HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 12 MAY 2021[1]

I. Monetary Policy Decision

The Monetary Board decided to:

a) Keep the the overnight RRP (borrowing) rate unchanged at 2.00 percent; anday

b) Maintain the accommodative levels of overnight deposit and overnight lending rates at 1.50 percent and 2.50 percent, respectively.

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

- The Monetary Board's decision was based on its assessment that the latest baseline inflation forecasts are within target for 2021 and 2022, but effective and timely supply-side interventions will be crucial in keeping inflation within target in 2021. The latest inflation forecast for 2021 is lower compared to the previous forecast due to the impact of lower tariffs on imported pork, lower-than-expected inflation for March and April 2021, slower domestic economic activity in H1 2021, and the continued appreciation of the peso.

- Meanwhile, the prospects for a sustainable recovery remain dependent on timely and robust responses to the pandemic and the risk of further outbreaks of COVID-19 infections. Critical near-term issue would be on the progress of the vaccine rollout programs to support the safe further reopening of the economy along with additional fiscal stimulus to boost aggregate demand.

- Given these key developments, the Monetary Board was of the view that it remained prudent to keep the current monetary policy settings unchanged to provide a conducive environment for credit growth and to support economic recovery amid the uncertainty brought about by the COVID-19 pandemic in domestic activities. At the same time, prospects for sustainable recovery remained dependent on responses to the pandemic and the risk of further outbreaks of Covid-19 infections.

[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 next meeting of the Monetary Board on the monetary policy stance is scheduled on 24 June 2021.

III. Recent Developments and Inflation Outlook

The Monetary Board considered the developments listed below in deciding appropriate the monetary policy stance:

A. Domestic price conditions

- Headline inflation was steady at 4.5 percent year-on-year in April compared to the previous month. Inflation was unchanged during the month as slower price increases of food items were offset by higher non-food inflation. Food inflation fell to 5.0 percent year-on-year in April from 6.2 percent in the previous month. Rice prices declined relative to year-ago levels, which led to negative inflation rate in April at -0.3 percent from 0.9 percent in the previous month. Likewise, vegetable prices declined due to ample domestic supply amid improved weather conditions. Inflation for other food commodities such as, fruits, milk, cheese, and eggs, as well as fruits and food products not elsewhere classified also slowed down in April, which contributed to the moderation in food inflation. This brought the year-to-date average inflation rate to 4.5 percent year-on-year for the first four months of 2021, higher than the government's annual average target of 2-4 percent.

- Core inflation, which excludes selected volatile food and energy items to depict underlying demand-side price pressures, eased to 3.3 percent year-on-year in April from 3.5 percent in the previous month.

B. Inflation expectations

- Results of the BSP's survey of private sector economists for April 2021 showed an unchanged mean inflation forecast for 2021 at 4.3 percent. By contrast, the mean inflation forecasts for 2022 and 2023 increased slightly but remained within the target range at 3.1 percent from 3.0 percent previously in the March 2021 survey.

C. Inflation outlook

- The latest baseline inflation forecasts are 3.9 percent for 2021 and 3.0 percent for 2022. The latest inflation forecast for 2021 is lower compared to the previous forecast of 4.2 percent due to the impact of lower tariffs on imported pork, lower-than-expected inflation for March and April 2021, slower domestic economic activity in H1 2021, and the continued appreciation of the peso. These factors were partly offset by the higher assumptions for global oil and non-oil prices. Meanwhile, the inflation forecast for 2022 is revised upwards from the previous forecast of 2.8 percent owing largely to higher global crude oil prices and improved domestic growth prospects for 2022.

Baseline Inflation Forecasts		
	25 March 2021 MB Meeting	**12 May 2021 MB Meeting**
2021	4.2	3.9
2022	2.8	3.0

- The risks to the inflation outlook are seen to be broadly balanced for 2021 and 2022. Uncertainty in the implementation of the approved reduction in pork import tariffs along with the impact of an earlier-than-expected easing of quarantine measures and stronger global growth are the primary upside risks to inflation. Meanwhile, faster arrival of imported pork with a lower tariff and the potential impact on domestic economic growth prospects of delays in the easing of containment measures as well as a weaker-than-expected global recovery owing to the spread of new COVID-19 variants are the main sources of downside risks.

D. Demand conditions

- There was a downward revision in the GDP forecast for 2021, reflecting mainly the higher-than-expected contraction for Q1 2021 and the lower growth nowcast for Q2 2021 due to the extension of stricter community quarantine measures in Metro Manila and surrounding provinces along with the continued weakness in the labor market, particularly in the manufacturing and services sectors. The domestic economy contracted by 4.2 percent in Q1 2021, but could start to rebound from Q2 2021 onwards. Meanwhile, the recovery in growth for H2 2021 and 2022 is expected to be supported by the implementation of the CREATE and FIST laws as well as the overall recovery in global economic activity. Based on the latest projected growth path, real GDP is projected to return to its 2019 level by Q3 2022.

- High-frequency data also showed mobility falling sharply with the imposition of quarantine measures in the NCR-Plus area (NCR, Bulacan, Cavite, Laguna, and Rizal) followed by a rapid bounceback after government eased restrictions to Modified Enhanced Community Quarantine (MECQ). The Google mobility report showed that mobility have fallen below the pre-pandemic baseline after peaking in December 2020. At the same time, the Easter holiday and the reimposition of the Enhanced Community Quarantine (ECQ) in the NCR-Plus area on 29 March, with shorter curfew hours, resulted in subdued mobility figures for end-March to beginning April. With the shift to the less stringent MECQ restrictions, mobility data have shown an uptick in mid-April.

E. Supply-side indicators

Developments in Agriculture

- Domestic retail rice prices remained stable as envisioned with the enactment of R.A. No. 11203. Although domestic rice prices are expected to trend upwards in the period between harvests, the easing of RMR prices in

March may be seen as moderation from the broad-based spike in the prices of agricultural commodities in January and February 2021.

Furthermore, the African Swine Fever (ASF) disease continued to spread in most parts of the Philippines bringing the affected areas to about 40 provinces and estimated losses of 3.0 million pigs. To temporarily reduce the tariff rates on pork imports, President Duterte issued Executive Order (E.O.) 128 on 7 April 2021. Under E.O. 128, the tariff rate for imported pork within quota or minimum access volume (MAV) will be reduced to 5.0 percent for the first three months upon the E.O.'s effectivity and 10.0 percent for the fourth to 12th month. Furthermore, the DA and the DTI implemented the suggested retail rice (SRP) on imported pork at ₱270 per kilo for *kasim*; and ₱350 per kilo for *liempo* effective on 9 April 2021.

- According to PAGASA's latest climate advisory, La Niña conditions continued to weaken. Nevertheless, PAGASA noted that La Niña might still affect parts of the country, which will likely result in above-normal rainfall conditions in April 2021.

Oil Price Developments

- Global crude oil prices have been on an uptrend in recent months due to expected recovery in global economic activity with the rollout of vaccines and despite the decision of OPEC+ members to ease production cuts. However, international crude oil prices fell in April as rising COVID-19 cases sparked concern over demand recovery amid the easing of production cuts from OPEC+. Meanwhile, futures prices remained in backwardation albeit at a generally higher path compared to recent weeks, reflecting both upside and downside factors to the oil price path.

Developments in the Utilities Sector

- Overall electricity rates increased slightly due mainly to higher generation charges. According to Meralco, the higher charges in the Wholesale Electricity Spot Market (WESM) led to the generation charge increase. WESM charges in turn were pushed upwards by tighter supply conditions in the Luzon power grid. The increased WESM charges were offset by the decreases in charges from the Independent Power Producers (IPPs) and Power Supply Agreements (PSAs) due to improved average plant dispatch and the appreciation of the peso against the US dollar.

F. Financial market developments

- The peso appreciated against the US dollar on market optimism following the easing of headline inflation in March and April 2021, upbeat remittance data for February 2021, Moody's Investors Service improved outlook on the local banking industry, and the arrival of more vaccine doses in April.

G. Domestic liquidity and credit conditions

- Liquidity conditions remained at an adequate level to support economic activity. Domestic liquidity (M3) expanded by 8.3 percent year-on-year, slightly slower than the 9.4-percent growth in February.

- Credit activity has weakened further banks reported tighter lending standards due to a reduced tolerance for risk and a less favorable economic outlook. Preliminary data show that outstanding loans of universal and commercial banks decreased by 4.5 percent year-on-year in March following a 2.7-percent fall in February. Furthermore, latest results of the Senior Bank Loan Officers' Survey (SLOS) continued to point to a net tightening of overall credit standards for both loans to businesses and consumers in Q1 2021. Respondent banks attributed the tightening of credit standards largely to deterioration in profiles of borrowers, reduced tolerance for risk, and less favorable economic outlook, among other factors.

- As the pandemic continued to affect the real economy, domestic financial market conditions remained stable amid supportive monetary policy settings and ample financial liquidity while market interest rates remained at all-time lows.

H. Fiscal developments

- The National Government (NG) recorded a ₱321.5 billion fiscal deficit for January – March 2021. Netting out the interest payments in NG expenditures, the primary deficit amounted to ₱195.6 billion, a reversal from the ₱33.7 billion surplus recorded in the previous year.

I. External developments

- Global economic prospects have further improved following better-than-expected performance among major economies in Q1 2021 and the successful rollout of vaccines in key economies around the world. Global economic activity expanded faster in March as output improved in both the manufacturing and service sectors amid global demand recovery and the reopening of major economies. Nevertheless, the pace of global recovery remained uneven as countries continued to face challenges from the pandemic.

- In the April 2021 World Economic Outlook (WEO) Update, the IMF raised its full-year GDP growth projection for 2021 relative to its January 2021 WEO forecast. The upward revision reflected the stronger-than-projected economic recovery across regions due mainly to expectations of wider vaccine availability as well as the impact of additional fiscal response in the US. Risks to growth outlook appeared evenly balanced in the near term but leaned toward the upside further out. According to the report, the main risk factors to the upside include expedited vaccine production and rollout, unanticipated impact of strong fiscal support, and coordinated monetary and fiscal policies. On the downside, the main risks to the outlook include the resurgence of COVID-19 cases; tighter financial conditions; likelihood of substantial and persistent damage to supply potential or extended scarring, especially in emerging market and developing economies (EMDEs); intensified social unrest; frequent and severe natural disasters; and geopolitical, trade, and technology risks.