Economic Outlook

1. Baseline Forecasts

The latest baseline forecasts are slightly lower for 2024 and slightly higher for 2025 relative to the projections cited in the February 2024 *Monetary Policy Report*. The forecast for 2024 has declined on account of lower projected inflation for Q2 2024. The forecast for 2025 has increased on account of the recent uptick in global crude oil prices and the depreciation of the peso.

While headline inflation is projected to accelerate above the target range over the near term, inflation is still seen to average within the target range over the policy horizon. Inflation is seen to breach the upper end of the target range from May to July 2024. Domestic supply constraints are seen to continue to exert pressures on the prices of key food items, while positive base effects emanate from the slowdown in food and energy inflation during the same period in 2023. Subsequently, inflation is projected to return to within the target range starting in August 2024 as food and crude oil price pressures ease.

Table 1
BSP Average Baseline Inflation Projections
in percent

	February 2024 *MPR* [a]	**May 2024 *MPR* [b]**
2024	3.6	3.5
2025	3.2	3.3

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

The outlook on domestic economic activity remains intact, even as the economy is projected to operate slightly below potential. Economic growth could settle below the DBCC's target of 6.0-7.0 percent for 2024 and 6.5-7.5 percent for 2025.[4] The projected impact of the BSP's policy rate adjustments is likely to peak in H2 2024. Higher global crude oil prices and positive real interest rates could also temper domestic demand. However, stronger net exports amid an improving global growth outlook could support GDP growth.

Meanwhile, estimates from the BSP's Policy Analysis Model for the Philippines (PAMPh)[5] indicate that the output gap may turn slightly negative in 2024 but will likely close in the latter part of 2025. Domestic economic activity could ease as the effects of previous policy interest rate adjustments and declining real incomes, along with the possibility of tepid global growth, temper aggregate demand. On

[4] Based on the 186th DBCC Meeting on 15 December 2023.
[5] 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.

balance, the latest assessment of the output gap indicates potential deflationary pressures going forward.

Meanwhile, sustained improvements in labor market conditions, continued investment growth, and stable infrastructure spending are seen to continue to drive productivity and potential output.

The peso could weaken but remain within the DBCC's assumptions of ₱55.00-58.00/US$1 for 2024 and 2025.[6] The revised peso outlook for 2024 and 2025 reflects the recent peso depreciation and narrowing interest rate differentials with the US, given market expectations of smaller interest rate reductions by the US Federal Reserve in 2024. The baseline forecasts are consistent with market expectations of a 50-basis-point reduction in the US fed funds rate each in 2024 and 2025.

2. Key Forecast Assumptions

External factors

World GDP growth. Global growth is seen to remain below the historical average of 3.8 percent, reflecting restrictive monetary policies, withdrawal of fiscal support, and low underlying global productivity. Growth in the US could accelerate in 2024 before slowing down in 2025 as gradual fiscal tightening and softening labor market slow aggregate demand. The Euro area is likewise seen to recover from its slow growth in 2023 driven by stronger household consumption. Meanwhile, output in Japan is projected to slow as one-off factors that supported growth in 2023, including a surge in inbound tourism, continue to fade. Similarly, a further slowdown in China is projected from 2024 to 2025 as a post-pandemic boost in consumption and fiscal stimulus ease while weakness in the property sector persists.

In its April 2024 World Economic Outlook (WEO), the International Monetary Fund (IMF) noted that downside risks to the global growth outlook have diminished since October 2023. From a clear tilt toward the downside in 2023, the risks to the outlook now appear more broadly balanced.

Table 2
World GDP Growth
in percent

	February 2024 ***MPR***	**May 2024** ***MPR***
2024	3.1	3.2
2025	3.2	3.2

Source: WEO (IMF, April 2024), WEO Update (IMF, January 2024)

Dubai crude oil prices.[7] Assumptions for global crude oil prices are higher compared with the previous round. The latest futures path shows a significant rise in crude oil prices for 2024 and 2025. Prices increased in April amid falling global oil

[6] Based on the 187th DBCC Meeting on 22 March 2024.
[7] 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. The Dubai crude oil assumptions in the latest round are based on the average futures path from 26 April to 9 May 2024.

inventories and heightened geopolitical tensions in the Middle East. Moreover, the US Energy Information Administration (EIA) expects voluntary OPEC+ crude oil production cuts, and ongoing geopolitical risks could sustain crude oil spot price near US$90.00/bbl for the remainder of 2024 before falling to an average of US$85.00/bbl in 2025 as global oil production picks up.

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

	February 2024 *MPR*	May 2024 *MPR*
2024	77.53	83.69
2025	73.47	79.11

Source: Bloomberg, BSP estimates

Scenarios of various outturns for world oil prices ranging from US$80-US$130 per barrel were also simulated. These assume that global oil prices are sustained at the stated levels starting June 2024. Holding all things constant, inflation is seen to breach the 2.0-4.0 percent target range if the average price of Dubai crude oil exceeds US$125 per barrel in 2024 and US$95 per barrel in 2025.[8]

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

Year	2024	2025
Baseline Inflation Forecast (US$)	3.5	3.3
80	3.5	3.3
90	3.6	3.8
100	3.7	4.3
110	3.9	4.7
120	4.0	5.1
130	4.1	5.5

Source: BSP estimates

World non-oil prices. Based on the IMFs April 2024 WEO, global prices of non-oil commodities are assumed to increase marginally in 2024 and to decline slightly in 2025. A rebound in agricultural commodity prices drives the latest forecasts for non-fuel commodity inflation. Concerns over *El Niño* put upward pressure on the prices of certain tropical crops, Meanwhile, seafood prices surged as demand outstripped supply growth amid stricter environmental legislation in some countries. However, the prices of cereals and vegetable oils declined owing to abundant global supplies. The risks to the price outlook are seen to be balanced, with larger-than-expected harvests offsetting the impact of further trade disruptions in the Black Sea and new food export restrictions.

[8] It should be noted that the impact of 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 5
World Non-Oil Price Inflation
in percent

	February 2024 *MPR*	May 2024 *MPR*
2024	-0.9	0.1
2025	-0.4	-0.4

Source: WEO (IMF, April 2024), WEO Update (IMF, January 2024)

Federal funds rate.[9] The latest federal funds rate assumptions are higher for 2024 and 2025. In the previous round, the US Federal Reserve is expected to reduce interest rates by a sum of 100 bps in 2024 beginning in May. Based on recent indicators, market players now expect the US Fed to hold the federal funds rate target steady until July 2024. Markets also appear to be pricing in an initial cut of 50 bps in July and December, with an additional total reduction of 75 bps in 2025.

Table 6
Federal Funds Rate
end-period, in percent

	February 2024 *MPR*	May 2024 MPR
2024	4.3	5.0
2025	3.6	4.2

Source: Bloomberg

Domestic factors

Target RRP rate and reserve requirement ratio (RRR). The BSP policy interest rate and reserve requirements are expected to remain unchanged over the policy horizon.

Wages. The baseline forecast assumes minimum wage hikes of ₱28.00 in August 2024 and ₱29.00 in September 2025 for the National Capital Region. 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 5.6 percent for 2024 and 5.2 percent for 2025, as stated in the DBCC 's medium-term fiscal program as of March 2024.

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. Excise taxes for fermented liquor, wine, and distilled spirits shall increase by 6.0 percent every year from 2025 onwards.

Tobacco products. Under R.A. No. 11346, signed in July 2019, the tax per pack of cigarettes (0.9 percent of the CPI basket) increases by a standard rate of 5.0 percent every year starting in 2024, following specified increases in the previous years.

[9] Based on futures prices as of 9 May 2024.

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% indexation	43.0	63.1	66.0	22%
2025			6% indexation		22%

Sources: Republic Act Nos. 11346 and 11467

Water rates. The Metropolitan Waterworks and Sewerage System (MWSS) approved the rate hike requests of Manila Water Company, Inc. and Maynilad Water Services, Inc. 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 so they may recover their operating, capital, maintenance, and investment expenditures. The second tranche of the rate rebasing adjustment took effect on 1 January 2024, with both Maynilad and Manila Water raising their rates. Both concessionaires are also seen to increase their rates further in 2025 to 2027.

Rice prices. The baseline forecast considers a possible deficit in local rice production in 2024, reflecting the impact on rice prices of *El Niño* as well as higher global prices. Based on the PAGASA climate outlook as of 24 April 2024, the ongoing *El Niño* dry conditions have weakened, but warmer and drier conditions are seen to continue throughout May before reverting to ENSO-neutral conditions.

3. Risks to the Outlook

Compared with the previous round, the risk-adjusted forecasts (RAF) are lower for 2024 but higher for 2025. After incorporating the impact of risks at their assigned probabilities, inflation is seen to reach 3.8 percent in 2024 and 3.7 percent in 2025.

The risks to the inflation outlook continue to be skewed to the upside over the policy horizon. The upside risks to the inflation outlook could emanate from higher transport charges and toll rates, food prices, electricity rates, and global oil prices. Meanwhile, no downside risk was identified.

Table 8
BSP Baseline and Risk-Adjusted Projections
in percent

		February 2024 *MPR*	May 2024 *MPR*
Baseline inflation forecast	**2024**	3.6	3.5
	2025	3.2	3.3
Risk-adjusted inflation forecast	**2024**	3.9	3.8
	2025	3.5	3.7

Nonetheless, the estimated impact of risk is higher for both 2024 and 2025 compared with the estimates made in February 2024, driven by upward adjustments in the impact of higher domestic food prices, higher transport charges, and global oil prices, removal of the measures to mitigate *El Niño* and implementation of higher toll rates. These are partly offset by the lower impact of higher electricity rates.

Table 9
Risk Matrix[10] [11]

Upside Risks	Probability
Higher transport charges	Medium
Higher domestic food prices	Medium
Higher electricity rates	High
Higher global oil prices	Medium

Higher fares for jeepneys, trains, and taxis, as well as higher toll rates, pose upside risks to inflation. On 8 October 2023, the Land Transportation Franchising and Regulatory Board (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 likewise be approved. Moreover, the Alliance of Transport Operators and Drivers Association of the Philippines (ALTODAP) filed a petition to increase the minimum fare for traditional jeepneys to ₱15.00. The scenario assumes implementation by Q2 2024 with medium probability, given the recent uptrend in oil prices.

A petition was likewise filed by the MRT-3 management with the Department of Transportation (DOTr) in December 2023 to raise the minimum fare of the rail line from ₱13.00 to ₱16.00. The alternative scenario reflects a high probability of this risk with implementation by Q2 2024.

Similarly, taxi operators filed a petition with the LTFRB in June 2021 to raise the flag-down rate to ₱70.00 should the price of gasoline reach ₱66.00 to ₱70.00. In October 2022, a provisional ₱5.00 increase was granted. The alternative scenario assumes a further increase in the flag-down rate to ₱70.00 by Q2 2024, given the recent uptrend in oil prices. A low probability is assigned to this risk.

Meanwhile, in June 2023, toll rate adjustments for the North Luzon Expressway (NLEX), Subic-Clark-Tarlac Expressway (SCTEX), and sections of the South Luzon

[10] 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.
[11] The measures to mitigate the impact of *El Niño*, identified as a downside risk in the previous round, has been removed from the matrix following the weakening of *El Niño* weather conditions based on latest climate outlook from PAGASA. Meanwhile, the impact of *El Niño* conditions on domestic food supply has been incorporated in the higher domestic food prices.

Expressway (SLEX) were approved for staggered implementation. The scenario assumes that the second tranche of the toll adjustments in the said expressways will be implemented in Q2 2024, while the third tranche of the adjustment in SCTEX will be implemented in Q1 2025. As said toll adjustments have been approved by the Toll Regulatory Board, a high probability is assigned to this.

An overall medium probability is assigned to the risk of higher transport charges based on the CPI weights of the various transport items considered.

Ongoing supply constraints on key food commodities could cause an uptick in inflation. Below-normal rainfall conditions could affect local rice and corn production, while African Swine Fever (ASF) and Avian Flu continue to threaten the production of pork and poultry. Meanwhile. reduced fishing activities from rising fuel costs, as well as restrictive imports, could result in insufficient fish supply. Moreover, the deficit in sugar and onion supplies are expected in the absence of sufficient import programs.

Under this risk scenario, elevated prices are assumed to persist until Q3 2024 for rice and until Q4 2024 for the rest of the commodities identified. An overall medium probability is assigned to this risk, given the relative weights of the commodities in the CPI basket.

Electricity rates could increase in 2024. In July 2023, the Supreme Court nullified the Energy Regulatory Commission's (ERC) 2014 decision to cap Wholesale Electricity Market (WESM) prices from 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 ₱15.77 billion worth of power generation cost will be passed on to consumers with the adjustment spread equally over the next three years starting in June 2024.

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.

The escalation of geopolitical conflict could lead to higher global crude oil prices. The conflict in the Middle East intensifies with the recent exchange of missile strikes between Israel and Iran and continuing attacks in the Red Sea by Houthi Rebels. Meanwhile, the Russia-Ukraine war continues with Ukrainian drones targeted at Russia's oil refineries.

The risk scenario assumes Dubai crude oil prices to average at US$94/bbl from May to December 2024. This is based on the World Bank's Commodity Markets Outlook for April 2024, which assumes a moderate conflict-driven disruption estimated to reduce oil supply by about one million barrels per day.

A medium probability is assigned to this scenario with the increase in regional tensions.

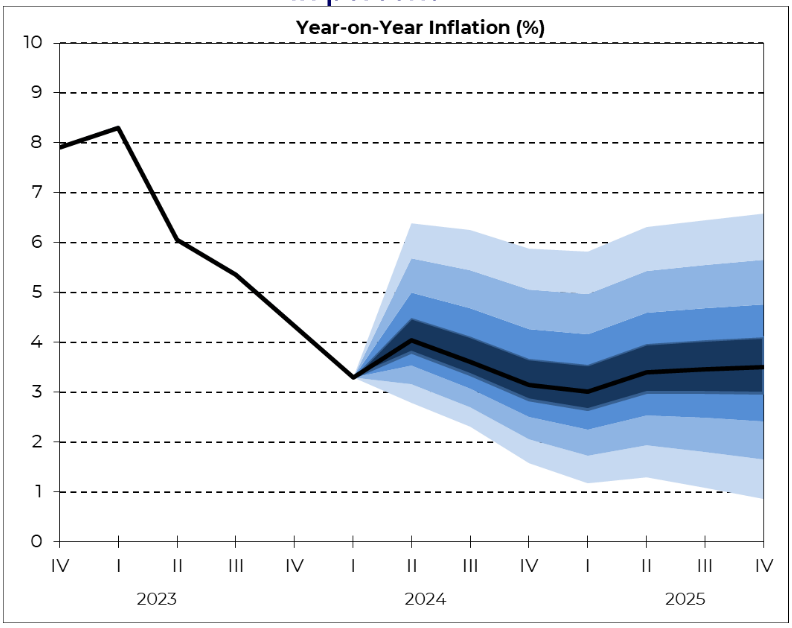
The risks to the inflation outlook continue to be skewed to the upside over the policy horizon. The probability of inflation breaching the high end of the target band in 2024 and 2025 remains high, reflecting the possible impact of the various upside risks on the outlook. Nevertheless, the latest probability distribution shows a slightly higher likelihood of inflation settling within the target range for 2024 compared with the previous round due to the downward adjustment in the baseline forecast. Meanwhile, the probability of inflation breaching the low end of the target range for 2024 and 2025 remains low.

Table 10
Probability Distribution of Inflation Forecasts
in percent

	Pr(<2%)		Pr(2-4%)		Pr(>4%)	
	Feb 2024 MPR	**May 2024 MPR**	**Feb 2024 MPR**	**May 2024 MPR**	**Feb 2024 MPR**	**May 2024 MPR**
2024	4.0	5.0	44.6	46.8	51.4	48.2
2025	13.2	10.5	49.7	48.0	37.1	41.5

Source: BSP estimates

Figure 1
Inflation Projection
in percent



Source: BSP estimateS

Table 11
Inflation Projection Ranges at Various Confidence Intervals Using the Fan Chart
in percent

Confidence Interval (%)	**Projection Range (%)**	
	2024	**2025**
80	2.7 – 5.0	1.6 – 5.6
90	2.5 – 5.5	1.1 – 6.3

Source: BSP estimates

Box Article No. 1
Monetary Policy Developments

On 8 April 2024, the BSP retained the target RRP rate at 6.50 percent. Accordingly, the interest rates on the overnight deposit and lending facilities also remained at 6.0 percent and 7.0 percent, respectively.

Relative to what was reported in the February 2024 MPR, the baseline inflation path was higher for 2024 but unchanged for 2025. The upward adjustment in the forecast path for 2024 was driven mainly by the uptick in global crude oil prices, higher-than-expected inflation outturns in February and March 2024, and the depreciation of the peso.

		February 2024 MPR[a]	April 2024 Monetary Policy Meeting[b]
Baseline inflation forecast	**2024**	3.6	3.8
	2025	3.2	3.2
Risk-adjusted inflation forecast	**2024**	3.9	4.0
	2025	3.5	3.5

Source: BSP estimates
[a] Baseline forecasts from the 14 February 2024 monetary policy meeting
[b] Baseline forecasts from the 8 April 2024 monetary policy meeting

Meanwhile, the risk-adjusted inflation forecast increased slightly for 2024 but was unchanged for 2025 due to revisions in the baseline forecasts, as the estimated impact of risks was broadly unchanged.

The balance of risks to the inflation outlook was skewed to the upside, with risks emanating from the implementation of higher transport charges, increased electricity rates, higher global oil prices, higher prices of food commodities facing supply constraints, and implementation of a legislated increase in the minimum wage.

The BSP noted that while upside risks to inflation raised inflation expectations, these expectations remained broadly anchored. Meanwhile, the latest demand indicators available at the time suggested that domestic growth prospects were largely intact over the medium term, even as overall activity continued to gradually respond to tighter financial conditions.

Given these considerations, the BSP deemed it appropriate to maintain tight monetary policy settings. The BSP also expressed support for the National Government's policies and programs to address supply-side pressures on the prices of key food commodities.

Finally, the BSP conveyed that it remained ready to adjust its monetary policy settings as necessary, in keeping with the primary mandate to safeguard price stability.