 2019, and market optimism over trade negotiations between the US and China. Likewise, the Philippine stock market index rose amid investor optimism over reports of positive corporate earnings results of several domestic firms in 2018 and better-than-expected US retail earnings in January 2019.

G. Domestic liquidity and credit conditions

- Domestic liquidity growth eased in January 2019 due to the slower expansion in domestic credit. In January, domestic liquidity growth decelerated to 7.6 percent (from 9.2 percent in December) while bank lending expanded at a slower rate of 15.3 percent (from 15.7 percent). Meanwhile, TDF rates as well as other market interest rates (deposit and lending rates) increased following the cumulative 175-bps hike in the BSP’s key policy rate in 2018.

H. Fiscal developments

- Sustained fiscal spending is expected to support the country’s growth momentum in 2019, even as the re-enactment of the budget is anticipated to temporarily curtail government expenditures in early 2019. The NG recorded a ₱558.3-billion fiscal deficit for 2018 equivalent to 3.2 percent of GDP, slightly exceeding the 3-percent target.

I. External developments

- Global economic activity expanded at a slightly faster pace in February 2019 owing to stronger growth in the service sector. During the month, economic activity expanded faster in the US, euro area, UK, India, and Russia, while growth remained modest in Japan and China. Nonetheless, downside risks to global growth remain due to tighter global financial conditions, policy uncertainty, and geopolitical risks.

- The US Fed’s decision to keep the Fed funds target rate unchanged during the Federal Open Market Committee (FOMC) meeting on 19-20 March 2019, along with the release of lower US GDP growth and inflation forecasts for 2019 and 2020, further reinforced market expectations that the US Fed would pause in raising interest rates 2019. Similarly, the European Central Bank (ECB) decided to keep interest rates unchanged during its 7 March 2019 Governing Council meeting amid a weaker euro area growth outlook over the near term. The ECB also announced that they would offer a third round of targeted longer-term refinancing operations (TLTRO-III) starting in September 2019.