PHILIPPINES

LIMITED SLOWDOWN IN ECONOMIC GROWTH IN 2023

The government of the Philippines maintained health restrictions linked to the pandemic for longer than the average period in emerging countries, with some regions still under lockdown until April 2022. The rebound in activity is not yet finished, and the strength of consumer spending, still supported by remittances, should help to offset the effects of higher inflation and the slowdown in global growth. Economic growth is expected to slow in 2023, but should remain solid. However, the after-effects from the crisis and health measures are weighing on the medium-term outlook.

DYNAMIC RECOVERY IN 2022

Strong real GDP growth in 2022 (estimated at around 8%, after a decline of 9.5% in 2020 and growth of 5.7% in 2021) can in particular be explained by a recovery in post-Covid activity that was later than in other countries in the region. After a stricter and longer lockdown in the Philippines (some regions remained under lockdown until April 2022), the wave of "Omicron" infections in 2022 was less severe, particularly as the vaccination rate was much higher than initially anticipated.

During the first three quarters of 2022, consumer spending and private investment recorded very dynamic growth rates (almost 9% and 12% respectively, on average and year-on-year). Despite still relatively strict health restrictions in 2022 (schools were only reopened to students in September 2022), the services sector contributed significantly to growth in the first three quarters. The return of tourists made a notable contribution to the vitality of the sector. In total there were over 2 million arrivals recorded in 2022, or around 15 times the number recorded in 2021. However, the number of tourists remains well below the pre-Covid level (over 8 million arrivals in 2019). It may take several years to reach this level again. In Q3 2022, GDP was 10% lower than in the last quarter of 2019.

Moreover, the unemployment rate has fallen significantly in recent months, recording a historic low of 4.2% in November. That said, according to the Central Bank, the low unemployment rate is mainly due to an increase in informal work.

The outlook for the next two years remains relatively favourable. Economic growth is expected to be around 6% in 2023, before accelerating again in 2024 and reaching a level close to the growth potential estimated by the IMF (6.5%). Consumer spending should continue to be sustained, despite the persistent inflation. Transfers from foreign workers will continue to support private consumption. In current dollar terms, they rose by more than 3% in 2022. Expressed as a percentage of GDP, transfers have remained broadly stable at around 8% over the past three years.

At the same time, the slowdown in global growth will impact on the export sector, despite the "shock absorber" effect of the return of tourists. That said, the effect on growth is expected to be less pronounced than in other countries in the region, given the lower degree of openness of the economy.

FORECASTS

	2020	2021	2022e	2023e	2024e
Real GDP growth (%)	-9.5	5.7	7.8	6.0	6.5
Inflation (CPI, year average, %)	2.4	3.9	5.8	4.8	3.5
Government balance / GDP (%)	-5.8	-4.6	-3.5	-3.2	-3.1
National government debt / GDP (%)	51.6	57.0	60.9	61.0	61.2
Current account balance / GDP (%)	3.2	-1.5	-5.0	-4.1	-3.4
External debt / GDP (%)	27.2	27.0	26.6	26.4	25.8
Forex reserves (USD bn)	110.0	108.8	94.1	88.7	83.9
Forex reserves, in months of imports	12.3	9.6	8.8	8.5	7.8

e: ESTIMATE & FORECASTS

TABLE 1 SOURCE: BNP PARIBAS ECONOMIC RESEARCH

PHILIPPINES: REMITTANCES

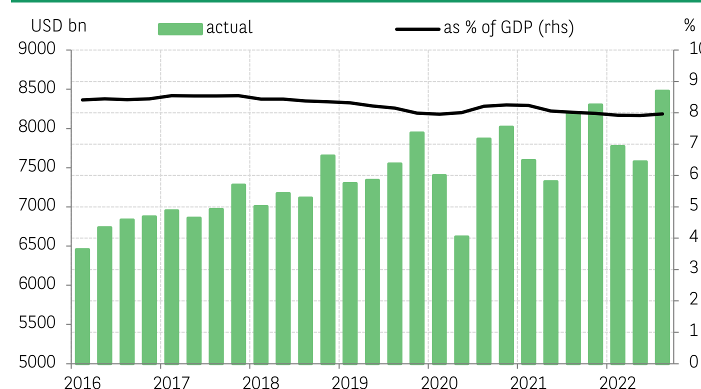

CHART 1 SOURCE: CENTRAL BANK, CEIC, BNP PARIBAS

PERSISTENCE OF INFLATION

Consumer price inflation has steadily accelerated since March 2022, reaching 8.1% year-on-year in December and averaging 5.8% in 2022. In its latest estimates, the Central Bank expects the inflation rate to remain high (close to 5% in 2023), due to strong domestic demand pressures (in the context of high commodity prices) and the continued high price of fertilisers. Since May, the Central Bank has steadily raised its interest rate (to 5.5% in December, a cumulative increase of 350 basis points). Monetary policy could tighten still further in the coming quarters. Rate differentials with the United States narrowed in recent months, causing outflows of capital and a depreciation of the exchange rate (the peso depreciated by around 15% against the USD over the first ten months of the year). The exchange rate reached PHP 59/USD at the beginning of October, despite interventions by the Central Bank (which however did reduce exchange rate volatility). The peso has stabilised around PHP 55/USD since the beginning of December.

Other interventions on the foreign exchange market are possible in the short term. The Governor of the Central Bank has stated on several occasions that the Central Bank is not aiming for a particular level on the exchange rate and remains focused on its mandate to maintain price stability. However, the Minister of Finance has stated that the government would «not allow the exchange rate to breach the PHP 60/USD level" and that around USD 10bn of forex reserves (which were estimated at USD 96bn in December) could be used for this purpose.

The final decision, however, lies with the monetary policy council of the Central Bank, of which the Minister is a member.

FISCAL CONSOLIDATION CONTINUES

The government of the Philippines has taken advantage of the fiscal room for manoeuvre which it had in 2020 and 2021 to support the economy. The public deficit stood at 5.8% of GDP in 2020, and 4.6% in 2021, while on average it was less than 1% between 2015 and 2019. In the context of stronger growth, the public deficit reduced to 3.5% of GDP in 2022.

At the same time, government debt increased sharply, from 37% of GDP in 2019 to 60% of GDP at the end of 2022. That said, the risks surrounding a possible slippage in the public finances have not increased significantly. On the one hand, the structure of the debt remained favourable: despite the rapid increase in debt, the share of fiscal revenues allocated to interest payments remained moderate (at a little under 10% in Q3 2022, while on average it represented 8.5% in 2019), and maturities remained long. The proportion of debt denominated in foreign currency remains relatively high, at around 33%, but has been falling continuously for almost 15 years and the Philippines government has been able to obtain finance easily on the local market, at relatively low interest rates. All these elements illustrate the effectiveness of the macroeconomic policies implemented over the past decade, and the strength of the Philippine fundamentals despite the economic crisis.

Moreover, President Marcos Jr., who was elected last May, has confirmed his intention to continue the policy of consolidation announced by the previous government. Shortly after taking up his post, the new Minister of Finance announced a medium-term plan, structured around three main objectives: to reduce debt to below 60% of GDP by 2025, to get the deficit down below 3% of GDP by 2028 and to maintain a pace of growth in infrastructure spending above the rate of growth in GDP.

Several proposals to improve the collection of revenues have also been announced, such as the expansion of the tax base for property taxes, as well as the introduction of new taxes on digital consumption, or the consumption of single-use plastic bags. On the basis of the measures announced, public investment (apart from infrastructure expenditure) could decrease. That being said, the numerous public-private partnership projects initiated by the previous government, and continued by the current one, could partially replace public investment, and contribute more to the revenues than was expected.

All in all, in the context of a limited slowdown in economic growth, fiscal consolidation is expected to continue over the next two years, and the objectives announced by the government for reducing debt are likely to be maintained.

PHILIPPINES: FX RESERVES AND EXCHANGE RATE

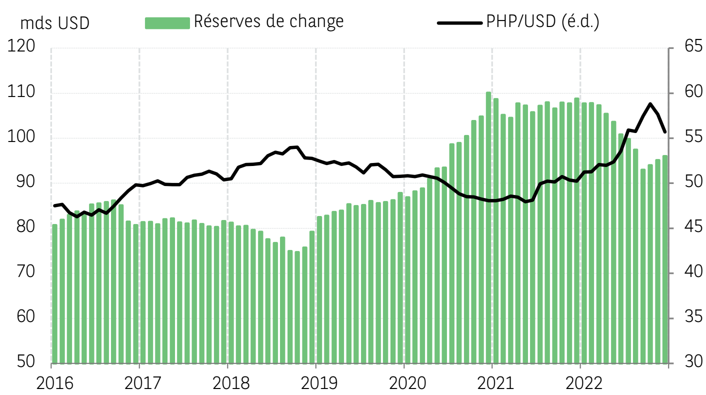

CHART 2 SOURCE: CENTRAL BANK, BNP PARIBAS

FRAGILITY RELATED TO THE PANDEMIC

Over the medium term, the forecasts for growth remain relatively high: according to the IMF, the GDP growth rate should be close to 6.5% over the next five years. However, the scale and the duration of the restrictions imposed in the country during the health crisis have caused many fragilities (increased poverty rate, increased use of undeclared work, reduction in the quality of education) which have partially erased the progress seen over the previous decade, and which are weighing on the potential for growth. Several avenues of reform have been announced by the new government, including a plan to encourage a return to school and to improve the level of education (Basic Education Development Plan 2030).

Hélène DROUOT
helene.drouot@bnpparibas.com
Article completed on 12 January 2023