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INFLATION REPORT

Q1 2020

BANGKO SENTRAL NG PILIPINAS

Foreword

The primary objective of monetary policy is to promote a low and stable rate of inflation conducive to a balanced and sustainable economic growth. The adoption in January 2002 of the inflation targeting framework for monetary policy was aimed at helping to fulfill this objective.

One of the key features of inflation targeting is greater transparency, which means greater disclosure and communication by the BSP of its policy actions and decisions. This Inflation Report is published by the BSP as part of its transparency mechanisms under inflation targeting. The objectives of this Inflation Report are: (i) to identify the risks to price stability and discuss their implications for monetary policy; and (ii) to document the economic analysis behind the formulation of monetary policy and convey to the public the overall thinking behind the BSP's decisions on monetary policy. The broad aim is to make monetary policy easier for the public to understand and enable them to better monitor the BSP's commitment to the inflation target, thereby helping both in anchoring inflation expectations and encouraging informed debate on monetary policy issues.

The government's target for annual headline inflation under the inflation targeting framework has been set at 3.0 percent ± 1.0 percentage point (ppt) for 2020-2022 by the Development Budget Coordination Committee. This is consistent with the desired disinflation path over the medium term, favorable trends in inflation dynamics, and expected higher capacity of the economy for growth under a low inflation environment.

The report is published on a quarterly basis, presenting an analysis of the various factors affecting inflation. These include recent price and cost developments, inflation expectations, prospects for aggregate demand and output, labor market conditions, monetary and financial market conditions, fiscal developments, and the international environment. An entire section is devoted to a discussion of monetary policy developments in the most recent quarter, while a separate section provides a comprehensive analysis of the BSP's view of the inflation outlook for the policy horizon.

The Monetary Board approved this Inflation Report at its meeting on 16 April 2020.

BENJAMIN E. DIOKNO
Governor

The Monetary Policy of the Bangko Sentral ng Pilipinas

The BSP Mandate

The BSP's main responsibility is to formulate and implement policy in the areas of money, banking and credit, with the primary objective of maintaining stable prices conducive to a balanced and sustainable economic growth in the Philippines. The BSP also aims to promote and preserve monetary stability and the convertibility of the national currency.

Monetary Policy Instruments

The BSP's primary monetary policy instrument is its overnight reverse repurchase (RRP) or borrowing rate. Other instruments to implement the desired monetary policy stance to achieve the inflation target include (a) increasing/decreasing the reserve requirement (RR); (b) conducting auctions for the term deposit facility (TDF);[1] (c) adjusting the rediscount rate on loans extended to banking institutions on a short-term basis against eligible collateral of banks' borrowers; and (d) outright sales/purchases of the BSP's holdings of government securities.

Policy Target

The BSP's target for monetary policy uses the Consumer Price Index (CPI) or headline inflation rate, which is compiled and released to the public by the Philippine Statistics Authority (PSA). The policy target is set by the Development Budget Coordination Committee (DBCC)[2] in consultation with the BSP. The inflation target for 2020-2022 is 3.0 percent ± 1.0 ppt.[3]

BSP's Explanation Clauses

These are the predefined set of acceptable circumstances under which an inflation-targeting central bank may fail to achieve its inflation target. These clauses reflect the fact that there are limits to the effectiveness of monetary policy and that deviations from the inflation target may sometimes occur because of factors beyond the control of the central bank. Under the inflation targeting framework of the BSP, these exemptions include inflation pressures arising from: (a) volatility in the prices of agricultural products; (b) natural calamities or events that affect a major part of the economy; (c) volatility in the prices of oil products; and (d) significant government policy changes that directly affect prices such as changes in the tax structure, incentives, and subsidies.

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[1] The TDF was introduced under the interest rate corridor system which was implemented on 3 June 2016.

[2] The DBCC, created under Executive Order No. 232 dated 14 May 1970, is an inter-agency committee tasked primarily to formulate the National Government's fiscal program. It is composed of the Office of the President (OP), Department of Budget and Management (DBM), National Economic and Development Authority (NEDA), and the Department of Finance (DOF). The BSP attends the Committee meetings as a resource agency.

[3] In a joint statement with the DBM on 11 December 2019, the DBCC decided to keep the inflation target at 3.0 percent ± 1.0 percentage point for 2020 – 2022.

The Monetary Board

The powers and functions of the BSP, such as the conduct of monetary policy and the supervision over the banking system, are exercised by its Monetary Board (MB), which has seven members appointed by the President of the Philippines. The Monetary Board holds eight (8) monetary policy meetings in a year to review and decide on the stance of monetary policy.

Chairman & Governor
Benjamin E. Diokno

Members
Carlos G. Dominguez III
Felipe M. Medalla
Juan D. De Zuñiga, Jr.
Peter B. Favila
Antonio S. Abacan, Jr.
V. Bruce J. Tolentino

The Advisory Committee

The Advisory Committee was established as an integral part of the institutional setting for inflation targeting. It is tasked to deliberate, discuss, and make recommendations on monetary policy to the Monetary Board. Like the Monetary Board, the Committee meets eight times a year but may also meet between regular meetings, whenever deemed necessary.

Chairman
Benjamin E. Diokno
Governor

Members
Francisco G. Dakila, Jr.
Deputy Governor
Monetary and Economics Sector

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Deputy Governor
Corporate Services Sector

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Financial Supervision Sector

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Financial Market Operations Sub-Sector

Johnny Noe E. Ravalo
Assistant Governor
Office of Systemic Risk Management

Iluminada T. Sicat
Assistant Governor
Monetary Policy Sub-sector

2020 SCHEDULE OF MONETARY POLICY MEETINGS, INFLATION REPORT PRESS CONFERENCE AND PUBLICATION OF MB HIGHLIGHTS

2020	Advisory Committee (AC) Meeting	Monetary Board (MB) Meeting	MB Highlights Publication	Inflation Report (IR) Press Conference
Jan	31 (Fri) (AC Meeting No. 1)		9 (Thu) (12 Dec 2019 MB meeting)	24 (Fri) (Q4 2019 IR)
Feb		6 (Thu) (MB Meeting No. 1)		
Mar	13 (Fri) (AC Meeting No. 2)	19 (Thu) (MB Meeting No. 2)	5 (Thu) (6 Feb 2020 MB meeting)	
Apr			16 (Thu) (19 Mar 2020 MB meeting)	24 (Fri) (Q1 2020 IR)
May	15 (Fri) (AC Meeting No. 3)	21 (Thu) (MB Meeting No. 3)		
Jun	19 (Fri) (AC Meeting No. 4)	25 (Thu) (MB Meeting No. 4)	18 (Thu) (21 May 2020 MB meeting)	
Jul			23 (Thu) (25 Jun 2020 MB meeting)	24 (Fri) (Q2 2020 IR)
Aug	14 (Fri) (AC Meeting No. 5)	20 (Thu) (MB Meeting No. 5)		
Sep	25 (Fri) (AC Meeting No. 6)		17 (Thu) (20 Aug 2020 MB meeting)	
Oct		1 (Thu) (MB Meeting No. 6)	29 (Thu) (1 Oct 2020 MB meeting)	30 (Fri) (Q3 2020 IR)
Nov	13 (Fri) (AC Meeting No. 7)	19 (Thu) (MB Meeting No. 7)		
Dec	11 (Fri) (AC Meeting No. 8)	17 (Thu) (MB Meeting No. 8)	17 (Thu) (19 Nov 2020 MB meeting)	

List of Acronyms, Abbreviations, and Symbols

ASF	African Swine Fever
AHFF	Agriculture, Hunting, Forestry and Fishing
AONCR	Areas Outside the National Capital Region
ASEAN	Association of Southeast Asian Nations
BAP	Bankers Association of the Philippines
BES	Business Expectations Survey
BI	Bank Indonesia
BIR	Bureau of Internal Revenue
BIS	Bank for International Settlements
BNM	Bank Negara Malaysia
BOC	Bureau of Customs
BOT	Bank of Thailand
bp	Basis Point
BPO	Business Process Outsourcing
BTr	Bureau of the Treasury
CALABARZON	Cavite, Laguna, Batangas, Rizal and Quezon
CAMPI	Chamber of Automotive Manufacturers of the Philippines, Inc.
CAR	Capital Adequacy Ratio
CBD	Central Business District
CDS	Credit Default Swap
CES	Consumer Expectations Survey
CI	Confidence Index
CPI	Consumer Price Index
DA	Department of Agriculture
DBCC	Development Budget Coordination Committee
DBM	Department of Budget and Management
DI	Diffusion Index
DOE	Department of Energy
DOF	Department of Finance
DPWH	Department of Public Works and Highways
EIA	Energy Information Administration
EMBIG	Emerging Market Bond Index Global
ERC	Energy Regulatory Commission
FCD	Foreign Currency Deposit
FDI	Foreign Direct Investment
FOMC	Federal Open Market Committee
GDP	Gross Domestic Product
GIR	Gross International Reserve
GNI	Gross National Income
GNPL	Gross Non-Performing Loan
GOUR	Generation Over/Under Recovery
GS	Government Securities
IMF	International Monetary Fund
IMTS	International Merchandise Trade Statistics
IPP	Independent Power Producers
kWh	Kilowatt Hour
LEM	Loans Especially Mentioned
LFS	Labor Force Survey
LGU	Local Government Unit
LRT	Light Railway Transit
LSOUR	Lifeline Subsidy Over/Under Recovery
MB	Monetary Board
mb/d	Million Barrels per Day
MERALCO	Manila Electric Company
MISSI	Monthly Integrated Survey of Selected Industries
MTP	Major Trading Partner
MUP	Military and Uniformed Personnel
NBQBs	Non-Banks with Quasi-Banking Function
NCR	National Capital Region
NEDA	National Economic and Development Authority
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NG	National Government
NGCP	National Grid Corporation of the Philippines
NIA	National Income Accounts
NNPL	Net Non-Performing Loans
NPC	National Power Corporation
NSFR	Net Stable Funding Ratio
NSS	Net Settlement Surplus
ODF	Overnight Deposit Facility
OFW	Overseas Filipino Worker
OP	Office of the President
OPEC	Organization of the Petroleum Exporting Countries
OPR	Overnight Policy Rate
PBOC	People's Bank of China
PISM	Philippine Institute for Supply Management
PMI	Purchasing Managers' Index
ppt	Percentage Point
PSA	Philippine Statistics Authority; Power Supply Agreement
PSALM	Power Sector Assets and Liabilities Management
PSEi	Philippine Stock Exchange Index
QBs	Quasi-Banks
q-o-q	Quarter-on-Quarter
RBs	Rural Banks
REER	Real Effective Exchange Rate
RP	Repurchase
RR	Reserve Requirement
RREL	Residential Real Estate Loan
RREPI	Residential Real Estate Price Index
RRP	Reverse Repurchase
RRR	Reserve Requirement Ratio
SBL	Substandard or Below Loan
SDA	Special Deposit Account
SEC	Securities and Exchange Commission
SLOS	Senior Bank Loan Officers' Survey
SLOUR	System Loss Over/Under Recovery
SME	Small and Medium Enterprise
SRR	Statutory Reserve Requirement
TAFPPC	True-up Adjustments of Fuel and Purchased Power Cost
TAFxA	True-up Adjustments of Foreign Exchange Related Costs
TBs	Thrift Banks
TDF	Term Deposit Facility
TLP	Total Loan Portfolio
TOUR	Transmission Over/Under Recovery
TPI	Trading Partner Index
TPI-A	Trading Partner Index in Advanced Countries
TPI-D	Trading Partner Index in Developing Countries
U/KBs	Universal and Commercial Banks
VaPI	Value of Production Index
VoPI	Volume of Production Index
WEO	World Economic Outlook
WESM	Wholesale Electricity Spot Market
WTO	World Trade Organization
y-o-y	Year-on-Year
y-t-d	Year-to-Date

Contents

Overview

Headline inflation remains within target range in Q1 2020. Average inflation settled at 2.7 percent year-on-year (y-o-y), higher than 1.6 percent in the previous quarter but within the national government's (NG) target range of 3.0 percent ± 1.0 percentage point (ppt). The faster inflation rate during the review quarter could be traced to higher price increases of selected food and non-food items.

Headline inflation rise but remains within 2020 target range

Core inflation was also higher at 3.2 percent y-o-y in Q1 2020 from 2.7 percent in the previous quarter. Of the BSP-computed alternative core inflation measures, net of volatile items and trimmed mean inflation measures were higher in Q1 2020 compared to the previous quarter while the weighted median measure was steady at 2.6 percent. Consistent with the uptrend in overall inflation, the number of CPI items with inflation rates higher than the threshold of 4.0 percent increased to 61 items in Q1 2020 from 47 items (revised) a quarter ago. Collectively, these items accounted for about 20 percent (from 12.6 percent in the previous quarter) of the total weight in the CPI basket.

Inflation expectations for 2020 remains unchanged. The results of the BSP's survey of private sector economists in March 2020 showed that mean inflation forecast for 2020 was at 2.9 percent, unchanged from the December 2019 survey. By contrast, the mean inflation forecast for 2021 declined to 3.0 percent from 3.1 percent. For 2022, the mean inflation forecast stood at 3.0 percent. Analysts expect inflation to ease but remain within the target range. Among the downside risks to inflation outlook, the primary consideration was the subdued demand due to the coronavirus (COVID-19) pandemic. Meanwhile, upside risks to inflation are seen to emanate from supply disruptions due to lower factory output and slower global trade amid the COVID-19 outbreak.

Domestic economy sustains growth. Real gross domestic product (GDP) grew by 6.4 percent y-o-y in Q4 2019, slightly higher than the 6.0 percent and 6.3 percent in the previous quarter and year. This brought the full year 2019 GDP growth to 5.9 percent. On the demand side, growth during the review quarter was driven by higher government expenditures, at 18.7 percent, and household spending, at 5.6 percent. On the supply side, the services sector remained strong as it expanded by 7.9 percent.

Real GDP grows at a moderate pace

Higher-frequency demand indicators point to a generally positive outlook for the domestic economy. The composite Purchasing Managers' Index (PMI) as of February 2020 remained above the expansion threshold at 53, although lower than the January PMI at 55. At the same time, trends in the property sector continue to indicate healthy prospects and vehicle sales sustained its recovery from the year-ago contraction.

Global economic activity contracts. The JP Morgan Global All-Industry Output Index fell to its lowest level since 2009 at 39.4 in March 2020 from 46.1 in the previous month as new business, business activity, and new export business contracted during the month. The US economy saw the weakest downturn among large developed economies. Japan, the euro area, and the UK also recorded steep declines in economic activity. The abrupt deterioration in global economic prospects, due primarily to containment measures implemented in response to the COVID-19 pandemic, led many central banks to ease their monetary policy settings in Q1 2020. A number of these central banks, namely the US Federal Reserve, Bank of England, Bank of Korea, Reserve Bank of Australia, Bank of Thailand and Bank of Canada pursued off-cycle policy rate cuts as well as additional monetary stimulus to provide support to their respective economies.

The domestic financial system saw increased volatility. The Philippine Stock Exchange index (PSEi) averaged 6,876.72 index points, 12.4 percent lower than the average in the previous quarter. Investor sentiment was weighed down by concerns over the economic impact of Taal Volcano's eruption, the spread of COVID-19 within and outside the country, and the imposition of the enhanced community quarantine (ECQ) to contain the virus outbreak. Nevertheless, continued inflows such as from remittances and BPO receipts provided cushion to the peso which appreciated by 0.39 percent from the previous quarter, averaging at ₱50.83/US$1 in Q1 2020. Moreover, the peso volatility during the review quarter was lower than most currencies in the region. In the government securities market, average interest rates for the 91-, 182- and 364-day Treasury bills in the primary market rose to 3.161 percent, 3.459 percent, and 3.793 percent in Q1 2020. The country's debt spreads likewise widened along with its international peers as the global financial system faced negative shocks from the impact of the global pandemic. Nevertheless, the country's banking system remained sound and stable. Asset and deposits continued to grow and capital adequacy ratios remain above the BSP's and Bank for International Settlements' prescribed levels.

The BSP reduced the policy rate by 75 bps in Q1 2020. The BSP lowered the key policy interest rate by 25 basis points (bps) to 3.75 percent in the 6-February monetary policy meeting. Furthermore, the BSP reduced the policy rate by another 50 bps in its 19-March policy meeting. In deciding to reduce the policy rate anew, the BSP noted that baseline forecasts indicate a lower path of inflation for 2020 and 2021, with inflation expectations remaining firmly anchored within the target range of 3.0 percent ± 1 percentage point over the policy horizon. The latest inflation forecasts are substantially below the February-meeting projections of 3.0 percent for 2020 and 2.9 percent for 2021 due to lower-than-projected inflation outturns, a sharp decline in global crude oil prices, and the adverse effects of the COVID-19 outbreak on global and domestic economic activity.

The balance of risks to the inflation outlook leans toward the downside for both 2020 and 2021. The uncertainty over the potentially protracted pandemic poses significant downside risks to aggregate demand. The BSP noted that while the enforcement of quarantine measures could help in slowing the spread of the virus, the resulting disruptions to industries and private spending are likely to reduce economic growth in the near term. Moreover, COVID-19 has likewise dampened prospects for the global economy, which could negatively impact tourism and trade, overseas Filipino remittances, and foreign investments.

Given these considerations, the BSP decided that there was a need for a follow-on monetary policy response to address the adverse spillovers associated with the ongoing pandemic. With a manageable inflation environment and stable inflation expectations, the BSP saw enough policy space for an assertive reduction in the policy rate at this juncture to cushion the country's growth momentum and uplift market confidence amid stronger headwinds.

The BSP also issued several time-bound monetary measures and regulatory forbearance. In addition, the BSP announced on 24 March the reduction in the reserve requirement (RR) for BSP-supervised financial institutions. The RR cut will ensure sufficient domestic liquidity in support of economic activity amidst the global pandemic due to the COVID-19 and remains in line with the BSP's broad financial sector reform agenda.

Going forward, the BSP emphasized that it will remain data driven as it considers a range of other supplementary measures that may be required to support non-inflationary and sustainable growth over the medium term. The BSP is prepared to use its full range of monetary instruments and deploy regulatory relief measures as needed in fulfillment of its price and financial stability mandates.

I. Inflation and Real Sector Developments

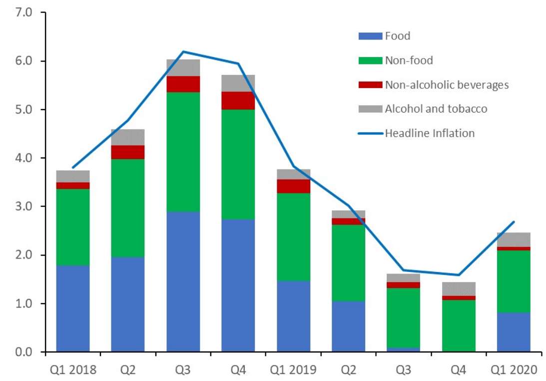
Prices

Headline inflation. Average inflation for Q1 2020 settled at 2.7 percent year-on-year (y-o-y), higher than 1.6 percent in the previous quarter but lower than 3.8 percent in the same period in 2019.

Q1 2020 headline inflation remains within target

Nonetheless, the Q1 2020 outturn was within the national government's (NG) inflation target of 2-4 percent for the year. The higher inflation rate in Q1 2020 could be traced to higher price increases of selected food and non-food items.

Chart 1. Quarterly Headline Inflation (2012=100)
In percent



Source: PSA and BSP estimates

Core Inflation. Core inflation— which excludes selected volatile food and energy items to measure underlying price pressures—also went up to 3.2 percent y-o-y in Q1 2020 from 2.7 percent in the previous quarter.

Official core inflation is higher

Similarly, preliminary estimates showed that two of the BSP-computed alternative core inflation measures (net of volatile items and trimmed mean inflation) also increased in Q1 2020 relative to the previous quarter. Meanwhile, the weighted median inflation was steady at 2.6 percent in Q1 2020 relative to the previous quarter's level.

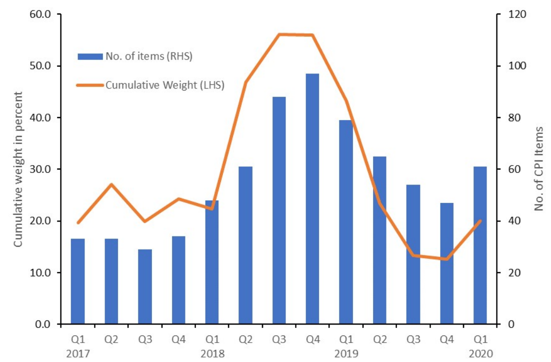
Table 1. Alternative Core Inflation Measures
Quarterly averages of year-on-year change

Quarter	Official Headline Inflation	Official Core Inflation	Trimmed Mean[1]	Weighted Median[2]	Net of Volatile Items[3]
2019					
Q1	3.8	3.9	3.8	3.4	3.7
Q2	3.0	3.4	2.9	3.0	3.0
Q3	1.7	2.9	1.9	2.8	3.3
Q4	1.6	2.7	1.7	2.6	3.3
2020					
Q1	2.7	3.2	2.2	2.6	3.8

[1] The trimmed mean represents the average inflation rate of the (weighted) middle 70 percent in a lowest-to-highest ranking of year-on-year inflation rates for all CPI components.
[2] The weighted median represents the middle inflation rate (corresponding to a cumulative CPI weight of 50 percent) in a lowest-to-highest ranking of year-on-year inflation rates.
[3] The net of volatile items method excludes the following items: bread and cereals, vegetables, sugar, jam, honey, chocolate, and confectionery, electricity, gas, fuel and lubricants for personal transport equipment, and passenger transport by road, which represents 29.5 percent of all items.
Source: PSA and BSP estimates

The number of CPI items with inflation rates higher than the threshold of 4.0 percent increased to 61 items in Q1 2020 from 47 items (revised) in the previous quarter.

Chart 2. CPI Items with Inflation Rates Above Threshold (2012=100)



Source: BSP

Collectively, these items accounted for about 20 percent (from 12.6 percent in the previous quarter) of the total weight in the CPI basket.

Food Inflation. Food inflation increased as prices of prime commodities such as fish went up due partly to the fishing ban imposed in certain provinces. Likewise, inflation for fruits and vegetables were also higher during the review quarter owing to weather-related supply disruptions.

Food inflation increases in Q1 2020

Year-on-year inflation for rice, corn, as well as sugar and other sweetened items continued to decline in Q1 2020 albeit less negatively compared to the previous quarter. Despite the ongoing optional cropping season, rice prices were relatively stable during the quarter given sufficient supply.

Meanwhile, inflation for tobacco remained elevated in Q1 2020, posting double-digit rates following the implementation of the higher excise tax on tobacco products.

Table 2. Inflation Rates for Selected Food Items
Quarterly averages in percent (2012=100)

Commodity	2019		2020
	Q1	Q4	Q1
Food and Non-Alcoholic Beverages	**4.6**	**0.3**	**2.3**
Food	4.1	**0.0**	2.3
Bread and Cereals	3.0	-5.5	-4.0
Rice	3.0	-8.3	-6.1
Corn	-0.7	-2.5	-2.2
Meat	4.4	3.1	3.0
Fish	6.8	3.6	9.3
Milk, Cheese and Eggs	2.6	3.2	3.3
Oils and Fats	4.1	0.6	1.0
Fruit	1.9	8.5	8.7
Vegetables	4.8	2.7	8.1
Sugar, Jam, Honey, Chocolate and Confectionery	7.9	-3.8	-1.7
Food Products N.E.C.	4.3	5.9	6.8
Non-Alcoholic Beverages	10.0	**3.2**	2.8
Alcoholic Beverages and Tobacco	13.0	17.5	18.4

Source of basic data: PSA and BSP

Non-food Inflation. Non-food inflation also accelerated in Q1 2020 driven largely by the turnaround in transport inflation, which picked up in Q1 2020 to 1 percent after declining for two consecutive quarters. Year-on-year inflation for operation of personal transport equipment went up while the approved fare hikes for public utility jeepneys (PUJs) minimum fare in selected provinces also exerted some upward pressure on inflation for transport services.

Non-food inflation also accelerates

The faster increase in non-food inflation during the quarter was partially tempered by rollbacks of domestic pump prices, particularly in March, due to the significant drop in global oil prices amid concerns over the adverse impact of the coronavirus (COVID-19) on global economic activity. It should be noted that quarter-on-quarter (q-o-q) transport inflation fell to -0.8 percent in Q1 2020 from 0.4 percent in Q4 2019. Meanwhile, lower power generation charges also led to reduction in electricity rates during the review quarter, which was reflected in the continued decline in the y-o-y electricity inflation.

Table 3. Inflation Rates for Selected Non-Food Items
Quarterly averages in percent (2012=100)

Commodity	2019		2020
	Q1	Q4	Q1
Non-Food	**3.0**	**1.8**	**2.1**
Clothing and Footwear	2.4	**2.7**	2.7
Housing, Water, Electricity, Gas, and Other Fuels	3.7	1.2	1.9
Furnishings, Household Equipment, and Routine Maintenance of the	3.7	2.9	3.6
Health	4.1	3.0	2.9
Transport	2.3	-0.7	1.0
Communication	0.4	0.3	0.4
Recreation and Culture	3.1	1.4	1.5
Education	-3.8	4.6	4.7
Restaurants and Miscellaneous Goods and Services	3.9	2.8	2.6

Source of basic data: PSA and BSP

Private Sector Economists' Inflation Forecasts. The results of the BSP's survey of private sector economists for March 2020 showed that mean inflation forecast for 2020 was unchanged at 2.9 percent relative to the December 2019 survey.[4]

Inflation forecast for 2020 by private sector economists remain unchanged

By contrast, the mean inflation forecast for 2021 declined to 3.0 percent from 3.1 percent. Meanwhile, the mean inflation forecast for 2022 stood at 3.0 percent based on the March 2020 survey.

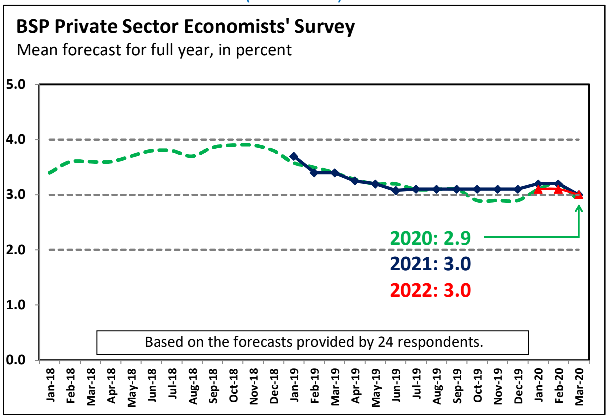
[4] There were 24 respondents in the BSP's survey of private sector economists in March 2020. The survey was conducted from 10 to 31 March 2020.

Chart 3. BSP Private Sector Economists' Survey*

Mean forecast for full year; in percent

January 2016 to February 2018 (2006=100)

March 2018 to March 2020 (2012=100)



Analysts anticipate inflation to ease but remain within the target range, with risks to the inflation outlook tilted to the downside due mainly to subdued demand amid the COVID-19 pandemic.

The key downside risks to inflation include declining global crude oil prices, strict implementation of non-monetary policy actions such as the rice tariffication law, muted global and domestic economic activity, and appreciation of the peso against the US dollar.

On the other hand, upside risks to inflation are seen to emanate from supply disruptions brought about by lower factory output and slower global trade amid the COVID-19 outbreak; strong demand for basic and essential commodities due to some panic buying; adverse weather conditions; African swine fever in some areas in the country; and lower oil production from OPEC member countries.

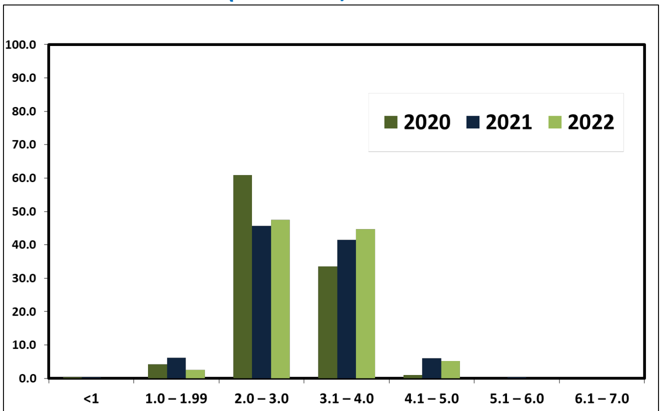
Table 4. Private Sector Forecasts for Inflation

Annual percentage change; March 2020 (2012=100)

	2020			2021	2022
	Q2	Q3	FY	FY	FY
1) Al-Amanah Islamic Bank	2.80	3.50	3.00	3.00	3.00
2) Banco De Oro	2.81	3.04	2.93	3.10	3.25
3) Bangkok Bank	2.70	2.80	2.70	3.00	3.20
4) Bank of Commerce	2.62	2.54	2.67	-	-
5) Bank of China Ltd.	2.90	3.50	3.50	3.50	3.00
6) Barclays	2.20	2.30	2.40	3.00	-
7) Citibank	2.50	2.70	2.70	2.90	3.00
8) Chinabank	2.90	2.90	2.90	3.00	3.00
9) CTBC Bank	2.70 - 3.70	3.00 - 4.00	3.00 - 4.00	3.00 - 4.00	3.00 - 4.00
10) Deutsche Bank	-	-	2.60	3.50	-
11) Eastwest Bank	2.80	3.20	3.00	3.00	3.10
12) Global Source	2.40	2.60	2.50	2.60	2.70
13) Korea Exchange Bank	3.00	2.50	2.75	2.90	3.00
14) Land Bank of the Phils	2.90	3.00	3.10	2.00	2.30
15) Maybank	3.15	2.85	2.92	3.10	3.00
16) Maybank-ATR KimEng	2.50	2.50	2.50	2.50	2.50
17) Metrobank	-	-	2.00 - 3.00	2.00 - 3.00	-
18) Mizuho	3.40	3.60	3.50	-	-
19) RCBC	2.50	2.90	2.80 - 3.00	3.00 - 3.50	3.20 - 3.70
20) Robinsons Bank	3.00	3.20	3.10	3.00	3.00
21) Philippine Equity Partners	2.81	2.99	2.91	3.20	-
22) Security Bank	3.20	2.90	3.10	2.80	3.00
23) Standard Chartered	2.60	2.90	2.90	4.00	2.50
24) Union Bank of the Phils.	3.00	3.10	3.00	3.00	3.60
Median Forecast	2.8	2.9	2.9	3.0	3.0
Mean Forecast	**2.8**	**3.0**	**2.9**	**3.0**	**3.0**
High	3.4	3.6	3.5	4.0	3.6
Low	2.2	2.3	2.4	2.0	2.3
Number of observations	22	22	24	22	18
Government Target	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**

Based on the probability distribution of the forecasts provided by 19 out of 24 respondents, there is a 94.5-percent probability that average inflation for 2020 will settle between the 2-4 percent range. For 2021 and 2022, the respondents assigned probabilities of 87.2 percent and 92.2 percent, respectively, that inflation will fall within the target band.

Chart 4. Probability Distribution for Analysts' Inflation Forecasts* (2020-2022)



*Probability distributions were averages of those provided by 19 of 24 respondents.
(Source: March 2020 BSP Survey)

Based on the Q1 2020 BSP Business Expectations Survey (BES), firms' inflationary expectations for the review quarter was higher as the number of respondents that anticipated higher inflation increased compared to the Q4 2019 survey results.

Firms and consumers expect inflation to rise but remain within the government's target range

Nevertheless, businesses expect that the rate of increase in commodity prices will remain within the government's 2 to 4 percent inflation target range for 2020 and 2021. In particular, firms generally anticipated that inflation will be at 2.9 percent for Q1 2020, 3.0 percent for Q2 2020 and 3.2 percent for the next 12 months (which was unchanged compared to the previous quarter's survey results).

The results for the Q1 2020 Consumer Expectations Survey (CES) indicated that consumers expect higher inflation over the next 12 months. Furthermore, inflation is anticipated to fall within the government's target range at an average of 2.6 percent in the next 12 months. Meanwhile, prices are expected to increase for the following items: rice (3.3 percent); bread and cereals (4.7 percent); meat (4.6 percent); fish and seafood (9.3 percent); vegetables (7 percent); milk, cheese, and eggs (7.1 percent); non-alcoholic beverages (6.3 percent); alcoholic beverages (8.9 percent); house rent (2.9 percent); water (4.3 percent); light (6.2 percent); fuel (4 percent); medical care (3 percent); transportation (6.8 percent); education (3.6 percent); and personal care (4.6 percent).

Energy prices. Average price of Dubai crude oil fell significantly by 18.3 percent in Q1 2020 relative to the previous quarter's level on expectations of weaker global demand arising from the adverse economic impact of the COVID-19 pandemic.

The International Energy Agency (IEA) cut its estimates for global oil demand by 1.1 million barrels per day (b/d) in 2020[5] while the US Energy Information Administration (EIA) also reduced its world oil and liquid fuels consumption forecast for 2020 and 2021 by 0.6 percent and 0.4 percent, respectively, in its March report compared to the previous month's assessment.[6]

At the same time, oil prices also declined due to expectations of higher supply from Saudi Arabia following the Organization of the Petroleum Exporting Countries (OPEC) and its allies' meeting in early March, which ended without an agreement of further production cuts.

Concerns for lower oil demand outlook weigh down on global oil prices in Q1 2020

Estimated futures prices of Dubai crude oil as of end-March 2020,[7] which are based on movements of Brent crude futures price, showed a lower path for 2020 – 2021 compared to end-December 2019 level.

On a cumulative basis, there was a net price decrease of domestic petroleum products as of 30 March-1 April 2020. Based on the Department of Energy (DOE) data,[8] prices of gasoline, kerosene, and diesel dropped on a net basis by ₱14.72 per liter, ₱18.20 per liter, and ₱13.39 per liter, respectively, compared to end-2019 level.

Power. The overall electricity rate in the Meralco-seviced area declined by around ₱0.43 per kilowatt hour (kWh) to ₱9.07 per kWh (from ₱9.50 per kWh in Q4 2019). The downward adjustment was attributed mainly to lower generation charge.

The decrease in generation charge was primarily due to the implementation of new Power Supply Agreements (PSAs) starting on 26 December 2019[9] as well as a reduction in capacity fees as a result of the annual reconciliation of outage allowances as approved by the Energy Regulatory Commission

[5] Source: IEA Oil Market Report - March 2020. https://www.iea.org/reports/oil-market-report-march-2020

[6] Based on the US EIA Short-Term Energy Outlook (March 2020). STEO Current/Previous Forecast Comparisons: International Crude Oil and Liquid Fuels

[6] Based on the US EIA Short-Term Energy Outlook (March 2020). STEO Current/Previous Forecast Comparisons: International Crude Oil and Liquid Fuels

[7] Future prices using Brent crude futures data. Taken as of 31 March 2020. Sources: Bloomberg L.P. and BSP-staff calculations.

[8] Based on actual prevailing common prices of domestic petroleum products for Metro Manila reported by the Department of Energy. Net adjustments are based on monitor report on the DOE website: https://www.doe.gov.ph/oil-monitor?q=oil-monitor

[9] The new baseload PSAs – with San Miguel Energy Corporation, South Premiere Power Corporation, and AC Energy – registered a significantly lower generation cost of ₱4.04 per kWh on average and contributed 21 percent to Meralco's supply requirements.

(ERC). At the same time, respective decreases in the generation charges from the Independent Power Producers (IPPs) on the back of improved average plant dispatch and stronger peso, as well as from Wholesale Electricity Spot Market (WESM) as a result of lower power demand and improved supply conditions in the Luzon grid contributed to the decline in generation charges during the review period.

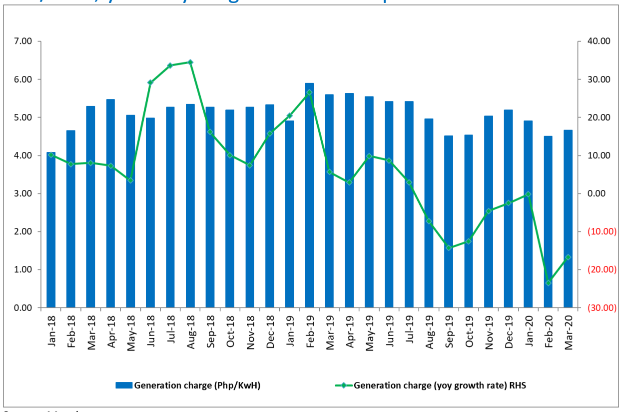
Retail electricity prices went down relative to Q4 2019

There are potential sources of upside pressures on electricity charges. Meralco has existing petitions for rate increases with ERC which include the petition to implement the Maximum Average Price for 2012, 2013, 2014, and 2015, amended application for a rate increase in the January 2014 billing (consisting of incremental fuel costs and deferred generation cost to be collected monthly for six months); and petitions for the refund of generation over/under recovery (GOUR), transmission over/under recovery (TOUR), system loss over/under recovery (SLOUR), and lifeline subsidy over/under recovery (LSOUR) for the period January-December 2011.

In addition, the Power Sector Assets and Liabilities Management (PSALM) has several pending petitions with ERC for the recovery of True-Up Adjustments of Fuel and Purchased Power Costs (TAFPPC), Foreign Exchange Related Costs (TAFxA) and Purchased Power Costs and Foreign Exchange Related Costs by the National Power Corporation (NPC), and NPC's Stranded Debt portion of the universal charge. Likewise, the National Grid Corporation of the Philippines (NGCP) also filed several petitions to recover connection charges and residual sub-transmission charges for 2011-2013 and the costs of repair on damages caused by force majeure events such as earthquake, flooding, landslides, and lightning incidents in 2011-2012.

Chart 5. Meralco's Generation Charge

PhP/kWh; yea-on-year growth rates in percent



Source: Meralco

Aggregate Demand and Supply[10]

Real gross domestic product (GDP) grew by 6.4 percent y-o-y in Q4 2019. This is higher than the revised 6.0-percent growth in Q3 2019 and the 6.3-percent expansion in Q4 2018.

Real GDP sustains growth in Q4 2019

On the demand side, growth in Q4 2019 was driven by higher government spending, at 18.7 percent from 9.6 percent in Q3 2019. Investments likewise expanded by 0.4 percent from a contraction of 2.6 percent in Q3 2019. Exports grew faster at 2.0 percent from 0.7 percent in Q3 2019 but was offset by higher goods imports, which increased by 0.3 percent in Q4 2019 from the 0.2-percent contraction in Q3 2019.

On the supply side, the services sector's performance remained strong as it expanded by 7.9 percent in Q4 2019 from 6.7 percent in Q3 2019. Similarly, the industry sector and agriculture, hunting, forestry and fishing (AHFF) sector continued to grow at 5.4 percent and 1.5 percent, respectively, although at slower rates compared to the previous quarter and year.

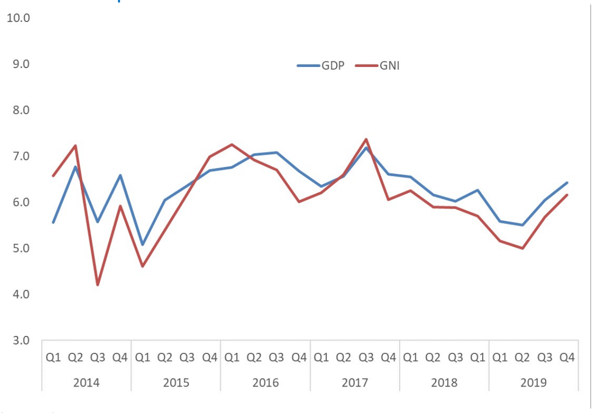
Gross national income (GNI) increased by 6.2 percent in Q4 2019, compared with the 5.7 percent growth in Q3 2019 and Q4 2018. Likewise, net primary income grew by 4.6 percent

[10] Based on revised National Income Accounts (NIA) released as of 8 August 2019.

from 3.9 percent in Q3 2019 and 2.7 percent in Q4 2018.

Chart 6. Gross Domestic Product (GDP) and Gross National Income (GNI)

At constant prices



Source: PSA

Aggregate Demand. Under the expenditure approach, household consumption, government spending, net exports, and investments (or capital formation) contributed 4.0 ppts, 1.8 ppts, 0.8 ppt, and 0.1 ppt, respectively, to total GDP growth in Q4 2019.

Household spending remains the key demand driver in Q4 2019

Household expenditures, which accounted for 71.2 percent of the country's total output in Q4 2019, expanded by 5.6 percent, still slightly slower than 5.9 percent in Q3 2019, but faster than 5.3 percent a year ago. The deceleration was attributed to the less upbeat consumer sentiment during the period on concerns over higher commodity prices, low or no increase in income, increase in household expenses, and high unemployment rate. In particular, the slower growth in private consumption was due mainly to the slowdown in housing, water, electricity, gas, and other fuels (5.3 percent from 7.7 percent) and transport due to the increase in crude oil prices, liquefied petroleum gas, and electricity rates during the reference quarter. Other household commodities that posted slower growth in Q4 2019 include furnishings, household equipment and routine household maintenance, miscellaneous goods and services, recreation and culture, and communication. Consumption of alcoholic beverages and tobacco dropped further in Q4 2019.

Government expenditures continued its uptrend, increasing by 18.7 percent in Q4 2019 from 9.6 percent growth in Q3 2019 and 12.6 percent growth in Q4 2018. Expenditures under personnel services increased, driven by the release of year-end bonuses for civilian employees and military and uniformed personnel (MUP), higher pension of retired MUP, payment of leave benefits and retirement gratuity and creation of positions in various agencies. Likewise, the government's maintenance and other operating expenses increased as payments for the government's free tertiary education and vocational courses and conditional cash transfers were released.

Investments in durable equipment improved marginally by 0.4 percent in Q4 2019 from the 2.6-percent contraction in Q3 2019, although slower than the 4.9-percent growth recorded in Q4 2018. The recovery in investments was driven largely by the significant increase in public construction (33.8 percent in Q4 2019 from 11.0 percent in Q3 2019), on account of the completed projects of the Department of Public Works and Highways, payment for the acquisition of right-of-way, and construction of the buildings of the Land Transportation Office and Land Transportation Franchising and Regulatory Board.

Table 5. Gross Domestic Product by Expenditure Shares

At constant 2000 prices; growth rate in percent

BY EXPENDITURE ITEM	2018	2019			
	Q4	Q1	Q2	Q3	Q4
Household Consumption	5.3	6.1	5.5	5.9	5.6
Government Expenditure	12.6	7.4	7.3	9.6	18.7
Capital Formation	4.9	8.0	-8.5	-2.6	0.4
Fixed Capital	8.5	6.4	-4.6	1.9	2.4
Exports	14.4	5.7	4.8	0.7	2.0
Imports	12.4	8.6	-0.1	-0.2	0.3

Source: PSA

Overall exports grew by 2.0 percent in Q4 2019 from 0.7 percent in Q3 2019 but slower than the 14.4 percent posted in Q4 2018. The growth was attributed to the recovery in merchandise exports (1.4 percent from -0.7 percent in the previous quarter), driven mainly by the uptick in exports of electronic components. Exports of semiconductors recovered after the continued downtrend in the last four quarters, mainly driven by the higher sales from the country's top three markets specifically Hong Kong, United States, and China.

Overall imports registered a marginal growth of 0.3 percent in Q4 2019 from the 0.2-percent contraction in Q3 2019. However, this is lower compared to the 12.4-percent expansion in Q4 2018. The growth in total imports can be attributed to the smaller decline in merchandise imports, on the back of higher importation of electrical machinery. Meanwhile, growth in services imports weakened slightly as transportation sustained its double-digit decline.

Other Demand Indicators. Higher-frequency demand indicators point to a generally positive outlook for the domestic economy. Preliminary composite PMI as of February remained above the expansion threshold at 53, albeit lower than the January PMI at 55. Trends in the property sector indicate healthy prospects and vehicle sales continue to recover from its year-ago contraction.

Property Prices

Capital Values. Average capital values[11] for office buildings in Metro Manila[12] in Q4 2019 rose to ₱204,990/sq.m., higher by 3.6 percent and 16.1 percent compared to the quarter- and year-ago levels, respectively.

Capital values for office and residential buildings increase

In terms of location, capital values for office buildings in Manila Bay area recorded the highest y-o-y growth at 32.9 percent in Q4 2019, albeit slower relative to the 37.1-percent expansion in the same period in 2018.

Chart 7. Capital Values
Price per square meter

[11] Probable price that the property would have fetched if sold on the date of the valuation. The valuation includes imputed land and building value.
[12] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, Alabang, and Manila Bay Area.

Likewise, average capital values for luxury residential buildings[13] in Metro Manila[14] increased to 232,078/sq.m. in Q4 2019, higher by 9.4 percent q-o-q and 25.9 percent y-o-y. In terms of location, capital values for three-bedroom luxury residential condominium units in Fort Bonifacio area recorded the highest y-o-y growth at 33.9 percent in Q4 2019, a further increase from the 17.0-percent expansion in the same period in 2018.

Rental Values.[15] Average monthly office rents in Metro Manila reached ₱1,024/sq.m. in Q4 2019, an increase by 1.9 percent from the previous quarter. This was also higher by 8.7 percent relative to Q4 2018.

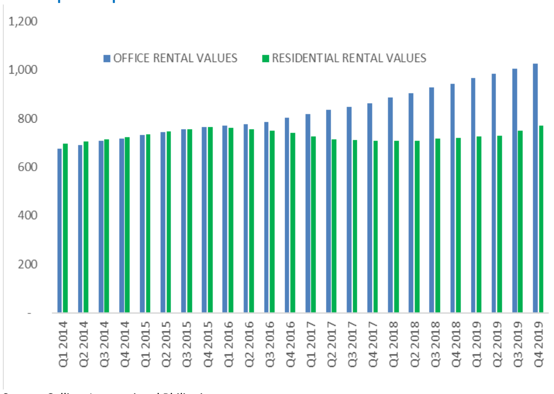
Rental values increase

The appreciation in office rental rates was due to the sustained demand from offshore gaming and traditional firms. In terms of location, rental values for office buildings in Manila Bay area recorded the highest growth at 18.7 percent y-o-y in Q4 2019 but slower than the 23.0-percent expansion in the same period in 2018.

Average monthly rents for luxury three-bedroom condominium units in the Metro Manila was recorded at ₱771/sq.m. in Q4 2019, higher by 2.8 percent compared to the previous quarter and 6.9 percent compared to year-ago levels.

[13] In terms of location, luxury residential units are located within the CBD core and have quality access to/from and have superior visibility from the main avenue. Meanwhile, in terms of general finish, luxury residential units have premium presentation and maintenance.
[14] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, and Rockwell.
[15] Actual rentals for housing account for 12.9 percent of the 2012-based CPI basket. The NSO presently surveys rentals only ranging from around ₱300-₱10,000/month to compute rent inflation. However, the rental values discussed in this section pertain to high-end rented properties, which may be considered as indicators of wealth and demand.

Chart 8. Rental Values
Price per square meter



Source: Colliers International Philippines

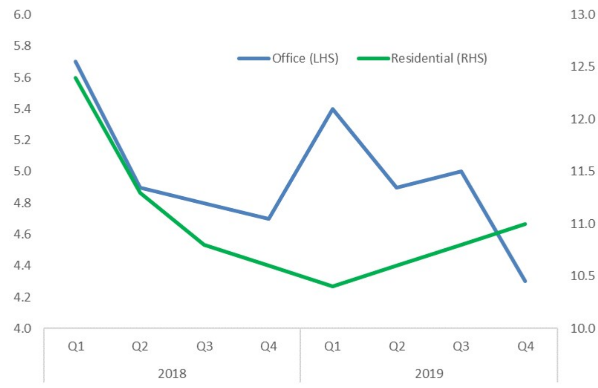
The increase in rents in Metro Manila in Q4 2019 could be attributed to the continued demand from foreign and local employees, especially in business districts. In terms of location, capital values for three-bedroom luxury residential condominium units in Makati CBD recorded the highest y-o-y growth at 10.3 percent in Q4 2019. This was faster than the 3.1-percent growth in the same period in 2018.

Vacancy Rates. The overall office vacancy rate in Metro Manila declined to 4.3 percent in Q4 2019 from 5.0 percent in the Q3 2019 due mainly to the increased take up from outsourcing and traditional firms.

Office vacancy rates decline

In terms of location, the office vacancy rates in Makati CBD (1.6 percent from 1.7 percent), Fort Bonifacio area (3.7 percent from 5.3 percent), and Manila Bay Area (0.5 percent from 0.6 percent) declined in Q4 2019 compared to the previous quarter. By contrast, office vacancy rates in Ortigas Center (5.0 percent from 4.4 percent) increased in Q4 2019 compared to the previous quarter. The overall office vacancy rate in Metro Manila is projected at 5.3 percent for 2020 due mainly to sustained take up from offshore gaming, outsourcing, and traditional tenants. Colliers International Philippines sees expansion in all segments, notably the offshore gaming and traditional sectors, which would contribute to a further diversification of the Metro Manila office demand base. However, headwinds such as the recent spread of COVID-19 as well as the lack of provincial supply of office space may have adverse impact on the office segment.

Chart 9. Vacancy Rates
In percent



Source: Colliers International Philippines

Meanwhile, the overall residential vacancy rate in Metro Manila increased to 11.0 percent in Q4 2019 from 10.8 percent in Q3 2019 due to the completion of additional units across Metro Manila. In particular, residential vacancy rates were higher in Makati CBD (10.9 percent from 10.8 percent), Fort Bonifacio (15.0 percent from 14.7 percent), and Rockwell Center (10.0 percent from 9.7 percent). By contrast, residential vacancy rates declined in Ortigas Center (4.4 percent from 4.5 percent), Eastwood City (4.3 percent from 4.4 percent), and Manila Bay area (12.8 percent from 13.0 percent). Colliers foresees vacancy peaking in 2020 at 11.9 percent due mainly to substantial completion of new units, especially in Manila Bay area. It added that vacancy would start declining in 2021 from the completion of new units.

BSP Residential Real Estate Price Index (RREPI).[16] Residential real estate prices of various types of housing units nationwide rose by 10.2 percent y-o-y in Q4 2019 based on the RREPI. While this is the second consecutive quarter that the index has registered a double-digit growth, this was slightly lower than the 10.4-percent growth in Q3 2019, but higher than the 0.6 percent in Q4 2018.

[16] The RREPI measures the average changes in prices of different types of housing units over a period of time across different geographical regions where the growth rate of the index measures house inflation. It is computed as a weighted chain-linked index based on the average appraised value per square meter weighted by the share of floor area of new housing units. The RREPI was computed based on data from housing loans granted by universal, commercial, and thrift banks.

Residential real estate prices increase

By area, residential property prices increase y-o-y in both the National Capital Region (NCR) and in Areas Outside NCR (AONCR). Residential prices in NCR increased by 15 percent, while prices in AONCR went up by 8.2 percent relative to year-ago prices. In the NCR, price increases were observed across all types of housing units, except for townhouses, which recorded a decline. In AONCR, price growth was registered in all types of housing units.

Table 6. Residential Real Estate Price Index[1] by Housing Type

Q1 2014=100; growth rate in percent

		Overall[2]	Single Detached/ Attached House	Duplex[3]	Townhouse	Condominium Unit
2017	Q1	**113.9**	108.0	91.2	107.6	128.3
	Q2	**111.8**	103.6	103.6	112.7	129.3
	Q3	**111.6**	103.4	88.4	107.7	131.0
	Q4	**117.4**	104.6	102.6	116.3	143.3
2018	Q1	**116.2**	107.3	131.5	122.4	130.9
	Q2	**117.0**	105.1	99.0	128.4	138.5
	Q3	**116.6**	103.6	115.5	127.7	138.6
	Q4	**118.1**	102.6	98.8	129.9	144.2
2019	Q1	**120.0**	105.7	121.0	134.4	145.2
	Q2	**117.5**	100.7	111.4	133.9	151.8
	Q3	**128.7**	106.1	144.2	135.4	178.9
	Q4	**130.2**	108.5	148.6	143.0	171.5
Year-on Year Growth Rates						
2017	Q1	**6.5**	9.2	-20.5	0.3	4.1
	Q2	**0.1**	-2.1	5.1	3.2	4.4
	Q3	**1.8**	0.8	-8.6	7.2	3.6
	Q4	**5.7**	-0.3	17.3	8.0	14.2
2018	Q1	**2.0**	-0.6	44.2	13.8	2.0
	Q2	**4.7**	1.4	-4.4	13.9	7.1
	Q3	**4.5**	0.2	30.7	18.6	5.8
	Q4	**0.6**	-1.9	-3.7	11.7	0.6
2019	Q1	**3.3**	-1.5	-8.0	9.8	10.9
	Q2	**0.4**	-4.2	12.5	4.3	9.6
	Q3	**10.4**	2.4	24.8	6.0	29.1
	Q4	**10.2**	5.8	50.4	10.1	18.9
Quarter-on-Quarter Growth Rates						
2017	Q1	**2.5**	3.0	4.2	-0.1	2.2
	Q2	**-1.8**	-4.1	13.6	4.7	0.8
	Q3	**-0.2**	-0.2	-14.7	-4.4	1.3
	Q4	**5.2**	1.2	16.1	8.0	9.4
2018	Q1	**-1.0**	2.6	28.2	5.2	-8.7
	Q2	**0.7**	-2.1	-24.7	4.9	5.8
	Q3	**-0.3**	-1.4	16.7	-0.5	0.1
	Q4	**1.3**	-1.0	-14.5	1.7	4.0
2019	Q1	**1.6**	3.0	22.5	3.5	0.7
	Q2	**-2.1**	-4.7	-7.9	-0.4	4.5
	Q3	**9.5**	5.4	29.4	1.1	17.9
	Q4	**1.2**	2.3	3.1	5.6	-4.1

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015
[2] No index generated for apartments due to very few observations
[3] Indices for duplex exhibit more volatility due to relatively small number of reported real estate loans

In Q4 2019, 73.9 percent of residential real estate loans (RRELs) were for the purchase of new housing units. Majority of residential property loans were used for the acquisition of condominium units (52.1 percent), followed by single detached/attached houses (38.8 percent) and townhouses (8.6 percent).

By area, most of the RRELs granted in NCR were for the purchase of condominium units, while RRELs granted in AONCR were for the purchase of single detached/attached houses. By region, NCR accounted for 48 percent of the total number of RRELs granted in Q4 2019, followed by CALABARZON (25.1 percent), Central Luzon (7.7 percent), Central Visayas (6.6 percent), Western Visayas (3.9 percent), Davao Region (2.9 percent) and Northern Mindanao (1.9 percent). NCR and these six other regions combined accounted for 96.1 percent of total housing loans granted by banks.

Table 7. Residential Real Estate Price Index by Area

Q1 2014=100; growth rate in percent

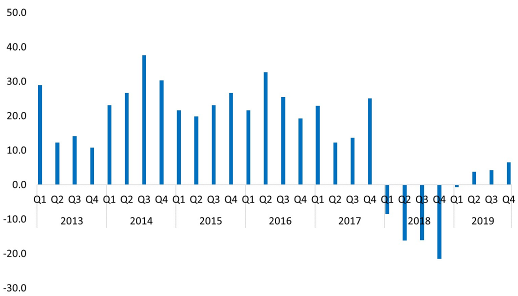
		Overall[2]	NCR	AONCR
2017	Q1	**113.9**	118.4	111.6
	Q2	**111.8**	120.4	107.5
	Q3	**111.6**	118.2	108.1
	Q4	**117.4**	127.6	111.1
2018	Q1	**116.2**	121.6	112.5
	Q2	**117.0**	125.7	112.0
	Q3	**116.6**	126.4	110.5
	Q4	**118.1**	129.8	110.2
2019	Q1	**120.0**	132.5	113.1
	Q2	**117.5**	132.2	110.8
	Q3	**128.7**	154.4	115.9
	Q4	**130.2**	149.3	119.2
Year-on Year Growth Rates				
2017	Q1	**6.5**	4.4	8.0
	Q2	**0.1**	3.7	-1.6
	Q3	**1.8**	2.2	1.8
	Q4	**5.7**	8.8	3.0
2018	Q1	**2.0**	2.7	0.8
	Q2	**4.7**	4.4	4.2
	Q3	**4.5**	6.9	2.2
	Q4	**0.6**	1.7	-0.8
2019	Q1	**3.3**	9.0	0.5
	Q2	**0.4**	5.2	-1.1
	Q3	**10.4**	22.2	4.9
	Q4	**10.2**	15.0	8.2
Quarter-on-Quarter Growth Rates				
2017	Q1	**2.5**	0.9	3.4
	Q2	**-1.8**	1.7	-3.7
	Q3	**-0.2**	-1.8	0.6
	Q4	**5.2**	8.0	2.8
2018	Q1	**-1.0**	-4.7	1.3
	Q2	**0.7**	3.4	-0.4
	Q3	**-0.3**	0.6	-1.3
	Q4	**1.3**	2.7	-0.3
2019	Q1	**1.6**	2.1	2.6
	Q2	**-2.1**	-0.2	-2.0
	Q3	**9.5**	16.8	4.6
	Q4	**1.2**	-3.3	2.8

Vehicle Sales. Sales of new vehicles from CAMPI-TMA[17] members rose by 6.5 percent y-o-y in Q4 2019, faster than the 4.2-percent expansion in Q3 2019 and a reversal of the 21.5-percent contraction recorded in Q4 2018, due mainly to higher sales of passenger and commercial vehicles during the period.

Sales of new vehicles continues to recover

Commercial vehicle sales, which account for about 71.8 percent of total vehicle sales, rose by 7.7 percent y-o-y in Q4 2019 from the 19.5-percent decline in the same period in 2018. Commercial vehicles sold during the quarter reached 73,697 units from 68,411 units in Q4 2018.

Chart 10. Vehicle Sales
Growth rate in percent



Source: CAMPI

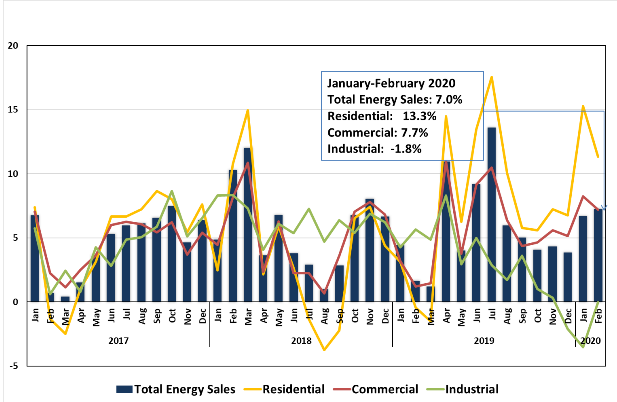
Similarly, sales of passenger cars went up by 3.4 percent y-o-y in Q4 2019, a turnaround from the 26.0-percent contraction in the same period in 2018. New passenger car sales accrued to a total of 28,880 units in Q4 2019 from 27,942 units in the same period a year ago.

Energy Sales. Energy sales of Meralco increased by 7.0 percent year-on-year in January – February 2020, faster compared to the 3.0-percent growth in the same period a year-ago.

Energy sales increase

Energy sales from the residential sector and commercial sector increased by 13.4 percent and 7.7 percent, respectively, while energy sales from the industrial sector contracted by 1.8 percent.

Chart 11. Energy Sales
Year-on-year rowth in percent



Source: Meralco, BSP calculations

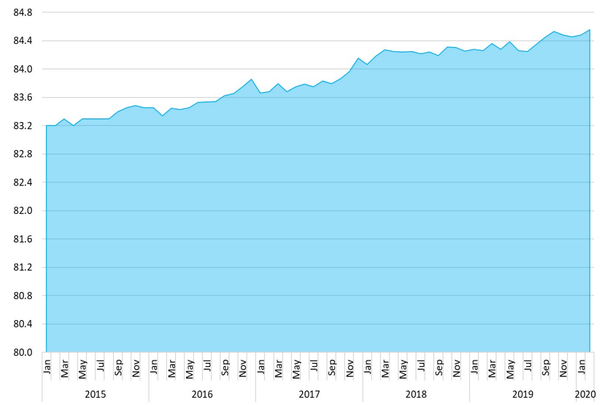
Capacity Utilization. The average capacity utilization rate of the manufacturing sector stood at 84.6 percent in February 2020, slightly higher than the month-ago level based on the Philippine Statistics Authority's Monthly Integrated Survey of Selected Industries (MISSI).

Capacity utilization in manufacturing remains above 80 percent

Of the 414 respondent-establishments, 61.1 percent operated at a capacity of at least 80.0 percent in February 2020. Data showed that most of the manufacturing companies have been operating above the 80.0-percent capacity since 2010.

[17] Vehicle sales data is gathered on a monthly basis by the Chamber of Automotive Manufacturers of the Philippines (CAMPI) and the Truck Manufacturers Association (TMA). CAMPI represents the local assemblers and manufacturers of vehicle units in the Philippine automotive industry. The following are the active members of CAMPI: (1) Asian Carmakers Corp., (2) CATS Motors, Inc., (3) Columbian Autocar Corp., (4) Honda Cars Philippines, Inc., (5) Isuzu Philippines Corp., (6) Mitsubishi Motors Philippines Corp., (7) Nissan Motor Philippines Corp., (8) Suzuki Philippines Inc., (9) Toyota Motor Philippines Corp. and (10) Universal Motors Corp.

Chart 12. Monthly Average of Capacity Utilization for Manufacturing
In percent



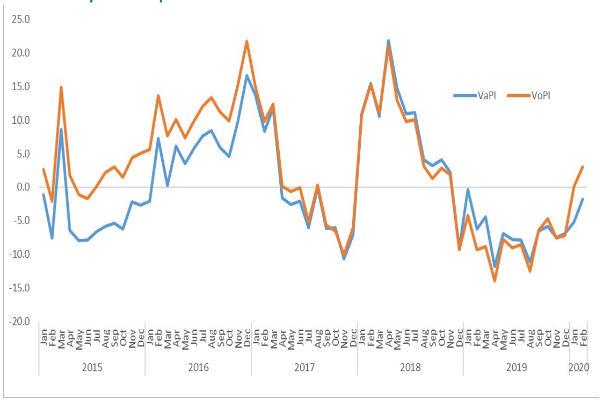
There were 12 (out of the 20) major industries in the sector that operated above the 80.0-percent capacity level that include: petroleum products (90 percent); basic metals (88.8 percent); machinery except electrical (86.7 percent); non-metallic mineral products (86.2 percent); food manufacturing (85.5 percent); chemical products (85.3 percent); electrical machinery (84.9 percent); printing (84.1 percent); paper and paper products (83.9 percent); rubber and plastic products (83.2 percent); wood and wood products (82.3 percent); and textiles (80.4 percent).

Volume and Value of Production. Preliminary results of the MISSI showed that volume of production index (VoPI) increased by 3.0 percent y-o-y in February 2020, a significant improvement from the 0.1-percent (revised) growth in the previous month. Of the 20 major industries, 10 industries posted expansion namely, machinery except electrical (28.0 percent), chemical products (23.8 percent), beverages (16.9 percent), food manufacturing (3.3 percent), printing (38.4 percent), fabricated metal products (30.3 percent), footwear and wearing apparel (3.5 percent), non-metallic mineral products (3.6 percent), rubber and plastic products (3.6 percent), and wood and wood products (11.3 percent).

Manufacturing output shows improvement

Factory output – as measured by the VoPI – grew on a y-o-y basis brought about by a surge in domestic demand for manufactured goods amid the COVID-19 outbreak. NEDA noted that firms likely to expand during the pandemic are those manufacturing food, beverages, chemical products, and health-related items. NEDA emphasized the importance of sustained production and distribution capacity to ensure domestic supply of food and essential commodities in this time of health crisis. However, NEDA also recognized the potential adverse impact of COVID-19 to the sector, as well as trade, aviation, tourism, and OFW remittances. In order to address possible risks and disruptions, the Inter-agency Task Force Technical Working Group for Anticipatory and Forward Planning chaired by NEDA has been conducting consultations with various sectors of the country to come up with measures and interventions.

Chart 13. Volume and Value Indices of Manufacturing Production
Year-on-year in percent



By contrast, the value of production index (VaPI) posted a 1.8-percent decline in February 2020 from a 5.2-percent contraction a month-ago. This was attributed to the deceleration of the following sub-sectors: petroleum products (-35.9 percent), electrical machinery (-8.9 percent), basic metals (-14.9 percent), transport equipment (-12.1 percent), tobacco products (-26.1 percent), miscellaneous manufactures (-24.4 percent), paper and paper products (-10.6 percent), textiles (-9.4 percent), footwear and wearing apparel (-4.5 percent), leather products (-26.1 percent), and furniture and fixtures (-6.4 percent).

Business Expectations. The Q1 2020 BSP Business Expectations Survey (BES) showed a weaker business outlook as the overall confidence index (CI) decreased to 22.3 percent from 40.2 percent a quarter ago. The lower index was attributed to the combined effects of lower percentage of optimists and increase in the percentage of pessimists compared to the previous quarter's survey results.

Business outlook weakens in Q1 2020

Respondents' less optimism for Q1 2020 was due to the following: the negative effects of virus outbreaks, African swine fever and the Taal volcano eruption; concerns on government policies, such as termination of Visiting Forces Agreement, non-renewal of mining rights,[18] and travel ban, among others; decrease in orders and lower volume of business activity and production; seasonal slack in demand after the holiday season; and low supply of raw materials and products.

The sentiment of businesses in the Philippines mirrored the less optimistic business outlook in Brazil, Canada, Croatia, Germany, Hungary, Israel, and the United States. Meanwhile, business confidence in Greece, India, and the Netherlands was more optimistic. However, view of businesses in Australia, Chile, China, Denmark, Euro Area, Hong Kong, Mexico, New Zealand, South Korea, and Thailand was pessimistic.

Table 8. Business Expectations Survey

BUSINESS OUTLOOK INDEX		Current Quarter	Next Quarter
2016	Q1	41.9	49.6
	Q2	48.7	45.3
	Q3	45.4	56.8
	Q4	39.8	34.5
2017	Q1	39.4	47.2
	Q2	43.0	42.7
	Q3	37.9	51.3
	Q4	43.3	39.7
2018	Q1	39.5	47.8
	Q2	39.3	40.4
	Q3	30.1	42.6
	Q4	27.2	29.4
2019	Q1	35.2	52.0
	Q2	40.5	47.6
	Q3	37.3	56.1
	Q4	40.2	40.3
2020	Q1	22.3	42.3

Source: BSP

However, for the quarter ahead (Q2 2020), business outlook was more favorable as the next quarter CI rose to 42.3 percent from 40.3 percent in the previous quarter. Respondents' more buoyant outlook for Q2 2020 was associated with expectations of the following: increase in orders or sales primarily in the community, finance, business, and trade sub-sectors; usual uptick in demand during summer, enrollment, and harvest seasons; implementation of new or enhanced business strategies; expansion of businesses; and higher government infrastructure spending.

[18] Oceana Gold's Didipio Gold and Copper Project's 25-year financial and technical assistance agreement (FTAA), which was the company's mining license with the Philippine government, has not been renewed since its expiration on June 20, 2019. However, the long delayed renewal processes of the mine's FTAA remains unresolved.

Consumer Expectations. Based on the Q1 2020 Consumer Expectations Survey (CES),[19] the country's consumer outlook remained positive for Q1 2020 even as the overall CI[20] declined marginally to 1.26 percent from 1.31 percent in Q4 2019. The lower but still positive CI reflected that the number of optimists continued to outnumber the pessimists, but by a lesser margin compared to Q4 2019.

Consumer confidence weaker but remains positive

The sustained positive sentiment for Q1 2020 was due to the following concerns: availability of more jobs; effective government policies and programs (e.g., anti-drug campaign and the Senior Citizens Act); and good governance. Nevertheless, their positive sentiment was mitigated by their concerns on the following: faster increase in the prices of goods; low income; occurrence of typhoon, volcanic eruption, and the COVID-19 outbreak; and higher household expenses.

The sentiment of consumers in the Philippines was comparable to the steady positive outlook of consumers in Poland for Q1 2020. Meanwhile consumer outlook in Australia, Czech Republic, France, Indonesia, and Italy was still optimistic, while those in Euro Area, Japan, South Korea, Switzerland, Taiwan, Thailand, United Kingdom, and the United States remained pessimistic.

For the next quarter (Q2 2020) and the next 12 months, consumers were less buoyant as the CIs declined, though remaining positive, at 9.2 percent (from 15.7 percent a quarter ago) and

[19] The CES is a quarterly survey of a random sample of around 5,500 households in the Philippines. The Q1 2020 CES was conducted during the period 29 January – 10 February 2020.

[20] The CI is computed as the percentage of households that answered in the affirmative less the percentage of households that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.

19.9 percent (from 26.4 percent in the previous quarter's survey results), respectively.

Table 9. Consumer Expectations Survey

CONSUMER OUTLOOK INDEX		Current Quarter	Next Quarter	Next 12 Months
2016	Q1	-5.7	9.1	25.4
	Q2	-6.4	5.6	26.6
	Q3	2.5	27.3	43.8
	Q4	9.2	18.8	33.4
2017	Q1	8.7	16.5	31.7
	Q2	13.1	13.6	34.3
	Q3	10.2	17.8	33.7
	Q4	9.5	17.5	32.0
2018	Q1	1.7	8.8	24.0
	Q2	3.8	8.7	23.1
	Q3	-7.1	3.8	13.0
	Q4	-22.5	-0.8	10.7
2019	Q1	-0.5	10.7	28.4
	Q2	-1.3	9.7	25.2
	Q3	4.6	15.8	29.8
	Q4	1.3	15.7	26.4
2020	Q1	1.3	9.2	19.9

Source: BSP

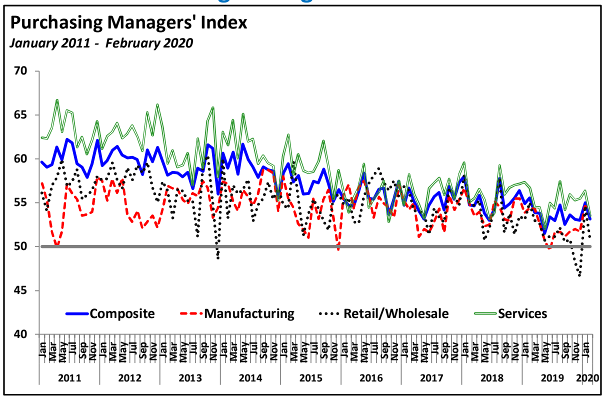
Consumers cited their anticipation of faster increase in the prices of goods; low or no increase in income; aforementioned natural calamities and virus outbreak; and higher household expenses as reasons for their less upbeat outlook for the next quarter and the next 12 months.

Purchasing Managers' Index.[21] The composite PMI in February 2020 remained above the 50-point expansion threshold[22] at 53.1. However, this is lower than the January PMI at 55. This was due to the slower expansion of all the sectors in review.

PMI remains above the 50-point expansion threshold

The manufacturing PMI decreased marginally by 0.2 index point to 54.4 in February 2020 from 54.6 in January, contrary to respondents' expectations of an acceleration for the month. Despite sustained demand in February, the sector slowed down following the seasonal high in the previous month, as well as due to production woes brought about by the African swine fever. In particular, lead time for delivery of major production inputs, as measured by the Supplier Deliveries Index, was longer due to strong demand and traffic build up. Consequently, New Orders outpaced Production, which was compensated by Inventories, while the Employment Index was broadly stable. Meanwhile, all firms by export category decelerated in February, except those with export volume of up to 25 percent of total revenues which breached the 60-point mark. On a per sector basis, six out of 12 subsectors grew at a faster pace namely, textiles (at a PMI of 58.3), paper products (52.3), fuel products (55.8), machinery (54), motor vehicles (56.9), and fabricated metal (53.9). Food and beverages, rubber and plastic, and communication and medical equipment decelerated, while the following posted a contraction: basic metals, publishing, and non-metallic minerals. Prospects are assessed to be less favorable for the manufacturing sector in March.

Chart 14. Purchasing Managers' Index



Similarly, the services PMI decreased by 2.8 index points to 53.5 from 56.4, which is contrary with business managers' expectations of an expansion in February. This may be attributed mainly to cyclical downtrend evident in the lower PMIs of all the indices, except the Outstanding Business Index. In particular, Business Activity Index and New Orders Index, which are both measures of demand activity, posted hefty declines in February. The COVID-19 outbreak also started to have an impact on the Services Sector that provides frontline services. Nonetheless, all the indices remained above the 50-point expansion threshold. On a per sector basis, three of the 14 subsectors were on faster expansion (real estate, postal and telecommunications, and business and knowledge processing). The education subsector grew steadily, six subsectors expanded at a slower pace (electricity, gas, and water; construction;

[21] Data based on the monthly purchasing managers' index report of the Philippine Institute for Supply Management (PISM).

[22] The actual formula used to calculate the PMI assigns weights to each common element and then multiplies them by 1.0 for improvement, 0.5 for no change, and 0 for deterioration. As a result, an index above 50 indicates economic expansion, and an index below 50 implies a contraction. PMI surveys are conducted on the last week of the month.

hotels and restaurants; banking and financial intermediation; provident and insurance; and recreational, cultural, and sporting activities), while four contracted (transportation including travel agency, renting of goods and equipment, miscellaneous business activities, and health and social work). Survey respondents expect the sector to further decelerate next month.

The retail and wholesale PMI also went down by 3.8 index points and posted a stable growth at 50.8 in February from 54.6 in the previous month, consistent with managers' expectations of a slowdown. This was attributed mainly to seasonal downturn, as well as due to the COVID-19 outbreak which immediately affected the frontline Retail-Wholesale Sector. Demand-related variables namely, Purchases Index and Sales Revenue Index posted the largest decline month-on-month. Inventories and Employment were also down from month-ago levels. By contrast, the Supplier Deliveries Index increased, indicative of longer delivery lead time, which may be due to factors such as traffic, truck ban, or port congestion. Meanwhile, the PMI of the retail subsector went down by 2.47 index points to 50.86 in February from 53.32 in January due to the deceleration of Purchases, Sales Revenues, and Employment, as well as the contraction of Supplier Deliveries and Inventories. The PMI of the wholesale subsector also decreased by 5.48 index points to 50.78 from 56.26 as the decline of Purchases, Sales Revenues, Supplier Deliveries, and Inventories more than offset the faster expansion of Employment. Managers are anticipating an improvement in the month ahead.

Aggregate Supply. On the production side of the economy, growth was driven largely by the services sector, which contributed 4.4 ppts. Meanwhile, the industry and AHFF sectors contributed 1.9 ppts and 0.1 ppt, respectively.

Service sector supports supply-side growth

The services sector expanded by 7.9 percent in Q4 2019, higher than the 6.7 percent in Q3 2019 and 6.8 percent in Q4 2018. The growth in the services sector was mainly driven by the stronger performance of public administration and defense (17.1 percent from 5.3 percent in Q3 2019), other services, and trade and repair of motor vehicles, motorcycles, personal and household goods, which offset the deceleration in financial intermediation, transport, storage and communication, and real estate, renting and business activities.

Trade and repair of motor vehicles, motorcycles, and personal and household goods sector expanded by 8.6 percent from 7.8 percent due to faster growth in wholesale and retail trade segments. Growth in public administration and defense accelerated on the back of higher personnel services and maintenance and other operating expenses disbursements. Growth in other services improved (7.0 percent from 4.2 percent) due to stronger performance of the health and social work, recreational, cultural, and sporting activities, hotel and restaurants, other services activities and sewage and refuse disposal sanitation and similar activities segments. Among others, the sector was boosted by higher tourists arrivals.

Chart 5. Gross Domestic Product by Industrial Origin (at constant prices)
Year-on-year growth in percent

Source: PSA

The growth of the industry sector slightly decelerated to 5.4 percent in Q4 2019 from 5.6 percent in Q3 2019 due to slower construction growth, which outweighed the gains from manufacturing, mining and quarrying, and electricity, gas, and water supply.

The manufacturing sector expanded faster (3.7 percent from 2.6 percent) due to the rapid expansion in food manufactures and chemical and chemical products. Faster output growth was also observed for miscellaneous manufactures, paper and paper products and wearing apparel. Growth in mining and quarrying was brought about by improvements in nickel mining and stone quarrying and clay and sandpits. Electricity, gas, and water supply also grew with the faster increase in electricity output.

Growth in agriculture sector slowed down by 1.5 percent in Q4 2019 from 3.1 percent in Q3 2019 and 1.8 percent growth in Q4 2018. The slower growth was mainly attributed to the decline in production of corn (-7.1 percent), livestock (-8.3 percent), and sugarcane (-15.6 percent). Poultry, other crops, mango, and pineapple also posted slower growth.

Table 10. Gross Domestic Product by Industrial Origin

At constant 2000 prices; growth rate in percent

BY INDUSTRIAL ORIGIN	2018	2019			
	Q4	Q1	Q2	Q3	Q4
AHFF	1.8	0.7	0.8	3.1	1.5
Agriculture and forestry	1.7	0.6	0.4	3.5	1.0
Fishing	2.5	1.4	3.4	1.0	3.9
Industry	6.6	4.8	3.7	5.6	5.4
Mining & Quarrying	8.1	4.7	14.6	-3.2	2.1
Manufacturing	3.2	4.9	3.9	2.6	3.7
Construction	20.0	5.4	-0.5	15.4	10.7
Electricity, Gas and Water Supply	6.7	3.1	7.8	7.2	7.3
Service	6.8	6.8	7.1	6.7	7.9
Transport, Storage & Communicatio	3.7	7.6	5.9	8.2	5.6
Trade and Repair of Motor Vehicles, Motorcycles, Personal and	6.7	7.3	8.4	7.8	8.6
Financial Intermediation	6.3	10.2	9.2	11.2	10.9
R. Estate, Renting & Business Activiti	4.1	3.7	3.8	4.1	3.3
Public Administration & Defense; Compulsory Social Security	14.7	9.7	8.6	5.3	17.1
Other Services	9.4	5.3	7.7	4.2	7.0

Source: PSA

The decline in corn production was due to the shift in planting and harvesting season in Cagayan Valley due to the early onset of rainfall. In contrast, insufficient rainfall resulted in lower yields in SOCCSKSARGEN, while lower buying price reduced areas harvested in Zamboanga Peninsula. Meanwhile, growth in the livestock sector slowed down as carabao, cattle and hog production declined. In particular, hog production dropped following the strict implementation and monitoring of movements of live animals in between provinces as local government authorities worked to prevent the spread of ASF. Sugarcane output posted negative growth for the third consecutive quarter as the dry spell in Western Visayas resulted in the reduction of areas harvested.

Labor Market Conditions

The labor market continued to make a respectable performance in Q1 2020 as major indicators for both quantity and quality of employment improved if not maintained their levels from the same period a year ago.

Labor market continues to improve in Q1 2020

Results of the January 2020 round of the labor force survey (LFS) showed that the country's employment rate was retained at 94.7 percent, unemployment rate was also maintained at 5.3 percent, underemployment rate declined to 14.8 percent (from 15.4 percent), and youth unemployment fell to 13.6 percent (from 14.2 percent). For 2020, the government set its targets for unemployment rate between 3.8 and 5.2 percent and for youth unemployment rate at 9.2 percent.[23]

The maintained level of employment rate in January 2020 is equivalent to 42.7 million employed individuals. The survey indicated an employment gain of 1.6 million or 4.0 percent higher compared to 41.0 million employed persons in the same period a year ago. However, employment gains were recorded only in services and agriculture sectors. Employment in the services sector increased by 4.0 percent to 25.0 million, mainly due to wholesale and retail trade, public administration and defense, and accommodation and food service activities. Employment in agriculture sector strongly recovered with 9.2 percent growth, which is a continuation of the improvement in agriculture employment since Q3 2019. Meanwhile, employment in industry sector contracted by 2.0 percent, mainly due to construction and manufacturing subsectors. The latter is consistent with the latest result of MISSI, which posted a 1.6-percent drop in the VOPI in January 2020. The decline in VOPI could be partly attributed to Taal volcano eruption[24] and concerns over COVID-19.[25]

For full year 2020, the government's employment generation target is 900,000 to 1.1 million. Meanwhile, the latest unemployment rate at 5.3 percent translates to 2.4 million unemployment level. This is a 4.7-percent increase or 107 thousand more unemployed individuals in Q1 2020. In terms of highest grade completed, majority of the unemployed are still college graduates (26.9 percent share) and junior high school graduates (28.7 percent). In terms of age, the bulk continues to belong to the 15-24 age group or the youth (42.4 percent), followed by 25-34 years old (32.1 percent). The number of unemployed youth slightly increased by 0.8 percent during the period.

Unemployment rate remains unchanged from the previous survey round

The quality of employment slightly improved as underemployment rate dropped to 14.8 percent from 15.4 percent a year ago. This lowest underemployment rate for all January rounds since 2006 is equivalent to a 9-thousand decline in the number of employed individuals who wanted more work compared to January 2019. However, other aspects of quality of employment did not improve during the period. This is evidenced by lower share of remunerative work or wage and salary workers (65.2 percent in January 2020 from 66.1 percent a year ago) and the decline in overall mean hours of work (hours per week) from 43.3 in January 2019 to 41.3 in January 2020.

To further improve the employment condition in the country, the government will continually improve its efforts towards providing an environment conducive to the creation of more and better employment opportunities. Also, the government intends to put in place interventions for workers that are displaced due to Taal volcano eruption and COVID-19, particularly those in the services and accommodation sectors.[26]

[23] NEDA (2019), "Socio Economic Report 2018." No targets for overall employment rate and underemployment rate.

[24] Taal volcano eruption could have a temporary impact on the manufacturing sector since CALABARZON accounts for 31 percent of the country's industry output (Source: NEDA (2020a), "Market Safeguards Needed as COVID-19 Concerns Pose risks to Factory Output-NEDA," 5 March).

[25] COVID-19 could have dampened the production of consumer-related manufactures (Source: NEDA (2020a)).

[26] NEDA (2020b), "Underemployment Rate Drops to New Record Low in 10 Years," 6 March.

II. Monetary and Financial Market Conditions

Domestic Liquidity

Domestic liquidity (M3) grew by 11.9 percent y-o-y in January 2020 to ₱12.8 trillion, faster than the 11.3-percent (revised) expansion as of end-Q4 2019.

Domestic liquidity expands faster

Money supply continued to increase due mainly to sustained demand for credit. Domestic claims grew by 11.7 percent in January from 10.6 percent (revised) as of end-Q4 2019 due to the sustained growth in credit to the private sector. Meanwhile, net claims on the central government rose by 31.9 percent in January, faster than the 23.8-percent (revised) growth as of end-Q4 2019.

Chart 16. Domestic Liquidity
Year-on-year growth rates in percent

Net foreign assets (NFA) in peso terms grew by 8.7 percent y-o-y in January from a growth of 8.9 percent (revised) in end-Q4 2019 as the NFA position of the BSP and banks improved during the month. The BSP's NFA position expanded in January, supported by foreign exchange inflows coming mainly from overseas Filipinos' remittances and business process outsourcing receipts. Similarly, the NFA of banks increased due to the sustained expansion in banks' foreign assets resulting from the growth in foreign loans and deposits with other banks.

Outstanding loans of commercial banks, net of reverse repurchase (RRP) placements with the BSP, increased by 11.6 percent y-o-y in January 2020, faster than the 10.9-percent growth rate posted at end-Q4 2019. However, this was slower than the 12.9-percent growth recorded in end-Q1 2019.

Although bank lending accelerates

Loans for production activities increased by 8.8 percent y-o-y in January 2020 from 9.1 percent in end-Q4 2019 and 12.8 percent in end-Q1 2019. The expansion in production loans was driven primarily by increased lending to the following sectors: real estate activities; financial and insurance activities; electricity, gas, steam and air conditioning supply; information and communication; and construction.

Chart 17. Loans Outstanding of Commercial Banks
Year-on-year growth rates in percent

Meanwhile, loans for household consumption grew by 40.1 percent in January 2020, higher than the 27.5-percent growth and 15.1-percent expansion in end-Q4 2019 and end-Q1 2019, respectively.

Monetary Operations

As of end-Q1 2020, total outstanding amount absorbed in the BSP liquidity facilities stood at ₱697.3 billion. Bulk of the BSP's liquidity-absorbing monetary operations had been through the reverse repurchase agreement or RRP facility, comprising about 44.8 percent of total outstanding amount of liquidity absorbed through the BSP liquidity facilities. Meanwhile, placements in the overnight deposit facility (ODF) and the term deposit facility (TDF) made up 43.7 percent and 11.5 percent, respectively.

Consistent with the BSP's assessment of prevailing liquidity conditions and taking into account the increase in system liquidity that needs to be absorbed following the holiday season, the average weekly total offer volumes was higher at about ₱151.8 billion for the TDF auctions on 2 January – 11 March relative to ₱126.9 billion average weekly volume offered in the previous quarter. The average bid-to-cover ratios for the 7-day, 14-day, and 28-day tenors were recorded at 1.4, 1.5, and 1.6 compared to 1.1, 1.1, and 1.1, respectively, in the previous quarter.

Following the NG's implementation of Enhanced Community Quarantine (ECQ) on 17 March 2020 to contain the spread of COVID-19,[27] the BSP cancelled the 18-March TDF auction. There were no TDF offerings for the scheduled TDF auction on 25 March as well. The suspension of TDF auctions were intended to ensure adequate short-term peso liquidity in the financial system and support the smooth flow of funding to businesses and households. Nevertheless, the RRP and standing overnight deposit and lending facilities remained open to help counterparties manage their liquidity requirements.

For Q1 2020, the average bid-to-cover ratio for the daily RRP offerings was higher at around 1.8 compared to 1.4 bid-to-cover ratio in Q4 2019. For ODF, average daily placements for the period 2 January – 13 March (period prior to ECQ) is at about ₱226.0 billion. During the ECQ period (16-31 March), average daily placements stood at about ₱227.0 billion. Meanwhile, availments in the BSP overnight lending facility (OLF) rose to an average of ₱28.5 billion (for the period 16-31 March 2020) from an average of ₱11.1 billion during the period 2 January - 13 March 2020.

[27] The NG initially implemented a community quarantine (CQ) beginning midnight of 15 March 2020. By 17 March, it put in place stricter quarantine measures with the enhanced CQ.

Credit Conditions

Credit Standards. The results of the Q1 2020 Senior Bank Loan Officers' Survey (SLOS)[28] showed that most of the respondent banks continued to maintain their overall credit standards for loans to both enterprises and households during the quarter based on the modal approach.[29] This is the 44th consecutive quarter since Q2 2009 that the majority of respondent banks reported broadly unchanged credit standards.

Majority of respondent banks maintain overall credit standards

The diffusion index (DI) approach,[30,31] meanwhile, indicated a net tightening of overall credit standards for loans to both enterprises and households. In the previous quarter, credit standards for business and consumer loans also showed a net tightening based on the DI approach.

The Q1 2020 SLOS was conducted during the period 28 February - 7 April 2020 and may not yet reflect the measures undertaken by the BSP, starting in the latter part of the reference quarter, to alleviate the effects of COVID-19 pandemic.

Lending to Enterprises. Most banks (66.7 percent of banks that responded to the question) indicated that they maintained their credit standards for loans to enterprises during the quarter using the

[28] The survey consists of questions on loan officers' perceptions relating to the overall credit standards of universal/commercial banks (U/KBs) and selected large thrift banks (TBs) in the Philippines, as well as to factors affecting the supply of and demand for loans by both enterprises and households. Survey questionnaires were sent to 65 U/KBs and TBs, of which, 37 banks responded to the current survey representing a response rate of 56.9 percent. The response rate for Q1 2020 SLOS is lower relative to previous survey rounds owing to the operational limitations of some banks following the implementation of the Luzon-wide enhanced community quarantine for the period 17 March - 30 April 2020, which coincided with the survey data collection period.

[29] In the modal approach, the results of the survey are analyzed by looking at the option with the highest share of responses.

[30] In the DI approach, a positive DI for credit standards indicates that the proportion of respondent banks that have tightened their credit standards exceeds those that eased ("net tightening"), whereas a negative DI for credit standards indicates that more respondent banks have eased their credit standards compared to those that tightened ("net easing").

[31] During the Q1 2010 to Q4 2012 survey rounds, the BSP used the diffusion index (DI) approach in the analysis of survey results. Beginning in Q1 2013, the BSP used both the modal and diffusion index (DI) approaches in assessing the results of the survey.

modal approach. Meanwhile, results based on the DI approach pointed to a net tightening of credit standards for the quarter, which was attributed by respondent banks largely to their perception of stricter financial system regulations, deterioration of borrowers' profiles as well as in the profitability and liquidity of banks' portfolios, and a reduced tolerance for risk. In terms of specific credit standards, the net tightening of overall credit standards was reflected in the reduced credit line sizes; stricter collateral requirements and loan covenants; and the increased use of interest rate floors.

Banks' responses likewise pointed to a net tightening of credit standards across all borrower firm sizes, namely, top corporations, large middle-market enterprises, small and medium enterprises (SMEs), and micro-enterprises based on the DI approach.

Table 11. General Credit Standards for Loans to Enterprises (Overall)

General Credit Standards for Loans to Enterprises (Overall)

	2018	2019				2020
	Q1	Q1	Q2	Q3	Q4	Q1
Tightened considerably	0.0	2.1	4.8	4.1	0.0	2.8
Tightened somewhat	3.7	22.9	11.9	12.2	15.2	30.6
Remained basically unchanged	**92.6**	**72.9**	**81.0**	**81.6**	**84.8**	**66.7**
Eased somewhat	3.7	0.0	0.0	0.0	0.0	0.0
Eased considerably	0.0	2.1	2.4	2.0	0.0	0.0
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Diffusion Index for Credit Standards	***0.0***	***22.9***	***14.3***	***14.3***	***15.2***	***33.3***
Weighted Diffusion Index for Credit Standards	***0.0***	***11.5***	***8.3***	***8.2***	***7.6***	***18.1***
Mean	*3.0*	*2.8*	*2.8*	*2.8*	*2.8*	*2.6*
Number of banks responding	***27.0***	***48.0***	***42.0***	***49.0***	***46.0***	***36.0***

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").

Over the next quarter, results based on the modal approach showed that most of the respondent banks expect credit standards to remain basically unchanged. Meanwhile, results based on the DI approach indicated expectations of net tightening of credit standards due largely to respondent banks' less favorable economic outlook, expected deterioration in borrowers' profiles as well as in the profitability and liquidity of banks' portfolios, and lower tolerance for risk.

Lending to Households. The results of the survey likewise showed that most respondent banks (69.6 percent) kept their overall credit standards unchanged for loans extended to households during the quarter based on the modal approach. However, results based on the DI approach indicated net tightening of credit standards for household loans, attributed largely to respondent banks' more uncertain economic outlook and reduced tolerance for risk, among other factors. The overall net tightening of credit standards for loans to households also reflected stricter collateral requirements and loan covenants as well as increased use of interest rate floors by respondent banks for the said type of loan.

Table 12. General Credit Standards for Loans to Households (Overall)

General Credit Standards for Loans to Households (Overall)

	2018	2019				2020
	Q1	Q1	Q2	Q3	Q4	Q1
Tightened considerably	0.0	3.3	4.0	3.1	0.0	0.0
Tightened somewhat	15.8	16.7	8.0	6.3	6.9	21.7
Remained basically unchanged	**78.9**	**73.3**	**88.0**	**81.3**	**89.7**	**69.6**
Eased somewhat	5.3	3.3	0.0	9.4	3.4	8.7
Eased considerably	0.0	3.3	0.0	0.0	0.0	0.0
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Diffusion Index for Credit Standards	***10.5***	***13.3***	***12.0***	***0.0***	***3.4***	***13.0***
Weighted Diffusion Index for Credit Standards	***5.3***	***6.7***	***8.0***	***1.6***	***1.7***	***6.5***
Mean	*2.9*	*2.9*	*2.8*	*3.0*	*3.0*	*2.9*
Number of banks responding	***19.0***	***30.0***	***25.0***	***32.0***	***29.0***	***23.0***

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").

Banks' responses pointed to a net tightening of credit standards across all types of consumer loans, including housing loans, credit card loans, auto loans, and personal/salary loans.

In terms of respondent banks' outlook for the next quarter, results based on modal approach reflected unchanged overall credit standards. However, DI-based results indicated expectations of net tighter credit standards for household loans due largely to respondent banks' expectations of uncertain economic outlook, deterioration in profitability of banks' portfolios, and a reduced tolerance for risk.

Loan demand. Responses to the survey question on loan demand indicated that the majority of respondent banks continued to see stable overall demand for loans from both enterprises and households during the quarter. Meanwhile, results based on the DI approach showed a net increase in overall demand[32] for both business and household loans.

The overall net increase in loan demand from firms was associated by respondent banks largely to their customers' higher investment in plant or equipment, lower interest rates, and increased inventory financing needs of clients. Meanwhile, respondent banks cited higher household consumption and housing investment as well as

[32] The "DI for loan demand" refers to the percentage difference between banks reporting an increase in loan demand and banks reporting a decrease. A positive DI for loan demand indicates that more banks reported an increase in loan demand compared to those stating the opposite, whereas a negative DI for loan demand implies that more banks reported a decrease in loan demand compared to those reporting an increase.

lack of other sources of funds as reasons for the overall net increase in household loan demand for the quarter.

Loan demand from firms and households remains stable

Over the next quarter, most of respondent banks expect steady overall loan demand from firms and households. However, DI-based results suggested expectations of a net increase in overall loan demand for business loans and a net decrease in household loans. For business loans, the expected net increase in demand was associated largely with corporate clients' higher working capital requirements, a decline in internally-generated funds, and increased inventory financing needs of clients. Meanwhile, the anticipated net decrease in household loan demand in Q2 2020 largely reflected expectations of less attractive financing terms offered by banks and availability of other sources of funds.

Real Estate Loans. Most of the respondent banks (80.0 percent) reported that overall credit standards for commercial real estate loans were maintained in Q1 2020. The DI approach, however, continued to point to a net tightening of overall credit standards for commercial real estate loans for the 17th consecutive quarter.

Respondent banks cited less favorable economic outlook, deterioration in the liquidity of banks' portfolios and borrowers' profiles, and a reduced tolerance for risk as reasons for the tightening of overall credit standards for the said type of loan. In terms of specific credit standards, the net tightening of overall credit standards for commercial real estate loans reflected wider loan margins, reduced credit line sizes, stricter collateral requirements and loan covenants, shortened loan maturities, and increased use of interest rate floors. Over the next quarter, while most of the respondent banks anticipate maintaining their credit standards for commercial real estate loans, DI-based results point to expectations of continued net tightening of overall credit standards for the said type of loan.

Majority of banks maintain credit standards for real estate loans

Demand for commercial real estate loans was also unchanged in Q1 2020 based on both the modal and DI approaches. Over the next quarter, although most of the respondent banks anticipated generally steady loan demand, more banks expected demand for commercial real estate loans to decrease compared to those expecting an increase amid a deterioration in economic outlook and lower inventory financing needs of clients.

For housing loans extended to households, most of the respondent banks (65.0 percent) reported maintaining their credit standards, while the DI approach pointed to a net tightening of overall credit standards on the back of respondent banks' perception of less favorable economic outlook and a reduced tolerance for risk. Over the next quarter, results based on the modal approach showed that respondent banks expect overall credit standards for housing loans to remain unchanged. However, using the DI approach, survey results pointed to expectations of continued net tightening of overall credit standards for housing loans, reflecting respondent banks' more uncertain economic outlook, expected deterioration in the profitability of banks' loan portfolio, and lower risk tolerance.

Results based on both the modal and DI approaches pointed to unchanged demand for housing loans in Q1 2020, which was attributed by respondent banks largely to steady interest rates and income prospects of clients. Majority of respondent banks also foresee unchanged demand for housing loans over the next quarter. However, DI-based results indicated expectations of a net increase in housing loan demand in Q2 2020, supported largely by higher household consumption.

Interest Rates

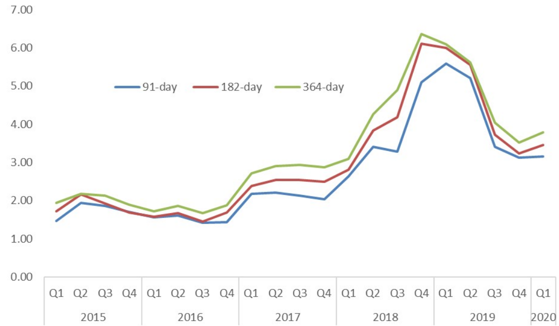
Primary Interest Rates

The average interest rates for the 91-, 182- and 364-day T-bills in the primary market in Q1 2020 rose to 3.161 percent, 3.459 percent, and 3.793 percent from 3.118 percent, 3.229 percent, and 3.528 percent, respectively, in the previous quarter.

T-bill rates increase

The results of the auctions reflected market players' risk aversion amid geopolitical tensions between the US and Iran as well as concerns over the impact of Taal Volcano eruption during the early part of the quarter. However, a declining trend was seen mid-part of the quarter following the 75-basis point (bp) cumulative policy rate cut by the BSP[33] and due to increased demand for shorter tenored debt notes amid uncertainties brought about by lingering concerns over the COVID-19 outbreak.

Chart 18. Treasury Bill Rates
In percent

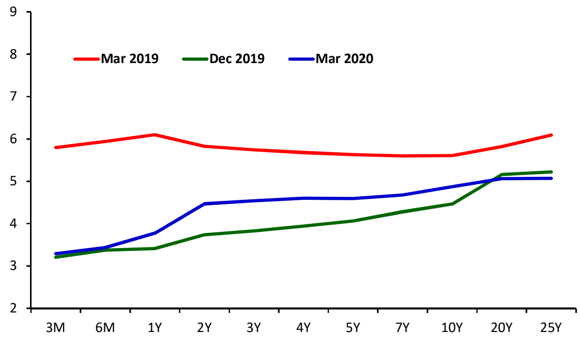


Yield Curve.[34] As of end-March 2020, the yields for government securities (GS) in the secondary market rose generally (except for the 10-year and 20-year GS) relative to the end-December 2019 levels, as market players invested their excess liquidity and serviced their clients' requirements in anticipation of the additional liquidity following the reductions in the reserve requirement ratios.

GS yields rose generally

Debt paper yields were higher by a range of 5.8 bps for the 6-month GS to 73.1 bps for the 2-year GS compared to end-December 2019 levels. Meanwhile, secondary market yields for the 10-year and 20-year GS declined by 15.0 bps and 9.8 bps, respectively.

Chart 19. Yields of Government Securities in the Secondary Market
In percent



Source: Bloomberg

Relative to year-ago levels, the secondary market yields for GS for all maturities decreased by a range of 73.3 bps (for the 7-year GS) to 250.9 bps (for the 3-month GS).

Interest Rate Differentials. The average differentials between domestic and US interest rates, gross and net of tax, widened generally in Q1 2020 relative to the previous quarter.

Interest rate differentials widen in Q1 2020

The average 91-day RP T-bill rate rose slightly q-o-q by 1.9 bps to 3.137 percent in Q1 2020 from 3.118 percent in Q4 2019. Meanwhile, the average US 90-day LIBOR and the US 90-day T-bill rate declined by 39.6 bps and 50.9 bps, respectively, to 1.534 percent and 1.083 percent in Q1 2020. These developments led generally to wider positive gross and net of tax differentials between the 91-day RP T-bill rate and US interest rates. Domestic and foreign interest rates showed mixed trends following market uncertainties from the COVID-19 outbreak, the BSP cuts in the reserve requirement ratios of universal and commercial banks and the reduction in the BSP's policy rates and the US federal funds target rate during the quarter.

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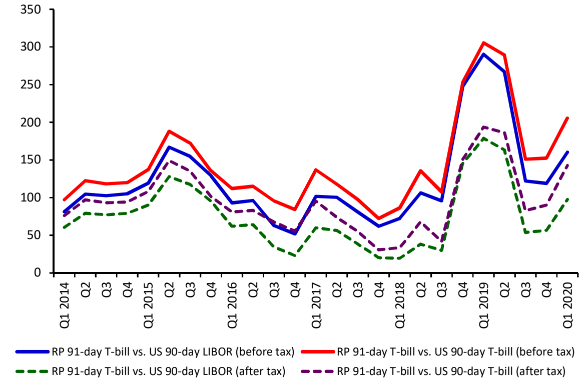
[33] The BSP reduced the key policy rate by 25 bps to 3.75 percent and 50 bps to 3.25 percent for the overnight reverse repurchase or RRP facility on 6 February and 19 March, respectively. The interest rates on the overnight lending and deposit facilities were likewise raised accordingly.

[34] On 29 October 2018, the Bankers Association of the Philippines (BAP) replaced the PDST Reference Rates and launched the PHP BVAL Reference Rates which will be used as the Philippine Peso GS benchmark. The PHP BVAL Reference Rates are calculated by Bloomberg Finance Singapore L.P. and/or its affiliates in an agreement with the BAP.

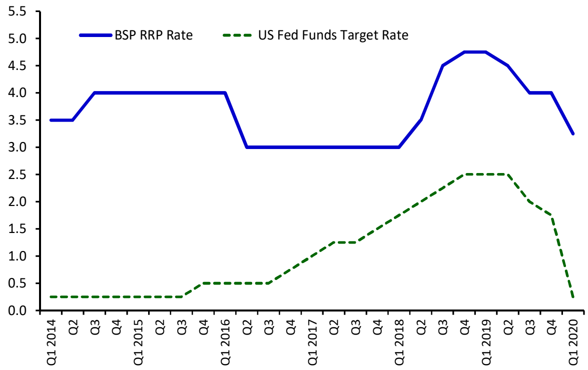
Chart 20. Interest Rate Differentials
Quarterly averages; in basis points



Source: Bloomberg, Btr and BSP

The positive differential between the BSP's policy rate (overnight RRP rate) and the US Fed funds target rate widened to a range of 300-325 bps in Q1 2020 from 225-250 bps in Q4 2019, reflecting the impact of the 75-bp cumulative decrease in the BSP’s overnight RRP rate to 3.75 percent on 6 February 2020 and 3.25 percent on 19 March 2020, and the 150-bp cumulative decrease in the US federal funds rate target range to 1.00-1.25 percent on 3 March 2020 and 0.00-0.25 percent on 16 March 2020.

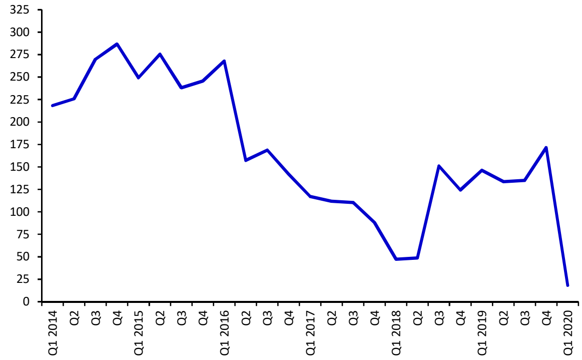
Chart 21. BSP RRP Rate and US Federal Funds Target Rate
In percent



Source: Bloomberg and BSP

Meanwhile, the interest rate differential between the BSP’s overnight RRP rate and the US Fed funds target rate adjusted for risk[35] narrowed to 18 bps as of end-March 2020 from 172 bps in end-December 2019.

Chart 22. Risk-Adjusted Differentials
In basis points



Source: Bloomberg and BSP

This development could be traced to the 228-bp increase in the country risk premium following the 122-bp decrease in the 10-year US note and the 106-bp rise in the 10-year ROP note, and 75-bp increase in the interest rate differential between the BSP’s overnight RRP rate and the US federal funds rate.

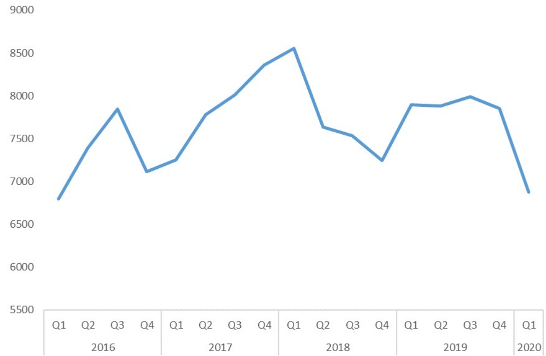
Financial Market Conditions

The financial system saw rising uncertainty as the COVID-19 pandemic, and the measures to contain the spread of the virus, affected the global and domestic economy. Nevertheless, the country’s firm macroeconomic fundamentals, as well as accommodative policies by the NG and BSP, provided support to the financial system and calmed market sentiment.

Stock Market. In Q1 2020, the Philippine Stock Exchange index (PSEi) averaged 6,876.72 index points, about 12.4 percent lower than the average in the previous quarter. In end-March 2020, the PSEi likewise closed 31.9 percent lower year-to-date at 5,321.23 index points. Relative to the all-time-peak registered in January 2018 at 9,058.62 index points, the PSEi also closed 41.3 percent lower on 31 March 2020.

[35] The difference between the 10-year ROP note and the 10-year US Treasury note is used as proxy for the risk premium.

Chart 23. Quarterly Average PSEi
In index points



Source: PSEi

Weighing down the main index were concerns over the economic impact of Taal Volcano's eruption, the spread of COVID-19, the imposition of the enhanced community quarantine (ECQ) to deal with the virus' spread, and uncertainty surrounding the renewal of the legislative franchise of a television network. Market pressures were also raised by brewing tensions between Libya and Iraq,[36] the mounting conflict between the US and Iran,[37] and Moody's downgrading of Hong Kong's credit rating. However, the decline was partly tempered by the market's positive reaction to the following: the signing of the Phase-one trade deal between the US and China on 15 January 2020, the faster Q4 2019 Philippine GDP growth, the BSP's decision to inject liquidity into the economy through cuts in the key policy rate and the reduction in banks' reserve requirement ratio (RRR), and R&I's upgrade of the Philippines' credit rating to "BBB+".

Other stock market indicators also exhibited general declines during the review period. Total market capitalization declined by 27.8 percent from ₽16.7 trillion in end-December 2019 to ₽12.1 trillion on 27 March 2020. Foreign investors posted net sales of ₽32.9 billion in Q1 2020 from net sales of ₽23.0 billion in the preceding quarter. Meanwhile, listed firms' price-earnings ratio declined to 12x in end-March 2020 from 17x in end-December 2019.

[36] On 20 January 2020g, oil prices climbed on supply disruption driven by unrest in Libya and Iraq. The largest oil field in Libya shutdown production after armed forces cut off a pipeline and blocked exports. Meanwhile, in Iraq, escalating protest stopped work at a minor field on 19 January.
[37] Since 3 January 2020, the conflict between the US and Iran heightened following the death of Iran's military commander, Qassem Soleimani, and Iran's retaliation by firing missiles on two military bases in Iraq that hosted US troops.

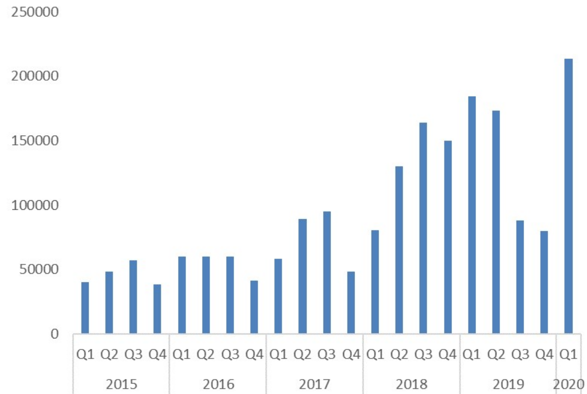
Government Securities. Results of the T-bill auctions conducted in January – March 2020 continued to show robust demand for government securities with total subscription for the quarter amounting to around ₽599.8 billion or about 2.2 times the ₽275.0-billion aggregate offered amount. The oversubscription for Q1 2020, at ₽324.8 billion, was higher than the ₽134.5-billion oversubscription in the previous quarter.

Demand for T-bills remains strong

The Bureau of the Treasury (BTr) awarded in full the ₱8.0-billion, ₱6.0-billion and ₱6.0-billion offered amounts for the 91-, 182- and 364-day T-bills in all auctions, however made partial awards for the 182- and 364-day T-bills during the 6-January and 14-January auctions and rejected all bids for the 91-day T-bills during the 16-March auction.

Meanwhile, all bids for the 91-, 182-, and 364-day T-bills were rejected by the BTr during the 23-, 30-, and 31-March auctions. The BTr also offered 35-day T-bills on 31 March as a response to the increased appetite of the market for short-term government securities. Similarly, the BTr rejected all bids for the 35-day T-bills.

Chart 24. Total Oversubscription of T-bill Auctions



Results of the T-bond auctions during the quarter likewise showed sustained demand for longer-term government debt papers.

Sovereign Bond and Credit Default Swap (CDS) Spreads. In January, debt spreads narrowed slightly, reflecting the relative stability in the sovereign credit markets and market participants' view of continued improvements in the country's financing conditions. Domestically, the eruption of the Taal volcano affected some parts of Luzon but the resulting brief interruption in business activities generally had insignificant impact on investor sentiment.

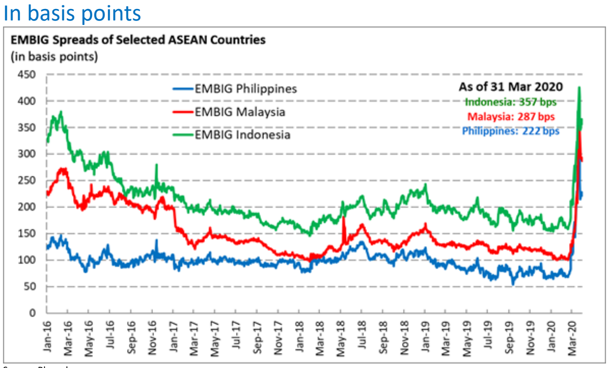
Debt spreads widen on uncertainty amid COVID-19 global outbreak

In February, debt spreads widened as market uncertainty increased amid the spread of COVID-19 in many countries. In March, debt spreads widened further due to a combination of different factors, namely, the increasingly rapid spread of COVID-19; large oil price declines; and financial shocks arising from the pandemic and its negative impact on economies around the world.

As of 31 March 2020, the extra yield investors demanded to own Philippine sovereign debt over US Treasuries or the Emerging Market Bond Index Global (EMBIG) Philippines spread stood higher at 222 bps from the end-December level of 67 bps.

Chart 25. EMBIG Spreads of Selected ASEAN Countries

In basis points

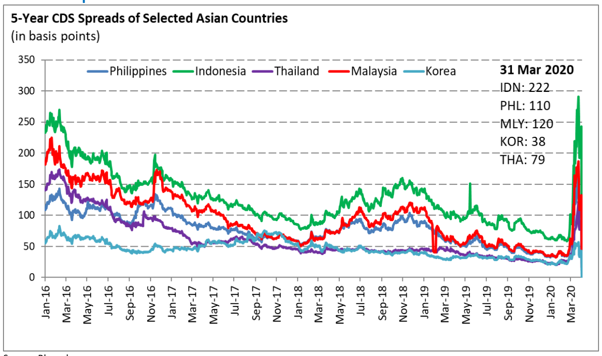


Source: Bloomberg

Similarly, the country's 5-year sovereign credit default swap (CDS) spread increased to 110 bps from its end-December level of 34 bps. Against other neighboring economies, the Philippine CDS spread was narrower than Malaysia's 120 bps and Indonesia's 222 bps but wider than Thailand's 79 bps and Korea's 38 bps spreads.

Chart 26. Five-Year CDS Spreads of Selected ASEAN Countries

In basis points



Source: Bloomberg

Banking System

The Philippine banking system continued to show resilience and stability. In Q1 2020, banks' balance sheets exhibited sustained growth in assets and deposits.

Banking system sustains growth in assets and deposits

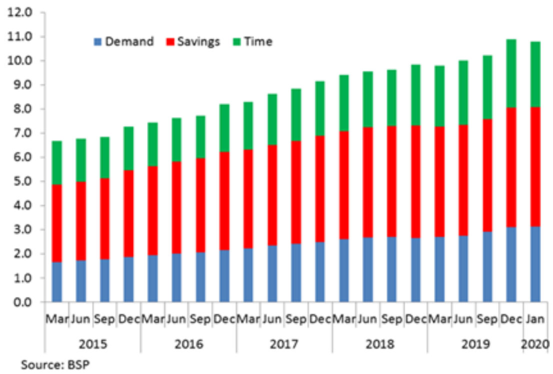
Furthermore, asset quality indicators remained healthy while capital adequacy ratios continued to be above international standards, even with the implementation of the tighter Basel III framework.[38]

Savings Mobilization. Savings deposits remained the primary sources of funds for the banking system. Banks' total deposits as of end-January 2020 amounted to ₱10.8 trillion, 10.8 percent higher than the year-ago level.[39] Relative to the end-December 2019 level, total deposits meanwhile decreased slightly by 1.0 percent.

[38] Beginning 1 July 2018, covered institutions (universal banks [UBs], commercial banks [KBs] and their subsidiary banks and quasi-banks [QBs]) must maintain a leverage ratio of no lower than five (5) percent. The leverage ratio is a non-risk based measure, which serves as a backstop to the Capital Adequacy Ratio. It is designed to constrain the potential build-up of leverage in the banking industry and to promote stability of the financial system. Also, the BSP sets an observation period of six months (from 1 July 2018 to 31 December 2018) for the Net Stable Funding Ratio (NSFR). This is to ensure a smooth transition to the new prudential standard and to allow prompt assessment and calibration of the components of the NSFR. Beginning 1 January 2019, however, the covered institutions (U/KBs) shall maintain an NSFR of 100.0 percent on both solo and consolidated bases.

[39] This refers to the total peso-denominated deposits of the banking system.

Chart 27. Deposit Liabilities of Banks
In billion pesos



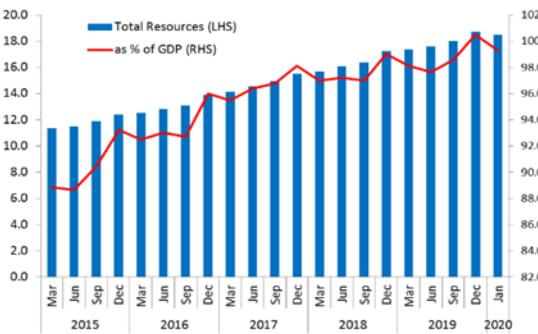
Source: BSP

Meanwhile, foreign currency deposits owned by residents (FCD-Residents) reached ₱2.0 trillion as of end-January 2020, posting a y-o-y growth of 2.3 percent. With respect to the end-December 2019 level, FCD-Residents likewise increased by 2.5 percent.[40]

Institutional Developments. The total resources of the banking system grew by 9.1 percent to reach ₱18.5 trillion as of end-January 2020 from ₱17 trillion a year ago. Meanwhile, relative to the end-December 2019 level, total resources of the banking system declined slightly by 1.1 percent. As a percent of GDP, total resources stood at 99.3 percent.[41]

Total resources of the banking system continue to grow

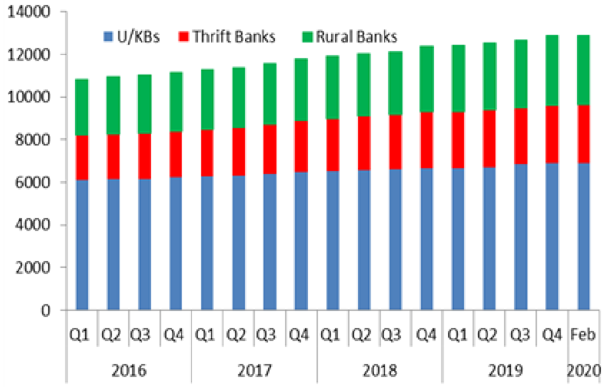
Chart 28. Total Resources of the Banking System
levels in billion pesos; share in percent



Source: BSP

The number of banking institutions (head offices) as of end-February 2020 decreased to 544 offices from 547 in end-December 2019. The banks' head offices are comprised of 46 U/KBs, 50 TBs, and 448 rural banks (RBs).

Chart 29. Number of Banking Institutions



Source: BSP

The banking system's gross non-performing loans (GNPL) ratio rose to 2.2 percent as of end-January 2020 relative to the 2.0 percent posted a month- and a year- ago.

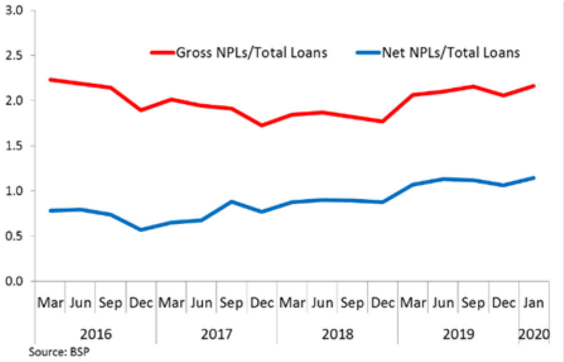
Asset quality of Philippine banks remains healthy

Banks' initiatives to improve their asset quality along with prudent lending regulations helped maintain the GNPL ratio below its pre-Asian crisis level of 3.5 percent.[42] Meanwhile, net non-performing loans (NNPL) ratio as of end-January 2020 remained unchanged at 1.1 percent relative to the previous month's and year's reported ratios. In computing for the NNPLs, specific allowances for credit losses on Total Loan Portfolio (TLP) are deducted from the GNPLs. Said allowances increased slightly to ₱110.8 billion in January 2020 from ₱108.3 billion posted as of end-December 2019.[43]

[40] FCD-Residents, along with M3, forms part of a money supply measure called M4. Meanwhile, M3 consists of savings deposits, time deposits, demand deposits, currency in circulation, and deposit substitutes.
[41] GDP as of the fourth quarter of 2019.

[42] The 3.5 percent NPL ratio was based on the pre-2013 definition.
[43] This type of provisioning applies to loan accounts classified under loans especially mentioned (LEM), substandard-secured loans, substandard-unsecured loans, doubtful accounts and loans considered as loss accounts.

Chart 30. Ratios of Gross Non-Performing Loans and Net Non-Performing Loans to Total Loans
In percent



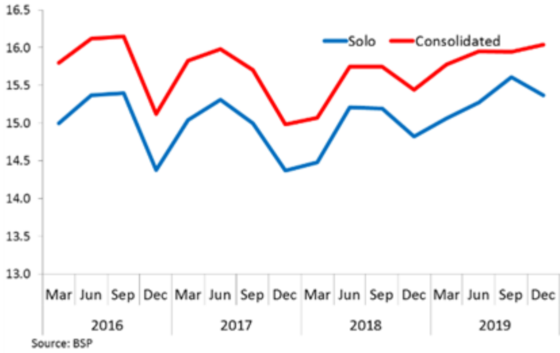
The Philippine banking system's GNPL ratio of 2.2 percent was higher compared to those of Malaysia (1.0 percent) and South Korea (0.8 percent) but was lower than that of Indonesia (2.4 percent) and Thailand (3.0 percent).[44]

The loan exposures of banks remained adequately covered with the banking system's NPL coverage ratio at 91.6 percent as of end-January 2020. This was, however, lower than the year- and month-ago ratios of 97.0 percent and 92.6 percent, respectively.

U/KBs' CAR remains above international and regulatory standards

The capital adequacy ratio (CAR) of U/KBs at end-December 2019, on solo basis, decreased marginally to 15.4 percent from 15.6 percent as of end-September 2019. Meanwhile, on a consolidated basis, CAR of U/KBs increased slightly to 16.0 percent in December 2019 from 15.9 percent as of end-September 2019. These ratios remained well above the BSP's regulatory threshold of 10.0 percent and international standard of 8.0 percent.

Chart 31. Capital Adequacy Ratio of Universal and Commercial Banks
In percent



The CAR of Philippine U/KBs, on consolidated basis, was higher than that of South Korea (15.3 percent) but lower than those of Malaysia (17.9 percent), Thailand (19.5 percent) and Indonesia (23.3 percent).[45]

Exchange Rate

The peso averaged at ₱50.83/US$1 in Q1 2020, appreciating by 0.39 percent from the Q4 2019 average of ₱51.03/US$1.

Peso appreciates on US Fed rate cut expectations

Despite the outbreak of COVID-19 in the country, the peso appreciated due mainly to the continued decline in global oil prices and positive market sentiment amid the credit rating outlook upgrade by Fitch Ratings for the Philippines in February 2020. Policy measures implemented by authorities to counter the impact of the COVID-19 on the economy also supported the peso. On a y-o-y basis, the peso likewise appreciated by 3.02 percent relative to the ₱52.37/US$1 average in Q1 2019.[46]

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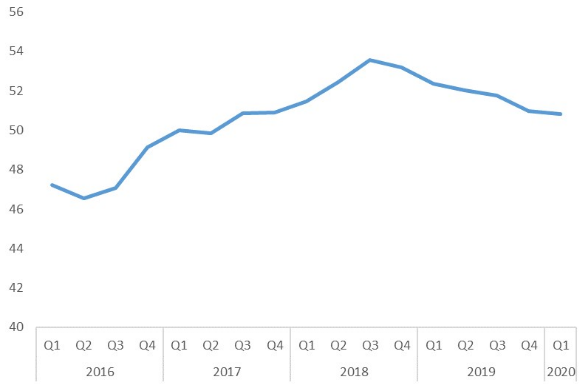
[44] Sources: Malaysia (Banking System's Ratio of net impaired loans to net total loans, December 2019); South Korea (Domestic Banks' Substandard or Below Loans [SBLs] ratio, December 2019); Indonesia, IMF and financial stability report (Banks' Nonperforming Loans to Gross Loans Ratio, December 2019); and Thailand (Total Financial Institutions' Gross NPLs ratio, December 2019).

[45] Sources: South Korea (Capital Ratios of Banks and Bank Holding Companies, December 2019); Malaysia (Banking System's Total Capital Ratio, December 2019); Thailand (Commercial Banks' Capital Funds Percentage of Risk Assets, January 2020); and Indonesia, IMF and financial stability report (Commercial Banks, Regulatory Capital to Risk-Weighted Assets Ratio, December 2019).

[46] Dollar rates (per peso) or the reciprocal of the peso-dollar rates were used to compute for the percentage change.

Chart 32. Quarterly Peso-Dollar Rate
PHp/US$; average per quarter



In January 2020, the peso depreciated by 0.14 percent to an average of ₱50.84/US$1 from the ₱50.77/US$1 average in December 2019, due partly to global market risk aversion and safe-haven buying driven by (i) the geopolitical tension between the US and Iran; and (ii) heightened fears of the potential economic impact of the spread of COVID-19.

Meanwhile, in February, the peso appreciated marginally by 0.18 percent to ₱50.74/US$1 from the month-ago average amid market expectation of a BSP rate cut in its 6 February 2020 monetary policy meeting and optimism over China's actions towards containing the COVID-19 outbreak. In addition, the credit rating outlook upgrade for the Philippines by Fitch Ratings, as well as the release of narrower trade deficit data for 2019 likewise provided support to the peso.

In March, the peso depreciated again by 0.31 percent to an average of ₱50.90/US$1 from the average in the previous month. The depreciation of the peso reflected continued concerns about the global impact of the COVID-19 outbreak, which has then spread outside China. The imposition of a community quarantine in NCR and, afterwards, the enhanced community quarantine covering the entire island of Luzon amid concerns over the spread of COVID-19 in the country have likewise added pressure to the peso.

On a y-t-d basis, the peso depreciated slightly against the US dollar by 0.09 percent to close at ₱50.68/US$1 on 31 March 2020 from the end-December 2019 closing rate of ₱50.64/US$1.[47]

Nevertheless, sustained inflows of foreign exchange from overseas Filipino remittances, foreign direct investments (expected to resume after the recovery from the COVID-19 pandemic), BPO receipts and the ample level of the country's gross international reserve (GIR) continued to provide support to the peso.

Meanwhile, the volatility of the daily closing rate of the peso (as measured by the coefficient of variation) stood at 0.43 percent in Q1 2020. This was lower than the 0.80 percent registered in the previous quarter.[48] The volatility of the peso in the review quarter was lower than the volatility of most currencies in the region.

On a real trade-weighted basis, the peso lost external price competitiveness in Q1 2020 against the basket of currencies of all trading partners (TPI); trading partners in advanced (TPI-A) countries; and trading partners in developing (TPI-D) countries relative to Q4 2019. This was indicated by the increase in the real effective exchange rate (REER) index of the peso by 3.58 percent, 6.58 percent, and 1.96 percent, against the TPI, TPI-A and TPI-D baskets, respectively.[49,50]

[47] Based on the last done deal transaction in the afternoon.
[48] The coefficient of variation is computed as the standard deviation of the daily closing exchange rate divided by the average exchange rates for the period.
[49] The TPI measures the nominal and real effective exchange rates of the peso across the currencies of 14 major trading partners (MTP:s) of the Philippines, which includes US, Euro Area, Japan, Australia, China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand. The TPI-A measures the effective exchange rates of the peso across currencies of trading partners in advanced countries comprising of the US, Japan, Euro Area, and Australia. The TPI-D measures the effective exchange rates of the peso across 10 currencies of partner developing countries which includes China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.
[50] The REER index represents the Nominal Effective Exchange Rate (NEER) index of the peso, adjusted for inflation rate differentials with the countries whose currencies comprise the NEER index basket. A decrease in the REER index indicates some gain in the external price competitiveness of the peso, while a significant increase indicates the opposite. The NEER index, meanwhile, represents the weighted average exchange rate of the peso vis-à-vis a basket of foreign currencies.

Relative to Q1 2019, the peso likewise lost external price competitiveness across currency baskets during the review period. This developed following the nominal appreciation of the peso and the widening inflation differential, resulting in the increase in the REER index of the peso by 5.18 percent, 6.04 percent and 4.70 percent against the TPI, TPI-A and TPI-D baskets, respectively.

III. Fiscal Developments

The NG recorded a ₱23.0-billion fiscal surplus for January 2020, about 48 percent lower than the surplus reported in the same period in 2019.

NG records a fiscal surplus in January 2020

Netting out the interest payments in expenditures, the NG posted primary surplus amounting to ₱84.5 billion which is 6 percent lower than the amount recorded in 2019.

Table 13. National Government Fiscal Performance
In billion pesos

	2019				
	Jan- Dec	Program	Percentage Share Program (%)	Jan	Jai
Surplus/(Deficit)	(660.2)	(620.0)	106.5	44.5	23.
Revenues	3,137.5	3,149.7	99.6	256.7	294
Expenditures	3,797.7	3,769.7	90.4	212.2	271

Revenues by the NG increased by 14.8 percent to ₱294.6 billion in January 2020 from ₱256.7 billion in the same period last year. The Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) contributed ₱194.9 billion and ₱55.9 billion, respectively. Revenue collections by the BIR and BOC were higher by 5.3 percent and 15.5 percent, respectively. Meanwhile, the Bureau of the Treasury (BTr) recorded an income of ₱28.4 billion, almost thrice the amount recorded last year. The increase was driven by ₱17.3-billion dividend remittance from the BSP and ₱1.4-billion increase in the Bond Sinking Fund (BSF) investment income.

Expenditures for the period in review amounted to ₱271.6 billion, 28 percent higher than the expenditures in January 2019. Excluding interest payments, expenditures went up by 26.4 percent to ₱210.2 billion. Meanwhile, interest payment was 33.8 percent higher compared to its year-ago level, reaching ₱61.4 billion in January 2020.

IV. External Developments

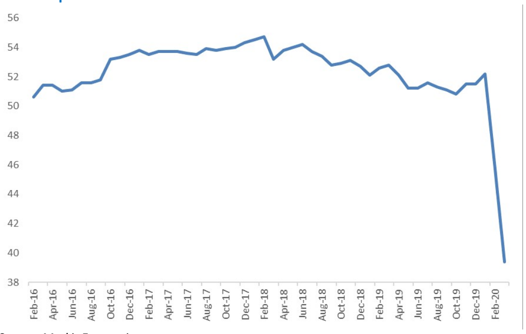
The JP Morgan Global All-Industry Output Index fell to its lowest level since 2009 at 39.4 in March 2020 from 46.1 in February as new business, business activity, and new export business contracted during the month.

Global economic activity contracts in March

China posted an easing in its rate of contraction, while the US saw the weakest downturn among large developed economies. Japan, the euro area, and the UK also recorded steep declines in economic activity.[51]

Chart 33. JP Morgan Global All-Industry Output Index

Index points



Source: Markit Economics

US. Real GDP expanded by 2.1 percent on a seasonally adjusted q-o-q basis in Q4 2019, the same rate posted in Q3 2019. On a y-o-y basis, real output grew by 2.3 percent in Q4 2019 from the 2.1-percent expansion in the previous quarter.

US manufacturing activity weakens

The increase in real GDP in the fourth quarter reflected positive contributions from personal consumption expenditures, exports, residential fixed investment, federal government spending, and state and local government spending. These movements were partly offset by negative contributions from private inventory investment and nonresidential fixed investment. [52]

Meanwhile, US manufacturing activity fell into contraction territory with a PMI reading of 49.1 percent in March from 50.1 percent in February, driven mainly by a decline in new orders amid weak demand.[53]

The unemployment rate decreased to 4.4 percent in March from 3.5 percent in February. Total nonfarm payroll employment rose by 701,000 during the month. Employment losses occurred in leisure and hospitality, health care and social assistances, professional and business services, retail trade, and construction. Meanwhile, on a y-o-y basis, inflation decreased to 1.5 percent in March from 2.3 percent in February, driven mainly by a decline in the energy price index.

The Conference Board Consumer Confidence Index fell sharply to 120.0 in March from 132.6 in February.[54] Consumers' assessment of current business and labor market conditions and their outlook regarding jobs and financial prospects declined during the month amid the intensification of the COVID-19 pandemic and the resulting volatility in the financial markets. Similarly, the Thomson-Reuters/University of Michigan Index of Consumer Sentiment fell to 89.1 in March from 101.0 in February.[55]

Euro Area. On a q-o-q basis, real GDP in the euro area expanded by 0.1 percent in Q4 2019 from 0.3 percent in Q3 2019. On a y-o-y basis, real GDP grew by 1.0 percent in Q4 2019 from 1.3 percent in the previous quarter.[56]

Economic activity in the euro area declines sharply

Meanwhile, composite PMI for the euro area recorded its biggest single monthly decline to

[51] JP Morgan Global Manufacturing & Services PMI, http://www.markiteconomics.com/

[52] US Bureau of Economic Analysis, "Gross Domestic Product: Fourth Quarter and Year 2019 (Third Estimate)," news release, 26 March 2020. https://www.bea.gov/system/files/2020-03/gdp4q19_3rd_0.pdf

[53] Institute for Supply Management, https://www.instituteforsupplymanagement.org

[54] The Conference Board, http://www.conference–board.org/

[55] University of Michigan Survey of Consumers, http://www.sca.isr.umich.edu/

[56] Eurostat news release 41/2020 dated 10 March 2020

29.7 in March from 51.6 in February as the COVID-19 pandemic led to all four major economies in the region tallying declines in activity, with Italy and Spain experiencing the sharpest contractions.[57]

Inflation in the euro area fell to 0.7 percent in March from 1.2 percent in February due mainly to lower inflation for energy and services.[58] Meanwhile, the seasonally adjusted unemployment rate decreased to 7.3 percent in February from 7.4 percent in the previous month.

The European Commission's Economic Sentiment Indicator in the euro area fell to 94.5 in March from 103.4 in February due to weaker confidence among consumers and in all the business sectors. Confidence collapsed substantially in services and retail trade.

Japan. On a q-o-q seasonally adjusted basis, real GDP contracted by 1.8 percent in Q4 2019 from zero percent (revised) in Q3 2019. Similarly, on a y-o-y basis, real GDP declined by 0.7 percent in Q4 2019 after expanding by 1.7 percent in the previous quarter as private demand contracted during the quarter.[59]

Manufacturing activity in Japan slides deeper into contraction

The seasonally adjusted manufacturing PMI remained in contraction at 44.8 in March from 47.8 in February as new orders and output decreased further amid weak demand for Japanese goods resulting from the COVID-19 pandemic.[60]

Inflation fell to 0.4 percent in February from 0.7 percent in January, driven mainly by lower inflation for energy; fuel, light, and water charges; and education. Meanwhile, the seasonally adjusted unemployment rate was 2.4 percent in February, unchanged from the rate posted in January.

China. Real GDP in China grew by 6.0 percent y-o-y in Q4 2019, unchanged from the record in Q3 2019 due to weak domestic and external demand amid US trade isssues during the quarter. The Q4 2019 GDP expansion brought China's GDP growth to 6.1 percent for the full-year 2019.

Chinese manufacturing activity recovers but appears to remain fragile

Meanwhile, the seasonally adjusted manufacturing PMI rose to 50.1 in March from 40.3 in February after some of the restrictive measures related to stemming the spread of COVID-19 were lifted during the month. However, demand conditions remained fragile, as indicated by a continued decline in total new business.[61]

Inflation decreased to 4.3 percent in March from 5.2 percent in February due to lower food and non-food inflation.

India. Real GDP in India grew by 4.7 percent y-o-y in Q4 2019 from 5.1 percent (revised) in the previous quarter. Notwithstanding the slowdown, the latest GDP expansion was driven mainly by growth in agriculture, forestry, and fishing; mining and quarrying; trade, hotels, transport, communication and services related to broadcasting; and financial, real estate and professional services.[62]

Economic activity in India expands at a slower pace

Meanwhile, the composite PMI fell to 50.6 in March from 57.6 in February, reflecting a sharp slowdown in private sector output growth due largely to the decline in service sector activity.

Inflation fell to 5.9 percent in March from 6.6 percent in February, driven by lower inflation for food and beverages.

ASEAN Region. The Nikkei ASEAN Manufacturing PMI fell from 50.2 in February to 43.4 in March, its lowest level since 2012, amid record declines in

[57] Markit Eurozone PMI, http://www.markiteconomics.com/
[58] Eurostat news release 61/2020 dated 17 April 2020
[59] Second Preliminary Estimate. Department of National Accounts, Economic and Social Research Institute, Cabinet Office. http://www/esri.cao.go.jp/
[60] Jibun Bank Japan Manufacturing PMI, http://www.markiteconomics .com/
[61] Caixin China General Manufacturing PMI, http://www.markiteconomics.com/
[62] Ministry of Statistics and Programme Implementation. http://mospi.nic.in/

output, new orders, inventories, and employment across the region.

Manufacturing conditions in the ASEAN region deteriorate

Declines were reported in each of the seven surveyed countries, with the most significant deterioration in the manufacturing sector of Singapore. Meanwhile, Vietnam, Malaysia, Thailand, and Myanmar recorded back-to-back monthly contractions in March. Manufacturing activity in Indonesia also fell into contraction territory during the month following an expansion in February. Meanwhile, in the Philippines, manufacturing activity contracted after posting a 50.0 no-change reading in the previous month.[63]

Policy Actions by Other Central Banks. On 30 March, the People's Bank of China (PBOC) decided to lower the interest rate on the 7-day reverse repurchase agreements by 20 bps to 2.2 percent from 2.4 percent. The adjustment reflects the intent of the PBOC to relieve pressure on the economy affected by the COVID-19 outbreak. On 20 February, the PBOC also lowered the benchmark one-year loan prime rate by 10 bps to 4.05 percent.

Several central banks have eased their monetary policy settings during the first quarter of 2020

In an earlier-than-scheduled monetary policy meeting on 27 March, the Reserve Bank of India (RBI) decided to cut its policy repo rate by 75 bps to 4.4 percent to mitigate the impact of the COVID-19 outbreak, revive domestic growth and preserve financial stability.

Similarly, in an unscheduled monetary policy meeting on 27 March, Bank of Canada (BOC) lowered its target for the overnight rate by 50 bps to 0.25 percent. The adjustment brings the policy rate to its effective lower bound and is intended to support the Canadian financial system and the economy during the COVID-19 pandemic. BOC reduced the target for the overnight rate thrice in March, with a cumulative reduction of 150 bps.

During a special meeting held on 20 March, Bank of Thailand (BOT) lowered the policy rate by 25 bps to 0.75 percent to reduce the interest burden on borrowers affected by the COVID-19 outbreak and to alleviate liquidity strain in the financial markets. The BOT also reduced the policy rate by 25 bps to 1.0 percent during its 5 February policy meeting as it expects a slower expansion of the Thai economy due to the COVID-19 spread.

During its special meeting on 19 March, the Bank of England (BOE) decided to reduce the bank rate by 15 bps to 0.1 percent to provide support to the economy amid the expected economic disruption brought about by the COVID-19 outbreak. The adjustment came after the BOE's decision to lower the bank rate by 50 bps to 0.25 percent during its 10 March unscheduled monetary policy meeting.

In an unscheduled monetary policy meeting on 19 March 2020, the Reserve Bank of Australia (RBA) decided to lower the cash rate by another 25 bps to 0.25 percent to reduce the economic and financial disruption resulting from the virus. The RBA also announced that it will not increase the cash rate until progress is being made towards full employment and its inflation objective. The RBA had already reduced the cash rate by 25 bps during its scheduled policy meeting on 3 March.

Similarly, on 19 March 2020, Bank Indonesia (BI) reduced the BI 7-day reverse repo rate by 25 bps to 4.5 percent amid prospects of weaker economic activity due to the COVID-19 outbreak. BI intends to retain its accommodative stance to stimulate the domestic economy and step up intervention measures to stabilize the Indonesian Rupiah. On 20 February, BI also lowered the policy rate by 25 bps to 4.75 percent as a pre-emptive measure to maintain domestic economic growth amid the pandemic.

On 19 March, the Central Bank of the Republic of China (Taiwan) lowered the discount rate by 25 bps to 1.125 percent, effective on 20 March. The decision to lower the rate was meant to support business continuity and to caution against the negative impact of significant cross border capital flows amid the COVID-19

[63] Nikkei ASEAN Manufacturing PMI, http://www.markiteconomics.com/

outbreak. The Board also decided to set in place a special accommodation facility that would provide banks with additional NT$200 billion to support lending to SMEs.

On 16 March, the Reserve Bank of New Zealand decided to lower the official cash rate by 75 bps to 0.25 percent as the negative economic implications of the COVID-19 outbreak continue to rise, warranting further monetary stimulus.

During an emergency policy meeting on 16 March 2020, Bank of Korea (BOK) lowered its benchmark interest rate by 50 bps to 0.75 percent, effective 17 March 2020. BOK assessed that further monetary policy accommodation is warranted to ease volatility in the financial markets and reduce the effects of the COVID-19 outbreak on future economic growth and inflation.

On 15 March, the Federal Reserve decided to lower the target range for the federal funds rate by 100 bps to 0-0.25 percent to support the US economy amid the COVID-19 outbreak and promote its employment and price stability objectives. This followed the Fed's decision to lower the target range for the fed funds rate by 50 bps during its unscheduled policy meeting on 3 March.

On 3 March, Bank Negara Malaysia (BNM) decided to reduce the overnight policy rate (OPR) by 25 bps to 2.50 percent. The adjustment in the OPR is intended to support economic activity amid the potential disruptive impact of the COVID-19 pandemic. On 22 January, BNM also lowered the OPR by 25 bps to 2.75 percent as a pre-emptive measure to secure Malaysia's improving growth trajectory amid stable prices.

V. Monetary Policy Developments

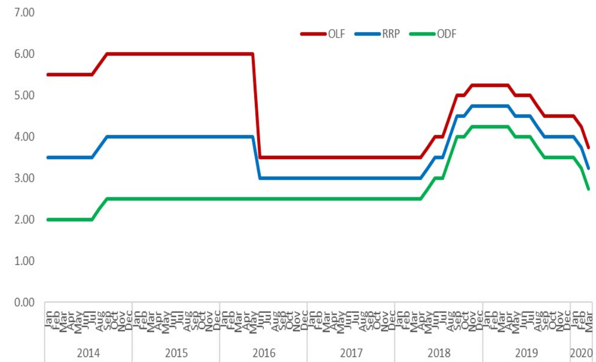
At its monetary policy meeting on 6 February, the BSP reduced the key policy rate by 25 bps to 3.75 percent for the overnight reverse repurchase or RRP facility. The interest rates on the overnight lending and deposit facilities were, likewise, reduced accordingly.

The BSP reduces the policy rate in February 2020…

In deciding on the stance of monetary policy in February, the BSP noted that baseline forecasts indicate a broadly steady path of inflation for 2020 and 2021 during the review period, with average inflation remaining within the target range of 3.0 percent ± 1 percentage point. Inflation expectations also continue to be firmly anchored within the target over the policy horizon.

Meanwhile, the risks to the inflation outlook continue to tilt slightly toward the upside in 2020 and toward the downside in 2021. Upside risks to inflation over the near term emanate mainly from potential upward pressures on food prices owing in part to the African Swine Fever outbreak and tighter international supply of rice. Moreover, there continues to be the burden on the economy posed by the ongoing Taal volcano eruption and the aftermath of typhoon Tisoy. However, uncertainty over trade and economic policies in major economies continue to weigh down on global demand, thus mitigating upward pressures on commodity prices.

Chart 34. BSP Policy Rates
In percent



The BSP also observed that prospects for global economic growth have weakened further amid geopolitical tensions. At the same time, the BSP noted that the spread of COVID-19 could have an adverse impact on economic activity and market sentiment in the coming months.

The BSP concluded, given these considerations, that the manageable inflation environment allowed room for a preemptive reduction in the policy rate to support market confidence. While demand indicators during the review period still point to a firm outlook for the domestic economy, the BSP believes that a policy rate cut would provide additional policy support to ward off the potential spillovers associated with increased external headwinds.

…and thereafter cuts policy rate anew in March 2020

In its 19-March policy meeting, the BSP reduced the key policy rate anew by 50 bps to 3.25 percent for the overnight reverse repurchase or RRP facility. The interest rates on the overnight lending and deposit facilities were also reduced accordingly.

The BSP authorized the time-bound, temporary relaxation of its regulations on compliance reporting by banks, calculation of penalties on required reserves, and single borrower limits. The BSP also approved a temporary reduction in the term spread on rediscounting loans relative to the overnight lending rate to zero. The BSP issued the detailed guidelines on these monetary measures and regulatory forbearance items on 19 March 2020.

In addition, the BSP announced on 24 March the reduction in the reserve requirement (RR) ratios for BSP-supervised financial institutions. The RR cut will ensure sufficient domestic liquidity in support of economic activity amidst the global pandemic due to the COVID-19.

In deciding to reduce the policy rate anew, the BSP noted that baseline forecasts indicate a lower path of inflation for 2020 and 2021, with inflation expectations remaining firmly anchored within the target range of 3.0 percent ± 1 percentage point over the policy horizon. Average inflation is seen to settle at 2.2 percent in 2020 and 2.4 percent in 2021. The latest forecasts are substantially below the February monetary policy meeting projections of 3.0 percent for 2020 and 2.9 percent for 2021 due to lower-than-projected inflation outturns in recent months, a sharp decline in global crude oil prices, and the adverse effects of the COVID-19 outbreak on global and domestic economic activity.

Equally important, the balance of risks to the inflation outlook leans toward the downside for both 2020 and 2021. The uncertainty over the potentially protracted pandemic poses significant downside risks to aggregate demand. The BSP noted that while the enforcement of quarantine measures could help in slowing the spread of the virus, the resulting disruptions to industries and private spending are likely to reduce economic growth in the near term. Moreover, COVID-19 has likewise dampened prospects for the global economy, which could negatively impact tourism and trade, overseas Filipino remittances, and foreign investments.

Given these considerations, the BSP decided that there was a need for a follow-on monetary policy response to address the adverse spillovers associated with the ongoing pandemic. With a manageable inflation environment and stable inflation expectations, the BSP saw enough policy space for an assertive reduction in the policy rate at this juncture to cushion the country's growth momentum and uplift market confidence amid stronger headwinds. The monetary policy easing was also aimed at mitigating the risk of financial sector volatility in light of unfolding global developments by ensuring adequate domestic liquidity and credit in the financial system as well as lowering borrowing costs for affected firms and households.

VI. Inflation Outlook

BSP Inflation Forecasts

The latest baseline forecasts indicate that inflation could settle below the midpoint of the target range for 2020 to 2021. Inflation is projected to remain below the midpoint of the target range throughout 2020 before approaching the midpoint in the latter part of 2021. Inflation is projected to be relatively benign throughout the policy horizon due to the impact of COVID-19 on global demand, domestic economic conditions, and commodity prices.

The forecast path for 2020 and 2021 is lower compared to the outlook presented in the previous report due mainly to the sharp decline in global crude oil prices and the impact of COVID-19 on global and domestic growth.

The risks to the inflation outlook are tilted to the downside for 2020 and 2021. The potential impact of a more disruptive pandemic episode on domestic and global growth prospects along with continued volatility in crude oil prices owing to the weaker global oil demand are the main downside risks to inflation.

Meanwhile, adjustments in utility rates, higher global rice prices, and the impact of African Swine Fever (ASF) on meat prices are the main upside risks to inflation.

Inflation is projected to settle below the midpoint of the target range for 2020 to 2021

Demand Conditions. Domestic growth remained favorable in Q4 2019 with GDP growth accelerating to 6.4 percent in Q4 2019 from 6.0 percent in Q3 2019 and 6.3 percent in Q4 2018. On the expenditure side, the expansion was driven by the double-digit performance of government consumption as well as the robust growth in household spending. On the production side, growth was driven by services and industry sectors particularly public administration and defense, compulsory social security; financial intermediation; and construction.

Looking ahead, domestic growth is expected to slowdown in 2020 due to the ongoing pandemic. The enforcement of the enhanced community quarantine measures has disrupted overall domestic economic activity. In addition, the spillovers from slower global growth, tourism, foreign investments, trade, and OF remittances are expected to further temper domestic economic conditions. However, a U-shaped recovery is expected with growth accelerating once the community quarantine is lifted and the necessary measures intended to stem the spread of the virus are implemented. GDP could also recover more strongly once the fiscal and monetary stimulus gain traction and workers and firms resume operations.

High-frequency real sector indicators also point to weak growth prospects in the near term. The volume of production index for manufacturing in January 2020 remains in negative territory. The composite Purchasing Managers' Index (PMI) also dropped below the 50-point mark as of March 2020, suggesting contraction across all sectors. Moreover, results of the BSP expectations surveys indicate weaker business sentiment and consumer confidence in Q1 2020.

Supply Conditions. Food prices could remain benign over the near term as neutral weather conditions are expected to persist in the first half of 2020, resulting in adequate domestic supply. In addition, the implementation of the price freeze by the Department of Agriculture (DA) and Department of Trade and Industry (DTI) on necessities could temper price pressures on commodity prices. However, production disruptions and logistical bottlenecks could affect the supply of some commodities if the quarantine measures are prolonged.

Food prices are expected to be benign but could be affected by supply disruptions due to measures to address COVID-19

Palay and corn production is projected to decline in Q1 2020 based on the PSA's latest assessment of standing crop estimates due to a decline in harvest areas. *Palay* production is projected to decline by 9.5 percent while corn production could be lower by 1.3 percent in Q1 2020 compared to the same period last year.

In addition, the below-average rainfall conditions have resulted in lower rice production volumes in Thailand. The droughts have caused a decline in harvested areas during the dry season. The US Department of Agriculture (USDA) projects that production in Thailand would settle at 18.5 million tons in 2019-20, which is 9.0 percent lower than the level registered in 2018-19. Similarly, the drought in the Mekong River has affected production in Vietnam. Consequently, export prices of the benchmark 5% broken rice for Thailand and Vietnam rose in Q1 2020. Meanwhile, meat prices in Asia, Europe, and North America have risen because of the rapid spread of African Swine Fever (ASF).

Meanwhile, global crude oil prices declined sharply in Q1 2020 mainly due to concerns on the impact of the pandemic on global demand. Moreover, the sudden surge in global oil supply owing to the price war between Saudi Arabia and Russia has resulted in further downward price pressures. The latest futures prices have shifted into contango wherein prices in the near term are lower than in the long term, which indicates expectations of continued excess global supply.

Output gap could widen in 2020

The balance of demand and supply conditions as captured by the output gap (or the difference between actual and potential output), provides an indication of potential inflationary pressures in the near term.[64]

Based on the Q4 2019 GDP outturn, estimates by the BSP show that the output gap remains broadly neutral and stable relative to the previous quarter. However, the output gap is projected to widen in 2020 with the expected slowdown in economic activity.[65]

Key assumptions used to generate the BSP's inflation forecasts. The BSP's baseline inflation forecasts are based on the following assumptions:

1) BSP's overnight RRP rate at 2.75 percent from April 2020 to December 2021;
2) NG fiscal deficits for 2020 to 2021, which are consistent with the DBCC-approved estimates;
3) Dubai crude oil price assumptions consistent with the trend of futures prices of oil in the international market;
4) Increase in nominal wages consistent with historical wage increases and labor productivity growth;
5) Real GDP growth is endogenously determined; and
6) Foreign exchange rate is endogenously determined through the purchasing power parity and interest rate parity relationships.

Risks to the Inflation Outlook

The risks to the inflation outlook may be presented graphically through a fan chart. The fan chart depicts the probability of different inflation outcomes based on the central projection (corresponding to the baseline forecast of the BSP) and the risks surrounding the inflation outlook.

Compared to the previous inflation report, the latest fan chart shows a lower inflation path. The inflation outlook for 2020 and 2021 is lower compared to the previous report due mainly to the sharp decline in global crude oil prices and the impact of COVID-19 on global and domestic growth.

Inflation path has shifted downward compared to the previous quarter

The BSP's review of current inflation dynamics suggests that the risks surrounding the inflation outlook appear to be on the downside for 2020 and 2021.

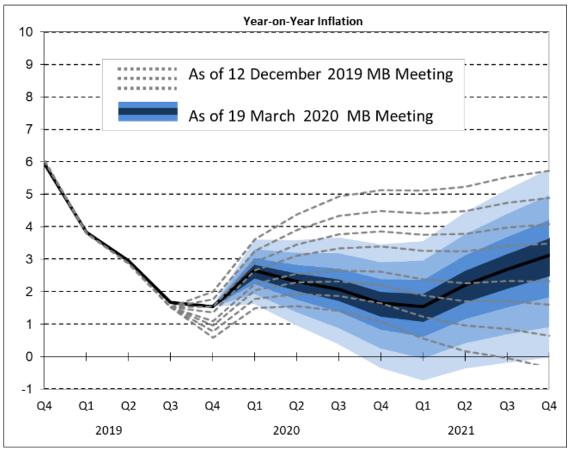
A more disruptive impact of COVID-19 could lead to a deeper slowdown in global and domestic growth prospects. This could lead to a sharper decline in tourist receipts, trade, and remittances. In addition, a prolonged imposition of the enhanced community quarantine in Luzon could further dampen domestic economic activity.

[64] Inflation tends to rise (fall) when demand for goods and services exert pressure on the economy's ability to produce goods and services, i.e., when the output gap is positive (negative).
[65] Based on the seasonally-adjusted GDP growth

The volatility in the global crude oil market could also dampen crude oil prices. Despite the agreement of the Organization of the Petroleum Exporting Countries (OPEC) and its allies to reduce oil production, a weaker global oil demand due to COVID-19 is expected to dominate and could push crude oil prices downwards.

The balance of risks to the inflation outlook significantly leans to the downside for 2020 and 2021

Chart 35. Inflation Projection



Source: BSP estimates

Various petitions for rate adjustments by Meralco and PSALM are considered as upside risks to inflation and have not yet been added to the baseline forecasts. Meralco's petitions include generation and transmission charges, system loss, lifeline subsidy, the December 2013 rate adjustment, which is the subject of Supreme Court temporary restraining order, and the ₱0.65/ kWh adjustment for the January 2014 billing period that is subject to the approval of the Energy Regulatory Commission (ERC). The petitions of PSALM cover adjustments for fuel and foreign exchange costs.

The outbreak of African Swine Fever (ASF) could lead to an uptick in meat prices over the near term. Meat products account for 6.2 percent of the CPI basket, of which 4.8 percent is from fresh or frozen meat and 1.4 percent from canned and processed meat. The outbreak of ASF is expected to lower domestic hog supply and also temper demand. Consequently, consumers could substitute away from pork products, resulting in possible increased demand and higher prices of chicken and beef products. Recent reports indicate that processed meat products have already been contaminated by ASF and that the outbreak has spread to several parts of Mindanao and Luzon as well.

Higher global rice prices present an upside risk on inflation. More than 90.0 percent of the Philippines' rice imports are sourced from Thailand and Vietnam. While prices have remained stable in other exporters like Bangladesh and India, higher demand due to lower export volumes in Thailand and Vietnam could push global prices further. In addition, tariffs from non-ASEAN countries are higher at 50.0 percent compared to rice imports from ASEAN countries.

The fan chart shows the probability of various outcomes for inflation over the forecast horizon. The darkest band depicts the central projection, which corresponds to the BSP's baseline inflation forecast. It covers 25 percent of the probability distribution. Each successive pair of bands is drawn to cover a further 25 percent of probability, until 75 percent of the probability distribution is covered. Lastly, the lightest band covers the lower and upper 90 percent of the probability distribution. The bands widen (i.e., "fan out") as the time frame is extended, indicating increasing uncertainty about outcomes. The band in wire mesh depicts the inflation profile in the previous report.

The shaded area, which measures the range of uncertainty, is based on the forecast errors from the past years. In greater detail, it can be enhanced by adjusting the level of skewness of the downside and upside shocks that could affect the inflationary process over the next two years in order to change the balance of the probability area lying above or below the central projection.

Implications for the Monetary Policy Stance

The BSP lowered the monetary policy interest rate twice in Q1 2020 for a cumulative reduction of 75 bps. In deciding on these follow-on policy actions, the BSP recognized that baseline forecasts indicate a lower path of inflation for 2020 and 2021. Moreover, inflation is projected to be relatively benign throughout the policy horizon due to the impact of COVID-19 on global demand, domestic economic conditions, and commodity prices. Meanwhile, inflation expectations remain well within the target range of 3.0 percent ± 1 percentage point over the policy horizon.

The balance of risks to the inflation outlook are tilted to the downside for 2020 and 2021. Uncertainty over the potential impact of a more disruptive pandemic episode on domestic and global growth prospects along with continued volatility in crude oil prices are the main downside risks to inflation. The BSP noted that with the enforcement of the necessary quarantine measures, the resulting disruptions to industries and private spending are likely to reduce economic growth in the near term. Moreover, the COVID-19 outbreak has likewise dampened prospects for the global economy, which could negatively impact tourism and trade, overseas Filipino remittances, and foreign investments.

Given these considerations, the BSP decided that there was a need for a follow-on monetary policy response to address the adverse spillovers associated with the ongoing pandemic. With a manageable inflation environment and stable inflation expectations, the BSP saw enough policy space for an assertive reduction in the policy rate at this juncture to cushion the country's growth momentum and uplift market confidence amid stronger headwinds. The monetary policy easing was also aimed at mitigating the risk of financial sector volatility in light of unfolding global developments by ensuring adequate domestic liquidity and credit in the financial system as well as lowering borrowing costs for affected firms and households.

Going forward, the BSP emphasized that it will remain data-driven as it considers a range of other supplementary measures that may be required to support non-inflationary and sustainable growth over the medium term. These supplemental actions may include, but are not limited to, recalibrating the interest rate corridor settings; reducing the reserve requirement ratios; suspending the term deposit facility (TDF) auctions; and ensuring access to liquidity-enhancing facilities such as the rediscounting windows. The BSP is prepared to use its full range of monetary instruments and to deploy regulatory relief measures as needed in fulfillment of its price and financial stability mandates.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
2008			
31 Jan 2008	5.00	7.00	The Monetary Board (MB) decided to reduce by 25 bps the BSP's key policy interest rates to 5 percent for the overnight borrowing or reverse repurchase (RRP) facility and 7 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts (SDAs) were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest inflation forecasts indicated that inflation would fall within the 4.0 percent ± 1 percentage point target range in 2008 and the 3.5 ± 1 percentage point target range in 2009.
13 Mar 2008 **24 Apr 2008**	5.00	7.00	The MB decided to keep the BSP's key policy interest rates at 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The MB also decided to implement immediately the following refinements in the SDA facility: (1) the closure of existing windows for the two-, three-, and six-month tenors; and (2) the reduction of the interest rates on the remaining tenors. The interest rates on term RRPs and RPs were also left unchanged.
5 Jun 2008	5.25	7.25	The MB decided to increase by 25 bps the BSP's key policy interest rates to 5.25 percent for the RRP facility and 7.25 percent for RP facility as emerging baseline forecasts indicate a likely breach of the inflation target for 2008 along with indications that supply-driven pressures are beginning to feed into demand. Given the early evidence of second-round effects, the MB recognized the need to act promptly to rein in inflationary expectations. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
17 Jul 2008	5.75	7.75	The MB increased by 50 bps the BSP's key policy interest rates to 5.75 percent for the overnight borrowing or RRP facility and 7.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
28 Aug 2008	6.00	8.00	The MB increased by 25 bps the BSP's key policy interest rates to 6.0 percent for the overnight borrowing or RRP facility and 8.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
6 Oct 2008 **6 Nov 2008**	6.00	8.00	The MB kept the BSP's key policy interest rates unchanged at 6.0 percent for RRP facility and 8.0 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
18 Dec 2008	5.50	7.50	The MB decided to reduce the BSP's key policy interest rates by 50 bps to 5.5 percent for the overnight borrowing or RRP facility and 7.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. This outlook is supported by the downward shift in the balance of risks, following the easing of commodity prices, the moderation in inflation expectations, and the expected slowdown in economic activity.
2009			
29 Jan 2009	5.00	7.00	The MB decided to reduce the BSP's key policy interest rates by another 50 bps to 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. The MB based its decision on the latest inflation outlook which shows inflation falling within the target range for 2009 and 2010. The Board noted that the balance of risks to inflation is tilted to the downside due to the softening prices of commodities, the slowdown in core inflation, significantly lower inflation expectations, and moderating demand.
5 Mar 2009	4.75	6.75	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.75 percent for the overnight borrowing or RRP facility and 6.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Given possible upside risks to inflation, notably the volatility in oil prices and in exchange rates, increases in utility rates, and potential price pressures coming from some agricultural commodities, the MB decided that a more measured adjustment of policy rates was needed.
16 Apr 2009	4.50	6.50	The MB reduced key policy rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility, effective immediately. This rate cut brings the cumulative reduction in the BSP's key policy rates to 150 bps since December last year. The current RRP rate is the lowest since 15 May 1992. Meanwhile, the interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest baseline inflation forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the MB considered that the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.
28 May 2009	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Baseline forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the Monetary Board considered that, on balance, the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
9 Jul 2009	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility, effective immediately. The interest rates on term RRPs, RPs, and SDAs were reduced accordingly. This is the sixth time since December 2008 that the BSP has cut its policy interest rates.
20 Aug 2009 1 Oct 2009 5 Nov 2009 17 Dec 2009	4.00	6.00	The MB kept key policy rates unchanged at 4 percent for the RRP facility and 6 percent for the overnight lending RP facility. The decision to maintain the monetary policy stance comes after a series of policy rate cuts since December 2008 totaling 200 bps and other liquidity enhancing measures.
2010			
28 Jan 2010 11 Mar 2010 22 Apr 2010 3 Jun 2010 15 Jul 2010 26 Aug 2010 7 Oct 2010 18 Nov 2010 29 Dec 2010	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4 percent for the RRP facility and 6 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
2011			
10 Feb 2011	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
24 Mar 2011	4.25	6.25	The MB decided to increase by 25 bps the BSP's key policy interest rates to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. The MB's decision was based on signs of stronger and broadening inflation pressures as well as a further upward shift in the balance of inflation risks. International food and oil prices have continued to escalate due to the combination of sustained strong global demand and supply disruptions and constraints.
5 May 2011	4.50	6.50	The MB decided to increase the BSP's key policy interest rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. Baseline inflation forecasts continue to suggest that the 3-5 percent inflation target for 2011 remains at risk, mainly as a result of expected pressures from oil prices.
16 Jun 2011	4.50	6.50	The MB decided to keep policy rates steady at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board decided to raise the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on Friday, 24 June 2011. The MB's decision to raise the reserve requirement is a preemptive move to counter any additional inflationary pressures from excess liquidity.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
28 Jul 2011	4.50	6.50	The MB maintained the BSP's key policy interest rates at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board increased anew the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on 5 August 2011. The MB's decision to raise the reserve requirement anew is a forward-looking move to better manage liquidity.
8 Sep 2011 **20 Oct 2011** **1 Dec 2011**	4.50	6.50	The MB decided to keep the overnight policy rates (OPR) steady. At the same time, the reserve requirement ratios (RRR) were kept unchanged.
2012			
19 Jan 2012	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB's decision is based on its assessment that the inflation outlook remains comfortably within the target range, with expectations well-anchored and as such, allowed some scope for a reduction in policy rates to help boost economic activity and support market confidence.
1 Mar 2012	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB is of the view that the benign inflation outlook has allowed further scope for a measured reduction in policy rates to support economic activity and reinforce confidence.
19 Apr 2012	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
14 Jun 2012	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that the inflation environment remains manageable. Baseline forecasts continue to track the lower half of the 3-5 percent target range for 2012 and 2013, while inflation expectations remain firmly anchored. At the same time, domestic macroeconomic readings have improved significantly in Q1 2012.
26 Jul 2012	3.75	5.75	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the third time in 2012 that the BSP has cut its policy rates. The MB's decision was based on its assessment that price pressures have been receding, with risks to the inflation outlook slightly skewed to the downside. Baseline forecasts indicate that inflation is likely to settle within the lower half of the 3-5 percent target for 2012 and 2013, as pressures on global commodity prices are seen to continue to abate amid weaker global growth prospects. At the same time, the MB is of the view that prospects for global economic activity are likely to remain weak.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
13 Sep 2012	3.75	5.75	The MB decided to keep the BSP's key policy interest rates steady at 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that the inflation environment remains benign, with the risks to the inflation outlook appearing to be broadly balanced.
25 Oct 2012	3.50	5.50	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the fourth time in 2012 that the BSP has cut its policy rates. The MB's decision was based on its assessment that the inflation environment continued to be benign with latest baseline forecasts indicating that the future inflation path will remain within target for 2012-2014. A rate cut would also be consistent with a symmetric response to the risk of below-target inflation.
13 Dec 2012	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that current monetary settings remained appropriate, as the cumulative 100-bp reduction in policy rates in 2012 continued to work its way through the economy.
2013			
24 Jan 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained accordingly. The reserve requirement ratios were kept steady as well. At the same time, the MB decided to set the interest rates on the SDA facility at 3.00 percent regardless of tenor, effective immediately, consistent with the BSP's continuing efforts to fine-tune the operation of its monetary policy tools.
14 Mar 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Following its previous decision to rationalize the SDA facility in January 2013, the MB further reduced the interest rates on the SDA facility by 50 bps to 2.50 percent across all tenors effective immediately.
25 Apr 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Meanwhile, the SDA rate was further reduced by 50 bps to 2.0 percent across all tenors.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
13 Jun 2013 **25 Jul 2013** **12 Sep 2013** **24 Oct 2013** **12 Dec 2013**	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.
2014			
6 Feb 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.
27 Mar 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirement by one percentage point effective on 11 April 2014.
8 May 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirements for U/KBs and TBs by a further one percentage point effective on 30 May 2014.
19 Jun 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained. The reserve requirement ratios were left unchanged as well. Meanwhile, the MB decided to raise the interest rate on the SDA facility by 25 bps from 2.0 percent to 2.25 percent across all tenors effective immediately.
31 Jul 2014	3.75	5.75	The MB decided to increase the BSP's key policy rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also raised accordingly. The rate on special deposit accounts (SDA) was left unchanged. Meanwhile, the reserve requirement ratios were also kept steady.
11 Sep 2014	4.00	6.00	The MB decided to increase the BSP's key policy rates by 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also raised accordingly. Meanwhile, the reserve requirement ratios were left unchanged.
23 Oct 2014 **11 Dec 2014**	4.00	6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2015			
12 Feb 2015 **26 Mar 2015** **14 May 2015** **25 Jun 2015** **13 Aug 2015** **24 Sep 2015** **12 Nov 2015** **17 Dec 2015**	4.00	6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent): Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2016				
11 Feb 2016 23 Mar 2016 12 May 2016	4.00		6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.
23 Jun 2016 11 Aug 2016 22 Sep 2016 10 Nov 2016 22 Dec 2016	3.00	2.50	3.50	The BSP formally adopted an interest rate corridor (IRC) system as a framework for conducting its monetary operations. The shift to IRC is an operational adjustment and not a change in the monetary policy stance. The IRC is a system for guiding short-term market rates towards the BSP policy interest rate which is the overnight reverse repurchase (RRP) rate. The IRC system consists of the following instruments: standing liquidity facilities, namely, the overnight lending facility (OLF) and the overnight deposit facility (ODF); the overnight RRP facility; and a term deposit auction facility (TDF). The interest rates for the standing liquidity facilities form the upper and lower bound of the corridor while the overnight RRP rate is set at the middle of the corridor. The repurchase (RP) and Special Deposit Account (SDA) windows will be replaced by standing overnight lending and overnight deposit facilities, respectively. Meanwhile, the reverse repurchase (RRP) facility will be modified to a purely overnight RRP. In addition, the term deposit facility (TDF) will serve as the main tool for absorbing liquidity. The interest rates for these facilities will be set as follows starting 3 June 2016: • 3.5 percent in the overnight lending facility (a reduction of the interest rate for the upper bound of the corridor from the current overnight RP rate of 6.0 percent); • 3.0 percent in the overnight RRP rate (an adjustment from the current 4.0 percent); and • 2.5 percent in the overnight deposit facility (no change from the current SDA rate).
2017				
9 Feb 2017 23 Mar 2017 11 May 2017 22 Jun 2017 10 Aug 2017 21 Sep 2017 9 Nov 2017 14 Dec 2017	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight (RRP) facility, 3.5 percent for the overnight lending facility (OLF) and 2.5 percent for the overnight deposit facility (ODF). The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent): Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2018				
8 Feb 2018	**3.00**	**2.50**	**3.50**	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
15 Feb 2018				The reserve requirement ratio was reduced by one (1) percentage point as an operational adjustment to support the BSP's shift toward a more market-based implementation of monetary policy as well as its broad financial market reform agenda. The reduction will apply to the reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions with reserve requirement at twenty (20) percent.
22 Mar 2018	**3.00**	**2.50**	**3.50**	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
10 May 2018	**3.25**	**2.75**	**3.75**	The MB decided to increase the BSP's key policy interest rates by 25 basis points to 3.25 percent for the overnight RRP facility, 3.75 percent for the OLF and 2.75 percent for the ODF.
24 May 2018				The reserve requirement ratio was reduced by one (1) percentage point as part of its medium-term financial market reform agenda to promote a more efficient financial system by lowering intermediation costs. The reduction will apply to those reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions that are currently subject to a reserve requirement of nineteen (19) percent.
20 Jun 2018	**3.50**	**3.00**	**4.00**	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 3.50 percent for the overnight RRP facility, 4.00 percent for the OLF and 3.00 percent for the ODF.
9 Aug 2018	**4.00**	**3.50**	**4.50**	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2018	**4.50**	**4.00**	**5.00**	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
15 Nov 2018	**4.75**	**4.25**	**5.25**	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
13 Dec 2018	**4.75**	**4.25**	**5.25**	The MB decided to maintain the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2019				
7 Feb 2019 **21 Mar 2019**	**4.75**	**4.25**	**5.25**	The MB decided to keep the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
9 May 2019	**4.50**	**4.00**	**5.00**	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
16 May 2019				The MB decided to reduce the reserve requirements by 200 basis points (or 2 percentage points) which shall be implemented according to the following schedule: 100 basis points on 31 May 2019; 50 basis points on 28 Jun 2019; and 50 basis points on 26 Jul 2019. The reduction will apply to those reservable liabilities of universal and commercial banks (U/KBs) that are currently subject to a reserve requirement of eighteen (18) percent.
23 May 2019				The MB complemented the reduction in reserve requirements for universal and commercial banks (U/KBs) with a phased 200-basis-point reduction in the reserve requirements for thrift banks (TBs) and non-bank financial institutions with quasi-banking functions (NBQBs), as well as a 100-basis-point reduction for demand deposits and NOW accounts of rural and cooperative banks on 31 May 2019. Moreover, long-term negotiable certificates of time deposits issued by all banks and NBQBs will have reduced and uniform reserve requirement ratio of 4.0 percent. The reductions on reserve requirements will take effect for U/KBs, TBs, and NBQBs on the reserve weeks beginning 31 May 2019, 28 Jun 2019, and 26 Jul 2019. The lower ratios shall apply to all reservable liabilities except bonds and mortgage/chattel mortgage certificates as the BSP continues to assess the impact of a reduction in the reserve requirements on said instruments.
20 Jun 2019	**4.50**	**4.00**	**5.00**	The MB decided to maintain the BSP's key policy interest rates at 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
8 Aug 2019	**4.25**	**3.75**	**4.75**	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.25 percent for the overnight RRP facility, 4.75 percent for the OLF and 3.75 percent for the ODF.
26 Sep 2019	**4.00**	**3.50**	**4.50**	The MB decided to cut the BSP's key policy interest rates by 25 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2019				The MB decided to reduce the reserve requirements for U/KBs, TBs, and RBs by 100 bps (or one percentage point). The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks. The reserve requirement of U/KBs was reduced from 16 percent to 15 percent, TBs from 6 percent to 5 percent, and RBs from 4 percent to 3 percent. The reduction will be effective on the first day of the first reserve week of November 2019.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
2019				
24 Oct 2019				The MB decided to reduce the reserve requirements for U/KBs and TBs by 100 bps (or one percentage point). The MB complemented the move with a reduction in the RRs for NBQBs. The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks and NBQBs. The reserve requirement of U/KBs was reduced from 15 percent to 14 percent, TBs from 5 percent to 4 percent, and NBQBs from 16 percent to 14 percent. The reduction will be effective on the first day of the first reserve week of December 2019.
14 Nov 2019	**4.00**	**3.50**	**4.50**	The MB decided to maintain the BSP's key policy interest rate at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
12 Dec 2019	**4.00**	**3.50**	**4.50**	The MB decided to maintain the BSP's key policy interest rates at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
2020				
6 Feb 2020	**3.75**	**3.25**	**4.25**	The MB decided to cut the key policy interest rate by 25 bps to 3.75 percent. The interest rates on the OLF and ODF were reduced to 4.25 percent and 3.25 percent, respectively.
19 Mar 2020	**3.25**	**3.75**	**2.75**	The MB decided to cut the key policy interest rate by 50 bps to 3.25 percent, effective 20 March 2020. The interest rates on the OLF and ODF were reduced to 3.75 percent and 2.75 percent, respectively.
24 Mar 2020				The MB announced a 200-bp reduction in the RR ratio of reservable liabilities of universal and commercial banks (U/KBs) effective 3 April 2020. This puts RRR of U/KBs to 12 percent. The RR cut is intended to calm the markets and to encourage banks to continue lending to both retail and corporate sectors. This will ensure sufficient domestic liquidity in support of economic activity amidst the global pandemic due to the COVID-19.

The *BSP Inflation Report* is published every quarter by the Bangko Sentral ng Pilipinas. The report is available as a complete document in pdf format, together with other general information about inflation targeting and the monetary policy of the BSP, on the BSP's website:

www.bsp.gov.ph/monetary/inflation.asp

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