I. Economic Outlook

1. Baseline Forecasts

The latest baseline forecasts show a slightly lower path compared to the previous Monetary Policy Report (MPR). Inflation is projected to average at 3.6 percent for 2024, slightly lower by 0.1 percentage point (ppt). The downward revision is driven by lower-than-expected inflation outturns, peso appreciation, and lower global crude oil prices, partly offset by higher assumptions for global non-oil prices, stronger domestic growth outlook, impact of *El Niño* weather conditions, and minimum wage adjustments in areas outside NCR (AONCR). Meanwhile, the inflation forecast for 2025 is broadly unchanged at 3.2 percent.

Inflation is projected to average within the target range over the policy horizon. While inflation is likely to settle within the target in Q1 2024, inflation could rise temporarily above the target for the period April to July 2024 due to possible price pressures from lower domestic supply of rice and corn as well as positive base effects due to the slowdown in food and energy inflation during the same period in 2023. Subsequently, inflation is projected to return to the target range for the rest of the year.

Table 1. BSP Average Baseline Inflation Projections
in percent

	November 2023 MPR[a]	February 2024 MPR[b]
2024	3.7	3.6
2025	3.2	3.2

Source: BSP estimates
[a] Baseline forecasts from 16 November 2023 monetary policy meeting
[b] Baseline forecasts from 14 February 2024 monetary policy meeting

Domestic economic activity will remain intact over the medium term, but growth could settle below the DBCC's target of 6.5-7.5 percent for 2024 and 6.5-8.0 percent for 2025.[4] The projected GDP growth path is supported by the improved global growth outlook and decline in global crude oil prices, tempered in part by the lagged impact of the policy rate adjustments.

While the projected impact of the BSP's policy rate adjustments is likely to peak in 2024, growth in the medium term could also be supported by structural reform measures that could enhance investment climate as well as economic sentiment in the country.[5] These measures include the recent ratification of the Regional Comprehensive Trade Partnership (RCEP) Agreement, which is seen to support greater market access for goods and services, reduced trade barriers, and improved export competitiveness from simplified and harmonized rules. Complementary to RCEP's ratification is the recent implementation of key economic liberalization laws such as the amendments to the Retail Trade Liberalization Act (RTLA), Foreign Investments Act (FIA), Public Service Act (PSA), and the Build-Operate-Transfer (BOT) Law.

[4] Based on the on the 186th Development Budget Coordination Committee (DBCC) Meeting on 15 December 2023.
[5] These measures have not been incorporated in the baseline GDP growth forecasts.

Nonetheless, the economy is projected to operate slightly below its potential. The output gap is estimated to be slightly negative in Q4 2023 with the economy projected to operate slightly below its potential over the policy horizon. The overall balance of demand and supply conditions, as captured by the output gap or the difference between actual and potential output, indicates possible disinflationary pressures over the policy horizon.

Estimates from the BSP's Policy Analysis Model for the Philippines (PAMPh)[6] indicate that the output gap is estimated to be slightly negative in 2024 and 2025, as the impact of previous policy interest rate adjustments takes hold on the economy. A projected slowdown in global growth owing in part to tight monetary conditions across countries could likewise dampen aggregate demand. Nonetheless, the output gap could be supported by higher consumption owing to higher wages and the increased value of remittances amid a peso depreciation. Meanwhile, potential output is expected to be sustained by improvements in labor market conditions and continued investment growth. Productivity growth is also seen to continue owing largely to generally robust economic activity and robust infrastructure spending. Moreover, key structural reforms, such as Corporate Recovery and Tax Incentives for Enterprises (CREATE), RCEP, and PSA could shore up investments and business activity, which could in turn help accelerate the country's potential output.

The exchange rate is expected to settle within the DBCC's assumptions of ₱55.00-58.00/US$1 for 2024 and 2025.[7] The projected exchange rate for 2024 and 2025 appreciated from previous round due mainly to the wider real interest rate differential arising from the expected larger interest rate reduction by the US Federal Reserve in 2024.

2. Key Forecast Assumptions

External Factors

World GDP Growth. The global economy is seen to grow below historical average over the policy horizon. While the latest assumptions for 2024 and 2025 are higher compared to the previous round on account of greater-than-expected resilience in the United States, as well as the renewed fiscal support in China, global growth is seen to remain below the pre-pandemic historical average of 3.6 percent from 2000-2019 owing mainly to elevated central bank policy rates to fight inflation and a withdrawal of fiscal support amid high debt weighing on economic activity.

In its January 2024 World Economic Outlook (WEO) Update, the International Monetary Fund (IMF) projects global growth for 2024 at 3.1 percent, higher by 0.2 ppt from the October 2023 WEO. Meanwhile, the forecast for 2025 is unchanged at 3.2 percent. The IMF noted that the likelihood of a hard landing has receded and that the risks to the global outlook are broadly balanced compared to the assessment in the October 2023 WEO.

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[6] The PAMPh is a monetary policy model for a small open economy like the Philippines. It is a semi-structural gap model based on New Keynesian foundations with a general equilibrium framework and forward-looking features that allow for the assessment of the dynamic path of key macroeconomic variables in a theoretically consistent manner. The BSP is currently undergoing a multi-year technical assistance (TA) mission with the IMF's Institute for Capacity Development to further improve the structural features and forecasting performance of the PAMPh to serve as the BSP's workhorse model for medium-term forecasting and policy analysis.
[7] Based on the on the 186th Development Budget Coordination Committee (DBCC) Meeting on 15 December 2023.

Table 2. World GDP Growth
in percent

	November 2023 MPR	February 2024 MPR
2024	2.9	3.1
2025	3.2	3.2

Source: WEO Update (IMF, January 2024), WEO (IMF, October 2023)

Dubai Crude Oil Prices. Global crude oil prices are set consistent with oil futures market data and the latest assessment by international energy agencies on the outlook for the global oil market. Developments in the domestic oil market in turn are assumed to broadly follow the trend in the world oil market. The Dubai crude oil assumptions in the latest round are based on the average futures path from 23 January to 5 February 2024.

Table 3. Dubai Crude Oil Price Assumptions
average, in US$ per barrel

	November 2023 MPR	February 2024 MPR
2024	82.3	77.5
2025	78.0	73.5

Source: Bloomberg, BSP Estimates

Assumptions for global crude oil prices are lower compared to the previous round. The latest futures path shows crude oil prices declining in the next two years as production growth is expected to slightly outpace demand increase, allowing inventories to build up modestly and contribute to downward pressures on crude oil prices. This reflected projections of lower global fuel consumption growth over the next two years, with the US Energy Information Agency (US EIA) citing the slowdown of oil demand in China due to easing GDP expansion, shift to electric cars, and the end to the post-pandemic recovery-related growth. The increase in global oil production is also seen to slowdown as OPEC+ continues its policy of production restraint. Nonetheless, global production is still anticipated to exceed consumption by mid-2025, leading to an increase in petroleum inventories from non-OPEC countries.

To determine the impact on the inflation forecasts for 2024 and 2025 of various outturns for world oil prices, scenarios ranging from US$70-US$130 per barrel were simulated. The scenarios assume that oil prices are sustained at these levels starting in March 2024. Inflation is seen to breach the upper end of target range if Dubai crude oil price averages above US$90 per barrel in 2024 and around US$95 per barrel in 2025. It should be noted that these oil price scenarios considered only the direct effects and do not incorporate any potential second-round effects on transport fares, food prices, and wage increases among others.

Table 4. Impact of Alternative Dubai Crude Oil Price Scenarios on Inflation
in percentage points

Year	2024	2025
Baseline Inflation Forecast (in US$)	3.6	3.2
70	3.4	3.0
75	3.5	3.2
80	3.7	3.5
85	3.8	3.7
90	4.0	3.9
95	4.1	4.1
100	4.2	4.3
105	4.4	4.5
110	4.5	4.7
115	4.6	4.9
120	4.7	5.0

Source: BSP estimates

World Non-Oil Prices. The latest assumptions for global non-oil commodities show a continued decline in prices over the policy horizon, but at a slower rate compared to previous round for 2024, based on the IMF's January 2024 WEO Update. Global non-fuel price inflation is seen to decline by 0.9 percent in 2024 and 0.4 percent in 2025 compared to the previous assumption of 2.7 percent and 0.1 percent decrease for 2024 and 2025, respectively. Adverse risks from commodity price spikes amid geopolitical and weather shocks remain. The conflict in Gaza and Israel could escalate further, while continued attacks in the Red Sea and the ongoing war in Ukraine could lead to resurgence of supply-side constraints. Container shipping costs have already increased sharply and the situation in the Middle East remains volatile. More extreme weather shocks, including floods and drought, together with the *El Niño* phenomenon, could also cause spikes in food prices.

Table 5. World Non-Oil Price Inflation
in percent

	November 2023 MPR	February 2024 MPR
2024	-2.6	-0.9
2025	-0.1	-0.4

Source: WEO (IMF, November 2023), WEO Update (IMF, July 2023)

Federal Funds Rate. The latest federal funds rate assumptions, based on the futures prices as of 5 February 2024, are lower for 2024 and 2025 relative to the previous round. The current futures path is consistent with the market expectations of the US Federal Reserve keeping the federal funds rate target unchanged until April 2024. Markets are pricing in a 100-bp easing in 2024 starting in May with an additional 75-bp rate cut in 2025. By contrast, the Federal Open Market Committee's (FOMC's) dot plot in its December 2023 meeting indicated a 75-bp cut in 2024 followed by a 100-bp cut in 2025.

Table 6. Federal Funds Rate
end-period, in percent

	November 2023 MPR	February 2024 MPR
2024	4.6	4.3
2025	4.1	3.6

Source: Bloomberg

Domestic Factors

RRP Rate and Reserve Requirement Ratio (RRR). The forecast path assumes unchanged interest rate over the policy horizon with the target RRP rate at 6.50 percent. Meanwhile, the RRR was maintained at 9.5 percent until end-2025.

Wages. The baseline forecast is consistent with the ₱40.00 minimum wage hikes for NCR in July 2023 as well as the 8.7 percent average wage increase for non-agricultural workers in AONCR. Furthermore, further increases of ₱28.00 in August 2024 and ₱29.00 in September 2025 are assumed. This is equivalent to an annual increase of 4.6 percent for both years, in line with historical wage increases.

Fiscal Sector. The baseline inflation forecasts are consistent with the government's fiscal deficit assumption of 5.1 percent for 2024 and 4.1 percent for 2025 based on the medium-term fiscal program of the DBCC as of 15 December 2023.

Alcoholic Drinks. The baseline forecasts reflect the impact of annual adjustments in the prices of alcoholic beverages (0.7 percent of the CPI basket) as mandated in Republic Act (R.A.) no. 11467. Higher excise taxes for fermented liquor, wine, and distilled spirits will be implemented on a staggered basis from 2020 to 2024 and shall increase by 6.0 percent every year from 2025 onwards.

Tobacco Products. The President signed R.A. no. 11346, increasing further the excise tax on tobacco products (0.9 percent of the CPI basket) to fund the Universal Healthcare Act. Under the law, the tax per pack of cigarettes will be raised on a staggered basis to ₱60.00 per pack in 2023 and subject to a 5.0 percent annual indexation onwards.

Table 7. Excise Tax

Year	Cigarettes (₱ per pack)	Fermented Liquor (₱ per liter)	Wine (₱ per liter)	Distilled Spirits	
				Excise Tax (₱ per liter)	Ad Valorem Tax (%)
2024	5%	43.0	63.1	66.0	22%
2025		6% indexation			22%

Source: R.A. nos. 11346 and 11467

Water Rates. The Metropolitan Waterworks and Sewerage System (MWSS) approved the rate hike requests of Manila Water Company and Maynilad Water Services for 2023-2026. The water rate rebasing process is conducted every five years to set the rates for water and sewerage services for water concessionaires to recover its operating, capital, maintenance, and investment expenditures. The second tranche of the rate rebasing adjustment took effect on 1 January 2024 with Maynilad Water Services Inc. raising rates by an average of ₱7.87 per cubic meter and Manila Water Co. Inc. increasing their rates by an average of ₱6.41 per cubic meter. For the subsequent years, the rates for Manila Water customers will be higher by ₱3.25 in 2025, ₱3.00 in 2026, and ₱1.08 in 2027 per cubic meter.

Meanwhile, the rates for Maynilad customers will be higher by ₱2.12 in 2025, ₱0.84 in 2026, and ₱0.80 in 2027.

Lower domestic supply due to weather conditions and higher global prices. The baseline forecast considers NEDA's latest supply and demand outlook indicating total rice and corn supplies to contract year-on-year (y-o-y) for the period Q2 to Q4 2024. The NEDA projections reflect the impact of *El Niño* and other weather disturbances as well as higher global prices, with *El Niño* dry conditions seen to be strong until February 2024 before transitioning to weak conditions from March to May 2024 and reverting to ENSO-neutral conditions from June 2024 onwards, based on the latest climate outlook of PAGASA as of 24 January 2024. Despite weakening *El Niño* conditions by June 2024, rice and corn prices are expected to remain higher for the rest of 2024 due to the projected decline in domestic supply.

3. Risks to the Outlook

While the risks to the inflation outlook continue to tilt toward the upside over the policy horizon, inflation risks in 2024 have eased compared to the previous round. The latest fan chart remains skewed towards the upside as reflected in the high probability of inflation breaching high-end of the target band in 2024 to 2025.

Using the 90 percent confidence interval for the fan chart, estimates indicate that the probability of average annual inflation settling within the 3.0 percent ± 1.0 percentage point target range is 44.6 percent for 2024 and 49.7 percent for 2025. The probability of inflation breaching the high end of the target range is 51.4 percent for 2024 and 37.1 percent for 2025. This reflects the downward adjustment in the baseline forecasts over the policy horizon.

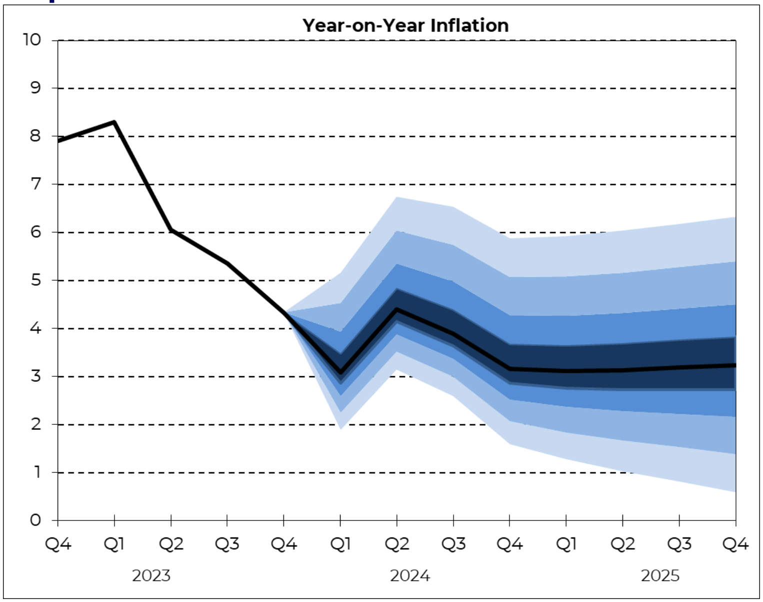
The latest probability distribution shows a higher likelihood of inflation settling within the target for 2024 at 44.6 percent compared to 42.8 percent in the previous round. Meanwhile, the probabilities of inflation breaching the low end of the target range for 2024 to 2025 remain low.

Table 8. Probability Distribution of Inflation Forecasts
in percent

	Pr(<2%)		Pr(2-4%)		Pr(>4%)	
	Nov 2023 MPR	Feb 2024 MPR	Nov 2023 MPR	Feb 2024 MPR	Nov 2023 MPR	Feb 2024 MPR
2024	3.4	4.0	42.8	44.6	53.8	51.4
2025	12.8	13.2	49.5	49.7	37.7	37.1

Source: BSP estimates

Figure 1. Inflation Projection
in percent



Source: BSP estimates

Table 9. Inflation Projection Ranges at Various Confidence Intervals Using the Fan Chart
in percent

Confidence Interval (%)	Projection Range (%)	
	2024	2025
80	2.6 – 5.5	1.4 – 5.5
90	2.3 – 6.1	0.9 – 6.1

Source: BSP estimates

Table 10. Risk Matrix[8]

	Risks	Probability	
		November 2023 MPR	**February 2024 MPR**
Upside Risks	Higher electricity rates	High	High
	Higher transport charges	Medium	Low
	Higher oil prices	Medium	Low
	Higher domestic food prices	Medium	Medium
	Impact of *El Niño* conditions	Medium	Low
Downside Risk	Measures to Mitigate Impact of *El Niño*	Medium	Low

[8] The BSP considers different scenarios that pertain to upside and downside risks to the inflation outlook, which is summarized in a risk matrix. The various scenarios are then assigned probability values. Scenarios that have more than 75 percent probability of taking place over the forecast horizon are incorporated in the baseline. The estimated impact of each scenario is then multiplied by the assigned probabilities. The sum of the weighted impact for each year will indicate whether the risks to the outlook are balanced, on the upside, or on the downside.

The estimated impact of upside risks to the inflation outlook outweighs the possible impact of downside risks. Should the risks materialize at their assigned probabilities, inflation is seen to average at 3.9 percent in 2024 and 3.5 percent in 2025.

Compared to the previous MPR, the risk-adjusted forecast is lower for 2024 by 0.5 ppt, which can be attributed to the lower baseline forecast and the decline in the estimated risks for the year. The lower estimated impact of risks for 2024 emanates from the removal of the impact of higher transport fares from the jeepney modernization; the lower probability of fare hikes for traditional jeepneys; the lower impact of higher global oil prices; and the removal of the risk from the non-extension of E.O. no. 10. Meanwhile, the risk-adjusted forecast for 2025 is only marginally higher by 0.1 ppt percent due mainly to the shift in the assumed implementation of higher electricity rates.

Table 11. BSP Baseline and Risk-Adjusted Projections
in percent

		November 2023 Monetary Policy Report	February 2024 Monetary Policy Report
Baseline inflation forecast	2024	3.7	3.6
	2025	3.2	3.2
Risk-adjusted inflation forecast	2024	4.4	3.9
	2025	3.4	3.5

The upside risks to the inflation outlook could emanate from higher transport charges, increased electricity rates, higher oil and domestic food prices, and the additional impact on food prices of a strong *El Niño* episode. Meanwhile, the implementation of government measures to mitigate the impact of *El Niño* weather conditions is the primary downside risk to the outlook.

Electricity rates could further increase in 2024. In July 2023, the Supreme Court nullified Energy Regulatory Commission's (ERC) 2014 decision to cap Wholesale Electricity Market (WESM) prices in November to December 2013. The ERC's decision was made to address the higher prices during the maintenance shutdown of the Malampaya gas field. The risk scenario assumes that an estimated ₱22 billion worth of power generation cost will be passed on to consumers starting in June 2024 with the adjustment spread equally over the next two years.

A high probability is assigned to this risk as the ERC is set to release an order that will authorize the collection of the said power generation cost.

Higher transport charges also provide upside risks to the inflation outlook. On 8 October 2023, the LTFRB approved a ₱1.00 provisional increase in the minimum jeepney fare for both traditional and modern jeepneys. As the original petition indicated a ₱5.00 increase, the alternative scenario assumes that the remaining ₱4.00 will be approved and implemented by Q2 2024. A low probability is assigned to this risk given the on-going jeepney modernization.

In addition, a petition was filed by the MRT-3 management with the Department of Transportation (DOTr) on 3 July 2023 to raise the minimum fare of the rail line from ₱13.00 to ₱19.00. A high probability is assigned to this risk following the adjustments in LRT-1 and LRT-2 fares. The alternative scenario assumes implementation by Q2 2024.

Similarly, taxi operators have filed a petition with the LTFRB to raise the ₱5.00 provisional increase in the flagdown rate granted in October 2022, bringing the flagdown rate from the current ₱45.00 to ₱55.00. The scenario assumes that the LTFRB will grant the increase by Q2 2024 with a low probability given broadly stable oil prices.

Meanwhile, the risk of higher jeepney fares following full implementation of the public utility vehicle (PUV) modernization program included in the previous round has been removed. The year-end deadline for the consolidation of the PUV drivers and operators into cooperatives and corporations was moved to Q2 2024 which could push the timeline of the entire program beyond the policy horizon.

An overall low probability is assigned to this risk based on the CPI weights of the transport items.

The escalation of conflicts in the Middle East could lead to higher global crude oil prices. In addition to the conflict between Israel and Palestine, the intensification of tensions in Yemen due to attacks by Houthi rebels could disrupt world oil supply and induce additional uncertainty in global oil prices.

The risk scenario assumes Dubai crude oil prices averaging at US$90/bbl in 2024 based on the peak price levels experienced during start of the Israel-Hamas conflict in 2023. A low probability is assigned to this scenario as tensions have eased and there are no indications of escalation into a direct military exchange between the two regional enemies.

Ongoing supply constraints on livestock, poultry, fish, sugar, and onions could cause a slight uptick to inflation.

- Pork prices remain elevated compared to previous year with the recovery in domestic hog industry still reeling from the impact of the African Swine Fever (ASF) outbreak. As of 19 January 2024, active ASF cases increased to 12 regions from only six in end-December 2023 based on data from the Bureau of Animal Industry (BAI). A medium probability is assigned to this risk with the ASF vaccine still undergoing trials and amid ban of entry of live hogs and pork products in some local government units.

- Meanwhile, after high production costs and the Avian Influenza (AI) put a strain on producers' operations since 2022, chicken meat prices have stabilized while farmgate prices of eggs have declined in 2023 following easing consumption and expanding supply due to favorable weather. A low probability is assigned to this risk with no new cases of AI reported since 13 January 2024.

- Average prices of fish have continued to creep up from December 2023 amid the closed fishing season. While the DA issued Circular No. 36 dated 15 August 2023 on the importation of 35,000 MT of frozen fish, all import clearances are deemed expired after 15 January 2024. A medium probability is assigned to this risk in the absence of adequate sustainable fisheries production programs to ensure sufficiency of fish supply.

- Sugar Regulatory Administration Resolution 2023-159, signed on 26 September 2023 and released on 5 October 2023, halted the release of sugar imports to keep farmgate prices at around ₱3,000 per bag. The resolution applies to the 150,000 metric tons of imported sugar under Sugar Order No. 7 issued in July 2023. A medium probability is assigned to this risk in the absence of a new import program.

- As of January 2024, onion prices remained elevated albeit lower y-o-y. While the DA expects positive growth in harvest in 2024, infestation of armyworms could negatively affect yield. In Nueva Ecija, the DA reported that 366 hectares out of the 10,217 hectares of farmlands planted to onion have been infested by armyworms. In addition, the DA Secretary has ordered a temporary halt to onion imports until May 2024 – possibly extending through July – if domestic harvest of the high value crop remains sufficient to meet local demand. A medium probability is assigned to this risk with the temporary halt in onion imports and possible worsening of armyworms infestation.

An overall medium probability is assigned to this risk based on the relative weights of the commodities in the CPI basket. The scenario assumes that the elevated price levels of the identified commodities will be sustained until Q2 2024.

Further declines in crop production due to strong *El Niño* conditions could lead to higher rice prices. The baseline scenario considers strong *El Niño* conditions until February 2024, easing to moderate conditions in Q2 2024. The risk scenario assumes the strong *El Niño* to persist until Q2 2024, further increasing rice prices due to lower rice production until the end of the year. A low probability is assigned to this risk based on the latest climate outlook from PAGASA.

The effective implementation of government measures to combat the impact of *El Niño* could lower inflation. Government measures include improvement and concreting of irrigation canals, distribution of pumps and engine sets, construction of solar powered irrigation system, established greenhouses, provision of planting materials and farm supplies, various support to fisheries sector, and information campaigns on *El Niño*.