BANGKO SENTRAL NG PILIPINAS

HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 17 FEBRUARY 2022 [1]

I. Monetary Policy Decision

The Monetary Board decided to:

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

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 decision of the Monetary Board is based on the assessment that inflation could average within the 2-4 percent target range for 2022 and 2023. However, the inflation projections have slightly increased from the previous monetary policy meeting, reflecting the impact of higher domestic food inflation and global oil prices. Inflation expectations have likewise risen marginally but continue to be anchored within the target band.

- The risks to the inflation outlook continue to lean slightly towards the upside for 2022 but remain broadly balanced for 2023. Upside risks are linked mainly to the continued shortage in domestic pork and fish supply and the possible impact of higher oil prices on transport fares. The implementation of non-monetary measures to ensure adequate supply of key food commodities must be sustained in order to mitigate supply-side pressures on inflation. At the same time, increased volatility in international oil prices warrants close monitoring and appropriate interventions when necessary in order to arrest potential second-round effects. Meanwhile, downside risks still emanate from the lingering threat of COVID-19 infections owing to possible case resurgence from new variants, as delays in the easing of containment protocols could temper domestic growth prospects.

- The Monetary Board also observed that the domestic economic recovery has continued to gain traction on the back of the Government's ongoing vaccination program and the easing of mobility restrictions. However, elevated global commodity prices, heightened geopolitical tensions, and

[1] The discussions herein reflect the assessment made by the Monetary Board based on a comprehensive set of macroeconomic and financial 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 March 2022.

the uneven pace of vaccinations across countries could dampen the outlook for global economic recovery.

- On balance, the Monetary Board deems it prudent to maintain the BSP's accommodative policy stance given a manageable inflation environment and emerging uncertainty surrounding domestic and global growth prospects. Looking ahead, given the stronger signs of recovery in output growth and labor market conditions and improvements in domestic financial markets, the BSP will continue to carefully develop its plans for the eventual normalization of its extraordinary liquidity measures when conditions warrant, in keeping with our price and financial stability mandates.

III. Recent Developments and Inflation Outlook

The Monetary Board considered the recent macroeconomic and financial developments listed below in deciding the appropriate monetary policy stance:

A. Domestic price conditions

- Using the 2018-based CPI series, headline inflation eased to 3.0 percent in January 2022 from 3.2 percent in December 2021. Inflation slowed down in January due to lower meat prices as pork supply stabilized owing partly to targeted government and private sector measures. Similarly, non-food inflation moderated, driven mostly by the slowdown in large-weighted CPI items such as housing, water, electricity, gas, and other fuels, along with restaurants and accommodation services. Electricity rates declined in January due to lower generation costs while liquefied petroleum gas (LPG) prices also fell, offsetting the increase in domestic fuel prices.

B. Inflation expectations

- Inflation expectations remain anchored to the target range over the policy horizon. The February 2022 survey results of inflation forecasts show that private sector economists expect inflation to average at 3.5 percent for 2022 from 3.4 percent in the previous survey round.[2] Meanwhile, the mean inflation forecasts for 2023 and 2024 were also within the government's target range of 2-4 percent at 3.1 percent (from 3.2 percent) and 2.9 percent (from 3.3 percent), respectively.

C. Inflation outlook

- The latest baseline inflation forecasts are 3.7 percent for 2022 and 3.3 percent for 2023, using the newly released 2018-based CPI series. The inflation forecasts for 2022 and 2023 are slightly higher relative to the estimates from the previous forecast round. The higher inflation path in

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[2] There were 22 respondents in the BSP's survey of private sector economists in February 2022. The survey was conducted from 4 to 10 February 2022.

2022 is mainly attributed to elevated domestic food and oil inflation. Nonetheless, imported oil and food inflation is projected to ease in 2023 as global supply chain disruptions are expected to dissipate. Inflation is seen to decelerate in early 2022 due mainly to negative base effects from the uptick in pork prices from the previous year. However, inflation is projected to accelerate slightly above the target range in Q2 2022 driven by elevated global oil and non-oil prices and positive base effects. Nonetheless, inflation is projected to decelerate back to within the target in Q3 2022 and in Q4 2022 as imported oil and food inflation is seen to ease amid expectations of higher production and improvements in global supply chain.

Baseline Inflation Forecasts		
	16 December 2021 MB Meeting (2012-based)	**17 February 2022 MB Meeting** (2018-based)
2022	3.4	3.7
2023	3.2	3.3

- The risks to the inflation outlook are now seen to be weighted slightly toward the upside for 2022, but broadly balanced for 2023. The potential impact of higher global food prices, the continued shortage in domestic pork and fish supply, and possible jeepney fare hikes due to higher oil prices are the major upside risks over the near term. Meanwhile, the possible 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. Risks to the global growth outlook are tilted to the downside in view of tight labor markets in advanced economies as well as uncertainty on inflation and monetary policy.

D. Demand conditions

- Domestic economic recovery appears to be gaining traction but the full-year growth forecast for 2022 is lower compared to the previous round due to the impact of the stricter COVID-19 alert level imposed during the start of the year as well as the slightly slower world GDP growth outlook. Global economic output expanded at a slower pace as rising COVID-19 cases, protracted supply chain disruptions, and persistent inflationary pressures dampen output capacity as well as demand conditions and consumer confidence. Meanwhile, household consumption and output for most production sectors has remained below the levels recorded prior to the pandemic period.

- Mobility indicators have declined in recent months with the shift to a more stringent alert level amid the surge in COVID-19 infections as well as the detection of local transmission of the omicron variant. Using the 7-day moving average, mobility in grocery and pharmacy, parks, retail and recreation locations declined, which may be attributed to the stricter mobility restrictions imposed on unvaccinated people such as stay-at-home orders. Meanwhile, the duration for people staying in residential areas rose during the period, consistent with the decline in mobility for other location categories.

- Meanwhile, labor market conditions improved, with some indicators performing even better than during the pre-pandemic period. Relative to the pre-pandemic period, employment rate was higher in January 2022 at 94.7 percent, while the unemployment rate of 5.3 percent is higher by only about 881,000 unemployed compared to pre-pandemic level. However, more granular data indicate that employment quality has not yet recovered relative to pre-pandemic level as recent employment gains were mostly low-skilled and less remunerative.

- Nevertheless, economic recovery in 2022 to 2023 is expected to be supported by the implementation of the Corporate Recovery and Tax Incentives for Enterprises (CREATE) Law and Financial Institutions Strategic Transfer (FIST) Act as well as improvements in external demand. The latest forecasts also show that the country's real GDP will return to its 2019 level by Q3 2022.

E. Supply-side indicators

Developments in Agriculture

- Sustained import arrivals and improved local harvest have kept rice prices at bay even amid the reimposition of mobility restrictions and ongoing planting season. Nonetheless, domestic retail rice prices remained generally stable as envisioned with the enactment of the Republic Act (R.A.) No. 11203.

- Meanwhile, the Department of Agriculture (DA) has also rolled-out targeted measures to help stabilize domestic supply of agricultural commodities such as pork, rice, and fish.

Oil Price Developments

- Global oil prices surged in January and early February 2022 due to geopolitical tensions in Emerging Europe and the Middle East, combined with tight supply conditions from disruptions even as OPEC+ gradually raised production. Heating oil demand is also expected to strengthen given snowfall in the Central and North-Eastern in the United States. At the same time, still elevated natural gas prices, which could be exacerbated with the ongoing Ukraine crisis, could drive oil prices higher as consumers switch to oil products. Meanwhile, futures prices remained in backwardation, which suggests that crude oil prices would decline going forward.

Developments in the Utilities Sector

- The overall electricity rate continued to decline due mainly to lower generation charge. The downward adjustment in the generation cost was on the back of lower costs from Independent Power Producers (IPPs) and Wholesale Electricity Spot Market (WESM), according to Meralco. Charges from the IPPs fell due to higher plant dispatch of Quezon Power and First Gas – Sta. Rita. Similarly, WESM charges went down due to significant reduction in Meralco's WESM purchases which mitigated the impact of higher spot market prices during the January 2022 supply month.

- Meanwhile, the decreases in IPPs and WESM charges were partly offset by the increase in costs from the Power Supply Agreements (PSAs) due to lower demand that led to lower excess energy deliveries as well as the lower plant dispatch of San Buenaventura amid scheduled maintenance.

F. Financial market developments

- The peso depreciated against the US dollar in January 2022 relative to December 2021. The peso depreciated due partly to concerns over the impact of typhoon Odette on the economy and the reimposition of tighter restrictions in NCR and some areas in the country due to a surge in coronavirus cases. In addition, (i) expectations of hawkish stance from the US Federal Reserve amid inflation risks; (ii) the increase in global oil prices following geopolitical tensions in the Middle East; and (iii) the slowdown in China's economy alongside the surprise policy rate cut by the People's Bank of China (PBOC) likewise weighed down the peso.

- Amid improving economic condition, lending picked up and loan quality further improved. Non-performing loans (NPLs) displayed a downtrend. Risk-based capital adequacy ratio (CAR) and Basel III leverage ratio of Philippine banks including liquidity capital ratio (LCR) and net stable funding ratio (NSFR) were well-above the BSP thresholds. The BSP relief measures are still in place to support credit growth in the country and, at the same time, provide continued access to financial services to households and vulnerable sectors. The extension of prudential relief measures intends to sustain the momentum of bank lending as well as minimize the possible long term economic scarring brought about by the COVID-19 pandemic.

G. Domestic liquidity and credit conditions

- Liquidity in the financial system continues to be ample. Preliminary data show that domestic liquidity (M3) expanded by 7.7 percent year-on-year to about ₱15.3 trillion in December 2021 following an 8.3-percent expansion in November.

- Credit activity continued to exhibit signs of recovery in recent months, reflecting the improvement in business activity amid easing quarantine restrictions, declining COVID-19 cases, and further progress in terms of vaccination. Preliminary data show that outstanding loans of universal and commercial banks (U/KBs), net of reverse repurchase (RRP) placements with the BSP, grew at a faster rate of 4.6 percent year-on-year in December 2021 from 4.0 percent in November.

H. Fiscal developments

- The National Government (NG) recorded a ₱1,332.1 billion fiscal deficit for January – November 2021. Netting out the interest payments in NG expenditures, the primary deficit amounted to ₱930.0 billion, thirty percent higher than the amount recorded in the previous year. The NG continues to have ample fiscal space to help cushion the pandemic's impact and provide further support to economic recovery.

I. External developments

- Global economic activity expanded at a slower pace in January 2022 as rising COVID-19 cases, protracted supply chain disruptions, and persistent inflationary pressures reduce output capacity and dampen demand conditions and consumer confidence. The JP Morgan Global All-Industry Output Index posted a purchasing managers' index (PMI) reading of 51.4 in January from 54.3 in the previous month as growth of output, new business, and outstanding business moderated due mainly to surging COVID-19 cases worldwide.

- Persistent global supply chain disruptions continued to affect manufacturing activity in some economies. The pace of expansion in US manufacturing activity eased as new orders, production, and inventories grew at a slower pace amid rising prices, protracted supply disruptions, and labor shortages. China's seasonally adjusted manufacturing PMI returned to contraction territory as quarantine measures were reinstated to curb rising COVID-19 cases. Meanwhile, manufacturing activity in the euro area and Japan expanded at a faster rate due to favorable demand conditions. However, the supply side of the manufacturing sector continued to hinder efficient business operations. The Nikkei ASEAN Manufacturing PMI settled at 52.7 in January 2022, unchanged from the recorded PMI reading in December.