



The Economy Soars, Grows by 6.9% in First Quarter 2007

The domestic economy grew by 6.9 percent in the first quarter of 2007, its fastest rate in the last 17 years. It was a big leap from last year's first quarter gross domestic product (GDP) growth rate of 5.7 percent, and surpassed the government's earlier forecast of 5.3 percent to 6.1 percent. The surge in the growth of transport, retail trade and mining as well as the government's pump priming activities propped up the GDP growth.

OFW remittances continued its inflow, posting a hefty growth of 14.0 percent during the quarter compared to last year's 3.4 percent. However, the net factor income from abroad was pulled down by the decline in the property income by 7.1 percent and the increase in the property expense by 25.7 percent. As a result, gross national product (GNP) growth was 0.3 percentage point lower than the GDP 6.6 percent.

Production Side

Services sector still drives growth. The services sector remained as the linchpin of the economy in the first quarter of 2007, expanding by a robust 9.1 percent. The major contributors in the sector's growth were transportation, communication and storage, finance; and private services.

Transport and storage went up by 8.8 percent, from -0.3 percent last year. There was a strong demand for motor vehicles, whose sales grew by 15 percent in the first quarter of the year. Election activities, likewise, increased the demand for all means of transportation.

Finance continued to post a double-digit growth, albeit slightly lower at 13.4 percent. Banks' growth decelerated to 8.1 percent after posting a 19.8 percent growth in the first quarter of last year. This was due to the decline in the interest incomes of banks. Non-banks and insurance, in contrast, posted a vigorous growth of 17.2 percent and 33.9 percent, respectively, a big turnaround from the measly 0.6 percent and 2.0 percent growth rates in the same period in 2006. Non-banks benefited from the trading gains

Table 1
First Quarter 2007 GDP Growth, by Industry and Expenditure
(at constant prices, in %)

Particular	Q1	
	2006	2007
<i>By industry</i>		
Agriculture, fishery & forestry	4.1	4.2
Agriculture & fishery	4.1	4.1
forestry	(9.2)	25.6
Industry	5.3	5.3
Mining & quarrying	1.8	11.0
Manufacturing	5.0	4.6
Construction	10.7	8.6
Electricity, gas & water	3.9	4.1
Services	6.7	9.1
Transportation, comm & services	6.9	9.6
Trade	5.3	9.1
Finance	14.6	13.4
Ownership of dwelling & real estate	3.4	5.4
Private services	7.7	8.9
Government services	3.7	7.1
<i>By expenditure</i>		
Personal Consumption	5.3	5.9
Government Consumption	7.6	13.1
Capital Formation	0.3	0.6
Fixed capital	2.4	2.7
Construction	8.0	7.3
Durable equipment	(3.2)	(0.4)
Breeding stock & orchard dev't	(0.7)	2.2
Changes in stocks		
Exports	13.0	9.1
Merchandise exports	11.4	10.3
Non-factor services	21.2	3.6
Imports	0.7	(2.5)
Merchandise imports	0.1	(3.4)
Non-factor Services	10.7	11.6
GDP	5.7	6.9

Source: National Statistical Coordination Board

Table 2
Growth of Transport, Communication and Storage
First Quarter of 2007 (at constant prices, in %)

Particular	growth		contribution to growth	
	Q1			
	2006	2007	2006	2007
Transport & storage	(0.3)	8.8	(0.1)	3.8
land	(0.8)	10.0	(0.1)	7.1
water	(1.4)	1.3	(0.1)	0.1
air	5.7	7.3	0.2	0.3
storage & services incidental transport	1.3	8.0	0.2	1.3
Communication	13.1	10.1	7.4	5.8

Source: National Statistical Coordination Board

in stock market and mutual funds while insurance's growth was attributed to the higher premiums collected from life insurance.

Private services also picked up by 8.9 percent in the first quarter of the year, an improvement from last year's 7.7 percent. The business subsector, which accounts for business process outsourcing (BPOs) was the biggest contributor to the sector's growth (3.3 percentage points), followed by personal services (1.8 percentage points), and hotel and restaurants (1.4 percentage points). According to industry players, prospects on BPOs remain bright as the industry has already started to shift to a higher form of BPO known as knowledge process outsourcing or KPO. Unlike the low-value BPOs, KPOs deal in domain-based processes and business expertise such as valuation, research, investment, patent filing, legal and insurance claims, medical diagnoses and reports, among others.

Also posting a higher growth in the first quarter was the ownership of dwelling and real estate sector (ODRE), which grew by 5.4 percent from last year's 3.4 percent. ODRE's real property sector soared to 18.6 percent in the first quarter of the year from 4.9 percent last year, reflecting the expansion of existing malls, as well as the increase in demand for office space, mostly from BPO companies. The high demand for subdivision lots and high-rise condominium units, fueled by real estate investments of OFWs, also contributed to the sector's growth.

Subdued industry. Industry remained unfazed as it grew by 5.3 percent during the period. Mining and quarrying rebounded from its measly first quarter growth of 1.8 percent in 2006 to 11.0 percent in 2007, as world metal prices continued to soar and investments in mining poured in. Manufacturing slightly decelerated in the first quarter from 5.0 percent in 2006 to 4.6 percent in 2007, though it was still the biggest contributor to industry's growth. Manufacturing's growth was spurred by the higher growth of food manufactures, and furniture and fixtures, which were likely driven by election spending.

Construction continued to post a positive growth rate although it decelerated to 8.6 percent in the first quarter of this year, from the previous year's 10.6 percent. Electricity, gas and water utilities posted a higher growth rate of 4.1 percent from 3.9 percent a year ago.

Moderate growth in agriculture. Agriculture hardly improved, growing by only 4.2 percent in 2007 from 4.1 percent in 2006, as it was still reeling from the after effects of the super typhoons that ravaged the country last year. Palay, corn and banana performed positively in the first quarter of 2007 but on a decelerated pace. Coconut, including copra, posted a negative growth of 4.5 percent in the first quarter of 2007, from a positive 2.5 percent the previous year. Livestock consistently grew by 2.2 percent while poultry recovered from its negative growth of 3.8 percent in the first quarter of the previous year to positive growth of 2.3 percent in 2007.

The fishery sector grew from 4.9 percent in the first quarter of 2006 to 8.7 percent this year. While aquaculture production was not as strong as in the

Table 3
Top Five Highest Growing, Manufacturing Sectors
First Quarter 2007 (at constant prices, in %)

Particular	growth		contribution to growth	
	Q1			
	2006	2007	2006	2007
Food manufactures	5.2	7.7	2.3	3.5
Furniture and fixtures	(2.8)	38.7	(0.0)	0.7
Chemical & chemical prod.	(1.8)	6.5	(0.1)	0.3
Non-metallic mineral prod.	(3.5)	15.7	(0.1)	0.3
Basic metal industries	11.4	9.4	0.3	0.3

Source: National Statistical Coordination Board

Table 4
Growth Rates of Agriculture Sectors
First Quarter 2007 (at constant prices, in%)

Particular	Q1	
	2006	2007
Agriculture	3.9	2.8
Palay	6.9	1.7
Corn	22.1	11.4
Coconut including copra	2.5	(4.5)
Sugarcane	1.5	(0.4)
Banana	12.9	5.4
Other crops	2.2	3.0
Livestock	2.2	2.2
Poultry	(3.8)	2.3
Agricultural activities & services	3.7	4.5
Fishery	4.9	8.7
Forestry	(9.2)	25.6
Gross value-added in AFF	4.1	4.2

Source: National Statistical Coordination Board

previous year, municipal fishery sustained the uptrend in production. Commercial fishery also rebounded.

Expenditure Side

Consumption, still on its upward trend. The continued surge in OFW remittances, coupled with election spending, pushed up private consumption by 5.9 percent in the first quarter, from last year's 5.3 percent. OFW inflows rose sharply by 17.7 percent during the period compared to 11.8 percent last year. Consumption spending remained high in the face of a benign inflation that averaged 2.9 percent in the first quarter of the year.

Similarly, government spending registered a higher growth, from 7.6 percent in the first quarter of 2006 to 13.1 percent in 2007. The uptick is largely attributed to the increase in government services which grew by 7.1 percent, the highest since a decade ago.

Investment. While foreign direct investments registered higher growth rates, domestic investments remained weak, slightly improving from 0.3 percent in the first quarter of 2006 to 0.6 percent in 2007. Durable equipment improved, although still negative, from -0.07 percent in the first quarter of 2006 to -0.04 percent this year. Construction grew at a slower pace, by 7.3

Highlights of Selected Economies' Growth in Q1 2007

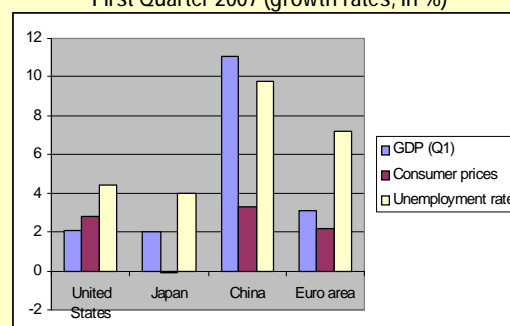
United States. The economy slowed down in the first quarter of the year, growing by a mere 0.6 percent at an annual rate. The declines in homebuilding and firm inventories, anemic exports, and weak government spending dragged down growth. Inflation rose by 3.6 percent in the first quarter. Unemployment slightly declined from 4.5 percent in February to 4.4 percent in March.

Euro Area. The euro-area economy continues to expand, recording a 3.0% growth in the first quarter, boosted by the rising confidence of businesses and consumers. Germany's industrial production accelerated by 7.7 percent in the first quarter, driving the country's boom. Inflation is still on the European Central Bank's target of just under 2 percent as consumer prices posted an increase of merely 1.9 percent in the first quarter. Unemployment rate slightly declined in March to 7.2 percent from 7.3 percent in February. France's unemployment rate decreased to 8.3 percent, the lowest since 1983. Germany's unemployment rate remained at 9.2 percent in April. The euro area posted a €7.4 billion trade surplus in March 2007, with exports up by 1.2 percent and imports down by 2.6 percent.

Japan. Output growth for the first quarter was pegged at 2.0 percent. Industrial output declined by 0.6 percent in March, but was still higher by 1.6 percent over the year. Inflation rate stayed in the negative as consumer prices fell by 0.1 percent in the year to March, vis a vis the 0.2 percent recorded in the year to February. In view of the weaker-than-expected inflationary pressures, the Bank of Japan has left monetary policy unchanged. Unemployment was down to just 4 percent.

China. The Chinese economy grew at a rapid pace of 11.1 percent in the first quarter of this year, fueled by the manufacturing boom. In advance of its strategic deal with the US, monetary authorities not only tightened its policy but also tinkered with its currency regime. The People's Bank of China raised interest rates and widened the daily band within which the yuan can move against the US dollar from 0.3 percent up or down to 0.5 percent. Consumer prices rose by 3.3 percent in March from 2.7 percent in February. Trade surplus in the first quarter, at US\$46.6 billion, was still twice as big as in the same period last year. A 9-percent drop in Chinese share prices in late February triggered a brief global sell-off. But *The Economist* says that China's economy may be less vulnerable to a bursting of the stock market bubble. Its stock market is still relatively small, so price movements—up or down—have less impact on spending than elsewhere. In addition, only 7 percent of the population own shares. The total value of tradable shares is only 25 percent of GDP and a large part of this is actually held by state firms and government agencies.

Growth Rates of Output, Prices & Jobs of Selected Economies
First Quarter 2007 (growth rates, in %)



Source of raw data: *The Economist*

Note: The available unemployment data for China are 2006 figures; US, Japan, and the Euro area are as of March 2007.

Table 5
Top 5 Exports, Growth Rates
First Quarter 2006 & 2007 (at constant prices, in %)

Particular	Q1	
	2006	2007
Finished electrical machinery	53.2	52.8
Cathodes & section of cathodes, of refined copper	27.8	58.2
Semiconductors & electronic microcircuits	14.1	2.5
Transmission apparatus	103.1	145.3
Copper concentrates	74.3	65.9

Source: National Statistical Coordination Board

Table 6
Top 5 Imports, Growth Rates
First Quarter 2007 (at constant prices, in %)

Particular	Q1	
	2006	2007
Manufactures of metals	33.6	71.0
Feeding stuff	33.6	21.4
Machinery other than electrical machinery	(4.6)	5.8
Transport equipment	24.2	13.0

Source: National Statistical Coordination Board

percent, compared to 8.0 percent in the first quarter of the previous year. Public construction went down to 16.9 percent in the first quarter of the year, from 36.5 percent in the first quarter of last year while private construction rebounded from -3.2 percent last year to 2.0 percent this year.

Exports. Despite the strong peso, merchandise exports still grew by 10.3 percent, although slightly lower from last year's 11.4 percent. The higher demand for high-tech gadgets and the rebound in prepared tuna supported export growth. According to the Department of Trade and Industry (DTI), non fiscal measures have been put in place to temper the effect of the strong peso on exports. These include diversifying exports, improving regulatory framework, and creating a 'special hedging facility' for small and medium exporters.

Imports. From an already weak growth of 0.1 percent a year ago, imports further decelerated to -3.4 percent in the first quarter of the year. The poor performance of imports was due to the declines in cereals and cereal products; mineral fuels, lubricants and related materials; textile fibers; base metals; and electrical machinery.

Other GDP Boosters

Other positive economic conditions propped up the first quarter growth. The 91-day T-bill rate eased to an average of 3.149 percent in the first quarter of the year, lower than 5.031 percent in the same period a year ago. The peso continued to be strong, averaging PhP48.60 in the first quarter of 2007 compare to PhP51.88 in the same period last year.

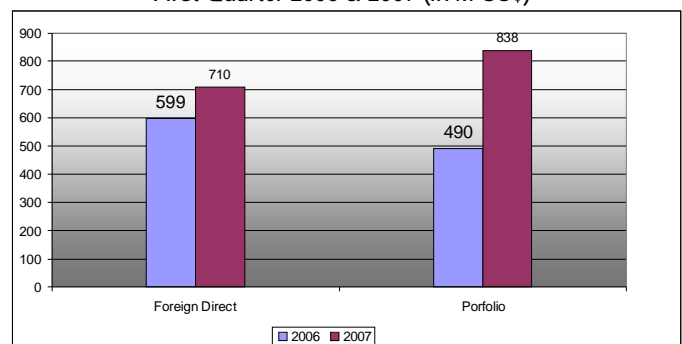
Likewise, foreign direct and portfolio investments remained upbeat. Foreign direct investments posted a net inflow of US\$48 million in March 2007, bringing the cumulative three-month level to US\$710 million, or an 18.5 percent year-on-year growth. Net portfolio investments for the first quarter of the year stood at US\$838-million, a 71-percent increase from the same period in 2006.

On the labor front, the National Statistics Office (NSO) reported that unemployment fell to 7.4 percent in April 2007 from 8.2 percent a year ago. Underemployment fell more steeply to 18.9 percent from 25.4 percent a year ago.

Slipping Fiscal Position

Investors, however, expressed their concerns on the recent fiscal data and warn the government of a possible backslide in its fiscal reforms. The national government in the first quarter of 2007 posted a revenue shortfall of P52.0 billion, higher than the P45.8 billion ceiling programmed for the period. The wider deficit is mainly attributed to

Figure 1
Foreign Direct & Portfolio Investments
First Quarter 2006 & 2007 (in M US\$)



Source: Bangko Sentral ng Pilipinas

Table 7
National Government Cash Budget Performance
First Quarter 2007 (in M PhP)

Particular	Jan 1 - Mar 31		Difference
	Programmed	Actual	
Revenues - schedule 1	255,811	237,303	(18,508)
Bureau of Internal Revenue	155,165	143,108	(12,057)
Bureau of Customs	46,886	40,221	(6,665)
Bureau of the Treasury	15,159	14,100	(1,059)
Others	38,601	39,874	1,273
Expenditures - schedule 2	301,648	289,271	(12,377)
Other NG expenditure account	163,896	140,175	(23,721)
Interest payments - schedule 2	94,255	89,149	(5,106)
Allotment to LGUs	36,788	51,609	14,821
Tax expenditures	2,056	391	n.a.
Net lending --schedule 3	2,766	1,791	(975)
Equity --schedule 3	30	112	82
Subsidy -- schedule 3	1,857	6,044	4,187

Source: Bureau of the Treasury

the P18.5-billion shortfall in tax collections during the said period. The country's tax effort dropped to 12.2 percent in the first quarter from 13 percent in the same period a year ago. Meanwhile, the government restrained its spending as it spent P12.4 billion less than programmed.

The E(lection) factor

Do elections affect the macroeconomy? According to the National Economic and Development Authority, at least for the first three months of the year, election-related spending did have a positive, albeit, minimal, economic impact. Election-related activities contributed 0.34 percentage points to the gross domestic product (GDP) in the first quarter of 2007. Among the components in the GDP equation, personal consumption expenditure (PCE) appears to have been the most affected, although a significant increase in government spending was also noted.

Electoral Spending and Higher PCE

According to the Omnibus Election Code, a candidate running for senator, congressman, governor or mayor under a political party can spend only P3 per registered voter while an independent candidate is allowed to spend P5. However, this limit is often breached.¹ The Institute

¹ For instance, according to Transparency and Accountability Network (TAN), in 2004 in Quezon City, a candidate running for mayor spent as much P8 per head.

Table 8
Estimated Amount Needed to Mount
A Decent Election Campaign (in M PhP)

Kind of Campaign	Estimated Amount
Senatorial	PhP 150 -PhP500
Congressional	PhP 3 -PhP 100
Gubernatorial	PhP 5 -PhP 150
Mayoral	PhP 1 -PhP 100

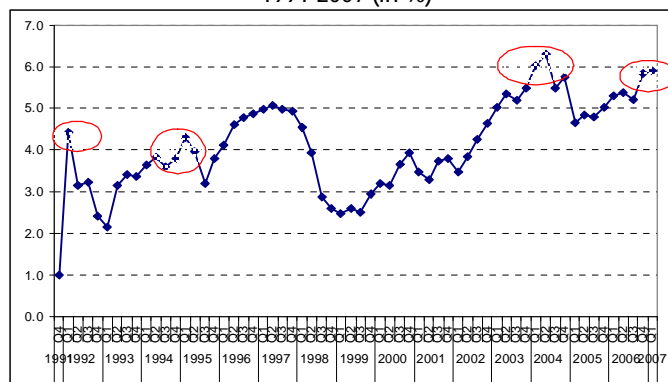
Source: Campaign Financing and Corruption, IPER.

of Political and Economic Reforms(IPER) estimates that nowadays, a candidate for an elective position will have to spend anywhere between P100 million to P500 million to mount a decent campaign.

As per COMELEC tally, there were more than 17,000 national and local posts up for grabs in the last May 2007 elections. This includes 12 vacant posts in the Senate, 219 positions in the House of Representatives, as well as gubernatorial and mayoral posts in the country's 81 provinces, 118 cities and 1,510 municipalities.² There were 36 senatorial candidates, and assuming that at least two people were vying for the rest of the positions, and the low-end range of IPER's campaign fund estimates were used, then, approximately, P10.8 billion of additional money was pumped into the economy. If the middle range of IPER's estimates were used, the amount shoots up to P211 billion, or nearly thrice the total EVAT collections in 2006.

From the political ads alone, approximately 2.8 billion pesos was spent by the candidates in the run up to the May election, up by 43.0 percent from

Figure 2
Personal Consumption Expenditure Growth Rates,
1991-2007 (in %)



Source: National Statistical Coordination Board

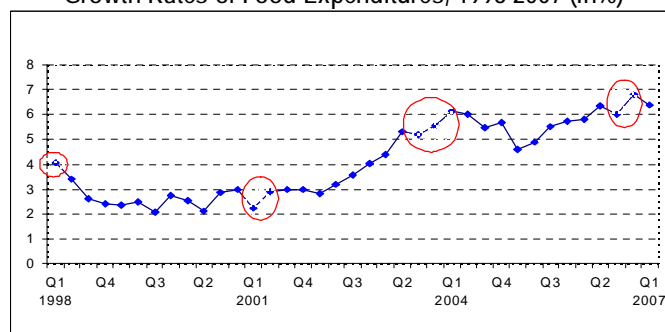
² "Golden Opportunity: The Lucrative Business of Elections", *Businessworld*, April 30, 2007

Table 9
Campaign Expenditures Totals, 2004 vs 2007 (in '000)

Period	Grand Total	Television			Newspapers			Radio		
		PhP	Number	Secs	PhP	Number	Col/Cms	PhP	Number	Secs
Y2004	1,959,331	1,405,668	16,120	448,230	23,593	762	75,862	530,070	171,844	5,010,060
Feb 2004	173,580	149,794	1,138	35,400	1,830	48	4,223	21,955	6,921	197,475
Mar 2004	413,671	332,167	3,599	113,055	923	28	2,508	80,581	26,144	754,965
Apr 2004	774,284	488,278	6,363	171,750	6,031	213	19,174	279,975	89,379	2,597,385
May 2004	597,796	435,429	5,020	128,025	14,808	473	49,957	147,559	49,400	1,460,235
Y2007 *	2,795,453	2,250,685	10,426	247,540	37,569	1,336	111,346	507,199	112,589	3,015,435
Feb 2007	314,853	278,834	1,262	32,230	3,113	75	9,223	32,906	5,116	128,910
Mar 2007	673,676	512,087	2,240	55,290	3,980	159	12,909	157,610	31,765	855,630
Apr 2007	1,023,403	695,968	3,144	71,670	10,752	418	33,008	316,682	75,708	2,030,895
May 2007	783,521	763,796	3,780	88,350	19,724	684	56,206	0	0	0

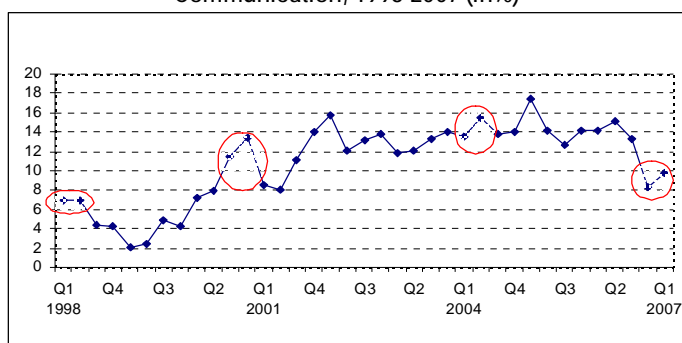
Source: Transparency and Accountability Network

Figure 3
Growth Rates of Food Expenditures, 1998-2007 (in%)



Source: National Statistical Coordination Board

Figure 4
Growth Rates of Expenditures on Transportation and Communication, 1998-2007 (in%)



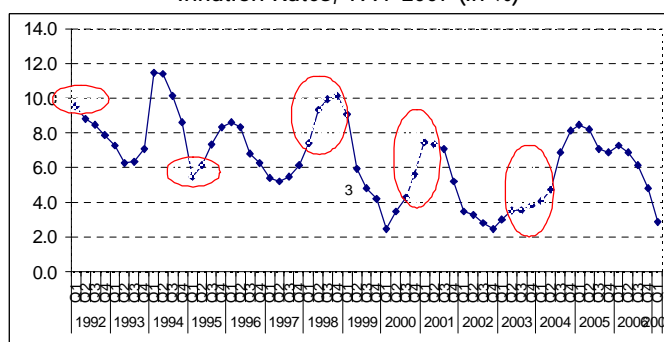
Source: National Statistical Coordination Board

2004. Bulk of the expenses went to advertisements aired on television (80.5%), where a 30-second ad reportedly cost between P130,000 to P300,000.

The temporary spike in income brought by election-related spending is manifested in the increase in PCE. Data shows that in the last 16 years, except in the post-crisis election years of 1998 and

2001, PCE usually goes up prior to and/or during election quarters. Although the increase in PCE can be attributed to other factors, anecdotal evidence suggests that as candidates attend to their campaign sorties, downstream businesses, particularly those related to food, beverages as well as transport and communication, benefit substantially.

Figure 5
Inflation Rates, 1997-2007 (in %)



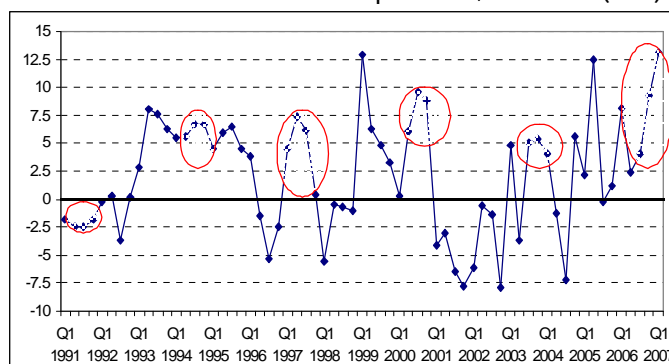
Source: National Statistics Office

With the economy being awash with money, upticks in the inflation rate have been observed in the quarters before or during elections.³ However, prior to May 2007, inflation remained tempered, falling even from the rates it posted in the previous quarters.

³This, however, can also be attributed to other factors other than the elections.

Figure 6

Growth Rates of Government Expenditure, 1998-2007 (in %)



Source: National Statistical Coordination Board

Gov't spending highest since 1990

According to Nordhaus (1975), in order to appear competent and win votes, incumbent politicians usually resort to the manipulation of policy tools, both monetary and fiscal, to stimulate the economy before an election. However, in countries like the Philippines where politicians are severely constrained in using monetary policies, pump-priming the economy is usually done by increasing government spending.

A simple trend analysis of the growth of government spending in the Philippines would suggest that there may be a pattern of pre-electoral government pump-priming in the country. This usually occurs in the last four quarters before the elections, after which a dip in public spending is observed, normally in the first and second quarters of the year as the election ban on public infrastructure spending sets in.

Perhaps it was because of the improved fiscal position, but the government's expansionary fiscal stance was more evident prior to the 2007 elections. In the last two quarters of 2006, public construction spending grew by 20.5 percent and 39.6 percent, and despite the election ban, by 19.6 percent in the first quarter of 2007. The surge in infrastructure activities and government services prior to the election saw total government consumption accelerating by 13.1 percent, the highest growth since the 1st quarter of 1990.

This paper was prepared by the Macroeconomic Group under the supervision of its section head and SEPO Director General.

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