Economic Report

SENATE ECONOMIC PLANNING OFFICE

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2013 Full-Year Report

Philippine Economy: Defying the Odds

Despite the external headwinds and domestic shocks that buffeted the country in 2013, the Philippines still posted a remarkable growth level.

Prospects for 2014 remain encouraging with the emerging favorable domestic conditions and the world economy showing signs of recovery.

To keep the momentum going, reforms aimed at removing structural bottlenecks, enhancing competitiveness, and increasing social and economic inclusion should be

The SEPO Economic Report, a semi-annual publication of the Senate Economic Planning Office, provides useful information on the current state of the economy to the Senators and Senate Officials. The SEPO Economic Report is also available at www.senate.gov.ph.

I. Introduction

The recent challenges experienced by the Philippines did not weaken the country's strong macroeconomic fundamentals.

Despite the slump in the world economy and the devastation left by natural calamities, the Philippines ended 2013 well—with a gross domestic product (GDP) growth of 7.2 percent, low inflation environment, steady interest rates, and robust fiscal and current account position.

It was also in 2013 that the country received its first ever investment grade status from all three major international rating agencies. Moreover, the Philippines stood out among its peers. It is the fastest growing economy in the Association of Southeast Asian Nations (ASEAN) and has the second highest GDP growth rate in Asia, next to China. The country's ranking in various international surveys likewise improved—from 138th to 108th in the latest Ease of Doing Business and 59th from 65th in the latest Global Competitiveness Report.

Table 1. GDP Growth: Asia

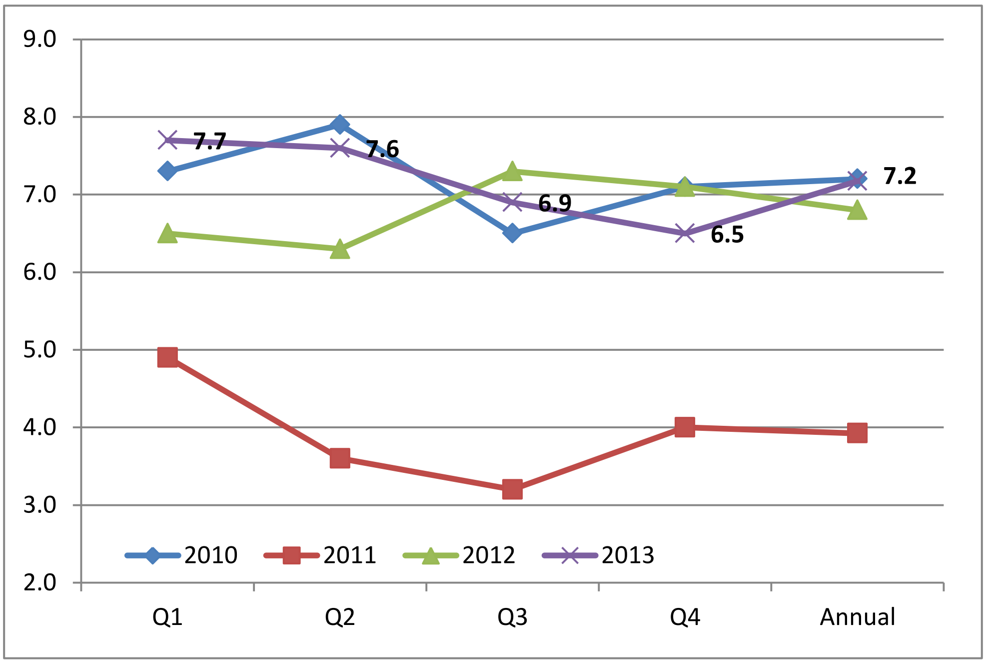
China	7.70
Indonesia	5.78
Malaysia	5.10
Philippines	***7.20***
Singapore	3.70
Thailand	2.90
Viet Nam	5.42

Source: ADB

II. Highlights of the Economy

GDP rose 7.2 percent in 2013, exceeding the government's own target of 6.0 to 7.0 percent. The 4th quarter marked the 8th consecutive quarter with above-6.0 percent GDP growth, notwithstanding the disruption on economic activity brought by the Bohol earthquake and Typhoon Yolanda.

Figure 1. GDP Growth



Source: NSCB

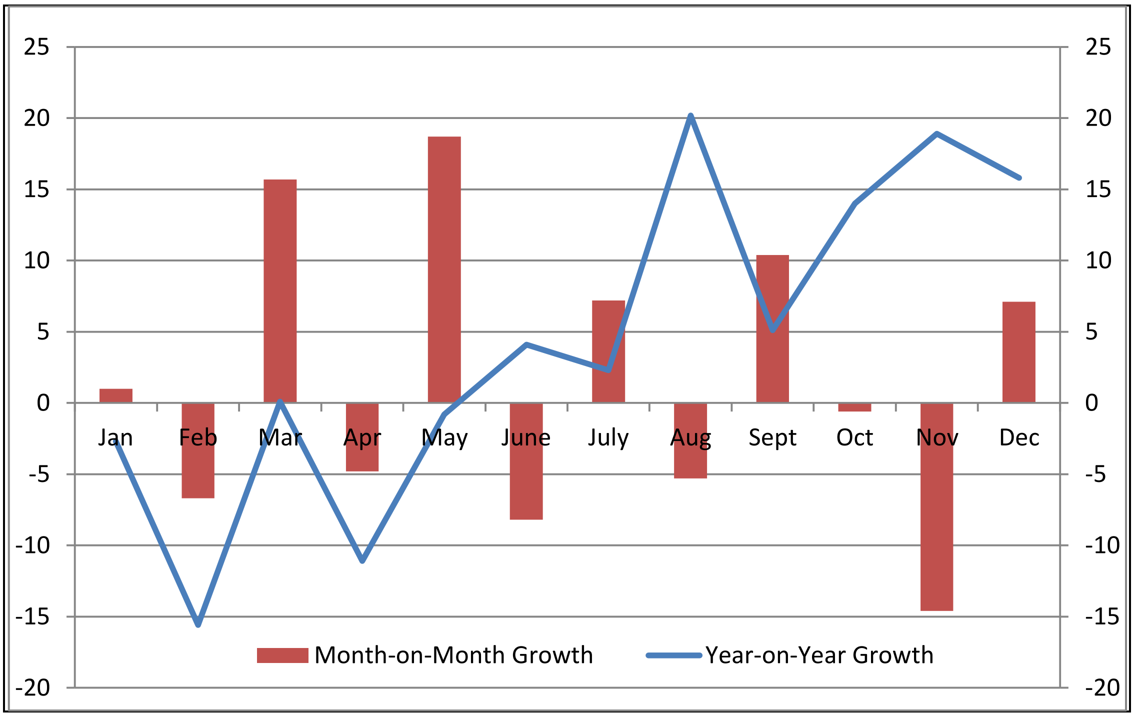
On the demand side, consumer spending which grew by 5.6 percent remains to be the biggest contributor, accounting for 4.2 percent of the economic growth. Likewise, investment growth has picked up and is increasingly becoming a major growth driver.

Investments in fixed capital and durable equipment boosted the growth of capital formation to a high of 18.2 percent in 2013, up from the -3.2 percent growth it posted 2012. This came as the private sector expanded capacity to cater to the surge in domestic consumption. This also lends support to the government's thrust in shifting the economy from being consumption-driven to investment-led.

On the supply side, growth was driven by the services and industry sectors. The sub-sectors on trade and real estate, as well as renting and business activities, continued to perform well. There has also been some renewed vigor noted in the manufacturing sector, which grew by 10.5 percent. The chemical and chemical products sub-sector, in particular, posted the highest growth at 124.5 percent.

The construction sector, on the other hand, had one of the biggest setbacks, contracting by 0.8 percent in the 4th quarter, due to the stricter rules imposed on real estate lending in compliance with prudential regulations. Still the sector was able to register a double digit annual growth of 11.1 percent. Similarly, the agriculture sector managed to post a positive growth of 1.1 percent in 2013 despite the serious damages caused by Typhoon Yolanda**.**

Figure 2. Exports Growth, Year-on-Year and Month-on-Month (%)



Source: NSO

Exports recovered in the second semester, but failed to reach the full-year growth target of 10.0 percent. Service exports grew by 7.0 percent during the last quarter of 2013. In contrast, goods exports decelerated to 6.2 percent. This brought total exports to US$53.98 billion.

Nonetheless, the positive outlook for economic expansion in the United States, Japan and the Eurozone for 2014 should provide the needed boost, albeit at a modest pace.

Fiscal deficit hit PhP164.1 billion for January to December 2013. The National Government (NG) posted a budget surplus twice during the second half of 2013—PhP21.9 billion in August and PhP1.0 billion in November. This lowered the full-year deficit to PhP164.1 billion or 68.9 percent of the full-year government target of PhP238.0 billion. The fiscal deficit accounts for 1.4 percent of GDP, lower than the 2.0 percent target and also below the 2.3 percent level recorded the previous year.

Table 2. GDP Growth Rates, 2012 and 2013 (at Constant 2000 Prices)

INDICATORS	2012				2013				ANNUAL	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2012	2013
GROSS NATIONAL INCOME	**5.7**	**6.5**	**7.3**	**6.4**	**7.8**	**6.4**	**8.1**	**7.8**	**6.5**	**7.5**
GROSS DOMESTIC PRODUCT	**6.5**	**6.3**	**7.3**	**7.1**	**7.7**	**7.6**	**6.9**	**6.5**	**6.8**	**7.2**
AGRICULTURE, HUNTING, FORESTRY AND FISHING	**1.1**	**0.6**	**4.4**	**4.9**	**3.1**	**-0.2**	**0.3**	**1.1**	**2.8**	**1.1**
Agriculture and Forestry	2.2	1.3	5.5	5.2	2.5	-0.9	0.1	2.4	3.6	1.2
Fishing	-3.8	-2.5	0.0	3.4	5.8	3.3	1.1	-4.4	-0.4	0.7
INDUSTRY	**5.3**	**5.8**	**7.1**	**8.9**	**10.9**	**10.3**	**8.2**	**8.4**	**6.8**	**9.5**
Mining and Quarrying	-1.7	6.5	-1.2	2.8	-1.9	-2.7	-0.8	-10.4	2.2	-2.5
Manufacturing	6.0	4.3	5.8	5.4	9.5	10.3	9.7	12.3	5.4	10.5
Construction	1.5	11.6	17.8	29.9	29.3	17.3	4.7	-0.8	15.7	11.1
Electricity, Gas and Water Supply	8.5	6.1	2.7	3.4	0.3	6.0	6.7	2.5	5.1	4.0
SERVICES	**8.4**	**7.7**	**8.0**	**6.5**	**6.8**	**7.5**	**7.5**	**6.5**	**7.6**	**7.1**
Transport, Storage and Communication	9.7	9.3	9.4	4.4	2.8	6.6	6.6	6.2	8.1	5.5
Trade and Repair of Motor Vehicles, Motorcycles, Personal and Household	7.8	7.8	8.2	6.6	5.5	6.8	5.8	7.4	7.5	6.5
Financial Intermediation	8.7	7.0	8.6	8.8	18.0	10.3	12.1	9.9	8.2	12.4
Real Estate, Renting and Business Activities	7.8	8.1	7.8	6.5	5.8	9.6	12.2	6.3	7.5	8.4
Public Administration and Defense; Compulsory Social Security	4.5	3.8	8.3	8.2	8.3	4.8	2.6	0.5	6.1	4.0
Other Services	10.4	8.4	6.5	5.8	5.3	6.4	5.4	5.4	7.7	5.4
HOUSEHOLD FINAL CONSUMPTION EXPENDITURE	**6.9**	**6.6**	**6.7**	**6.2**	**5.5**	**5.1**	**6.2**	**5.6**	**6.6**	**5.6**
GOVERNMENT FINAL CONSUMPTION EXPENDITURE	**21.3**	**7.2**	**12.3**	**9.5**	**13.2**	**18.0**	**4.6**	**-5.2**	**12.2**	**8.6**
CAPITAL FORMATION*	**-31.3**	**3.6**	**6.2**	**9.5**	**44.5**	**18.0**	**15.6**	**5.7**	**-3.2**	**18.2**
Fixed Capital	2.8	8.7	10.5	19.7	15.6	13.2	11.9	7.0	10.4	11.7
Construction	-1.2	10.2	19.2	30.4	30.1	16.0	4.1	-0.5	15.1	10.9
Durable Equipment	4.5	8.4	5.8	14.1	9.6	13.0	20.0	15.5	8.0	14.4
Breeding Stock and Orchard Development	1.3	2.5	0.9	1.0	0.6	-1.5	-0.9	-3.8	1.4	-1.5
Intellectual Property Products	31.7	10.3	1.6	31.4	10.4	16.2	13.0	21.2	18.0	15.4
EXPORTS	**9.8**	**1.8**	**6.2**	**8.6**	**-7.6**	**-6.8**	**10.6**	**6.4**	**8.9**	**0.8**
Exports of Goods	9.9	12.7	7.0	11.9	-8.9	-8.8	13.7	6.2	10.3	0.1
Exports of Services	9.1	2.7	2.8	-0.6	-3.2	2.3	8.8	7.0	3.6	3.5
LESS: IMPORTS	**-1.9**	**8.3**	**7.0**	**8.0**	**2.0**	**-2.9**	**14.2**	**1.9**	**5.3**	**4.3**
Imports of Goods	-5.9	5.9	5.5	6.8	0.8	-4.3	18.1	1.1	3.0	3.9
Imports of Services	16.7	22.6	13.9	12.0	6.5	3.7	8.7	4.6	15.9	5.8

**** Capital Formation includes fixed capital & changes in inventories***

Source: NSCB

BIR and BOC improved their tax collection, but still fell short of target. Revenues grew by 11.8 percent year-on-year due to notable improvements in the collections of both the Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC). With the amendment of the Sin Tax Law in 2012, sin tax collection for 2013 amounted to PhP91.6 billion, surpassing the BIR's target of PhP85.8 billion. The BIR collected a total of PhP1,216.7 billion in tax revenues in 2013, 15 percent higher than the previous year. However, this was still PhP37.0 billion short of the full-year 2013 target as collections from both operations and non-operations, which include debt issues made by government, fell short of goals.

The BOC also improved its tax take by 5 percent with the influx of importations for the yuletide season. Collections in Subic and Clark ports, alongside the district collections of Legazpi, Iloilo, Cebu, Cagayan de Oro, Davao and Aparri, exceeded the revenue targets for 2013. However, the total BOC collection was still 10.4 percent short of the desired level of PhP340.0 billion. Underperformance of the biggest ports—Manila and Batangas—may have compromised the BOC's ability to meet its annual target. Smuggling in these two ports is still observed and has overshadowed the confidence of the business community on the BOC. Nonetheless, improvements in collection in most ports indicate that the administration is slowly gaining some traction with its Customs Reform Program.

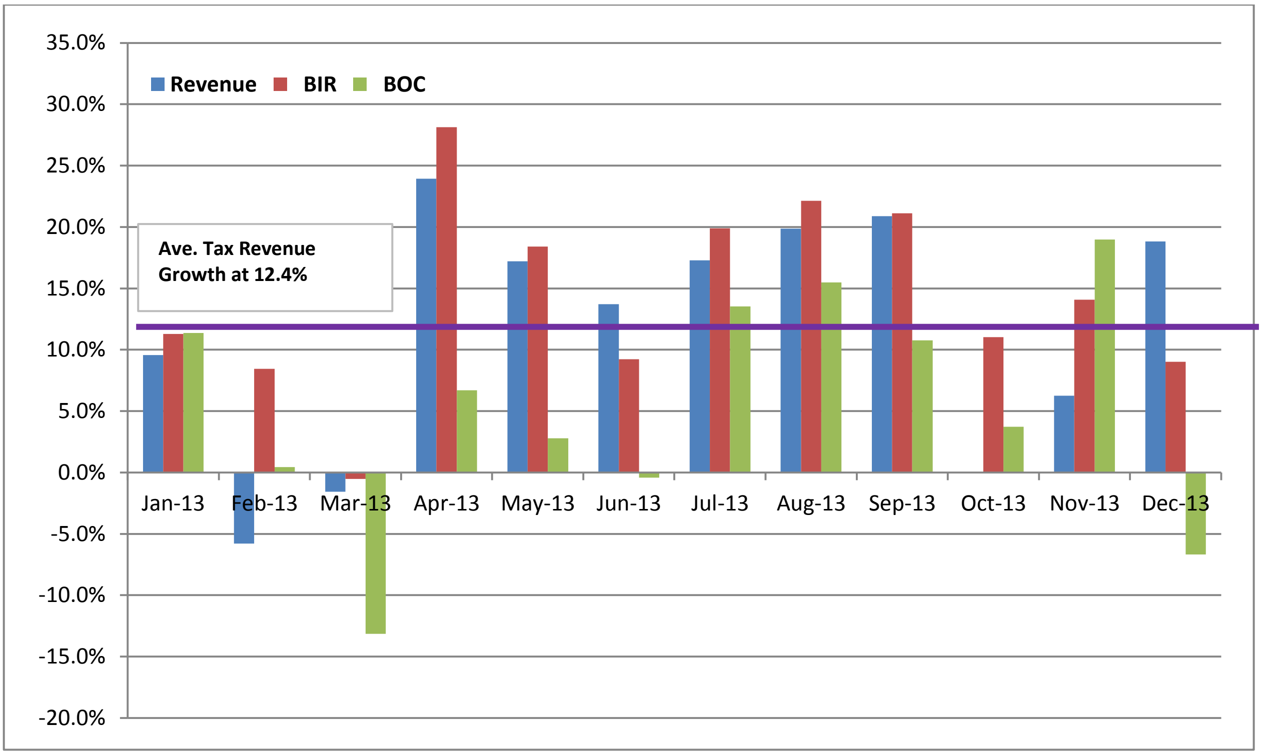
Table 3. NG Fiscal Performance, 2012-2013 (in billion PhP)

PARTICULARS	2012	2013		Variance	% Growth
	Actual	Q1-Q4 Program	Actual		
REVENUES	1,534.9	1,745.9	1,716.1	(29.8)	11.8
Tax Revenues	1,361.1	1,607.9	1,535.3	(72.6)	12.8
Bureau of Internal Revenue	1,057.9	1,253.7	1,216.7	(37.0)	15.0
Bureau of Customs	289.9	340.0	304.5	(35.5)	5.0
Other Offices	13.3	14.2	14.1	(0.1)	6.0
Non-Tax Revenues	173.8	138.0	180.8	42.8	4.0
o/w Bureau of the Treasury Income	84.1	57.7	81.0	23.2	(3.7)
EXPENDITURES	1,777.7	1,983.9	1,880.2	(103.7)	5.8
Surplus/(Deficit)	**(242.8)**	**(238.0)**	**(164.1)**	**73.9**	**(32.4)**

Source: BTr

Government spending posted positive full-year growth. Full-year 2013 expenditures amounted to PhP1,880.2 billion, 5.8 percent higher than in 2012. The rapid increase in government spending during the first half is attributed to the frontloading of spending by the various agencies as they are keen to make use of the funds allotted to them for the year. However, there was a marked deceleration beginning in the 3rd quarter amidst the controversies with the utilization of the Priority Development Assistance Fund (PDAF) which was later declared unconstitutional by the Supreme Court.

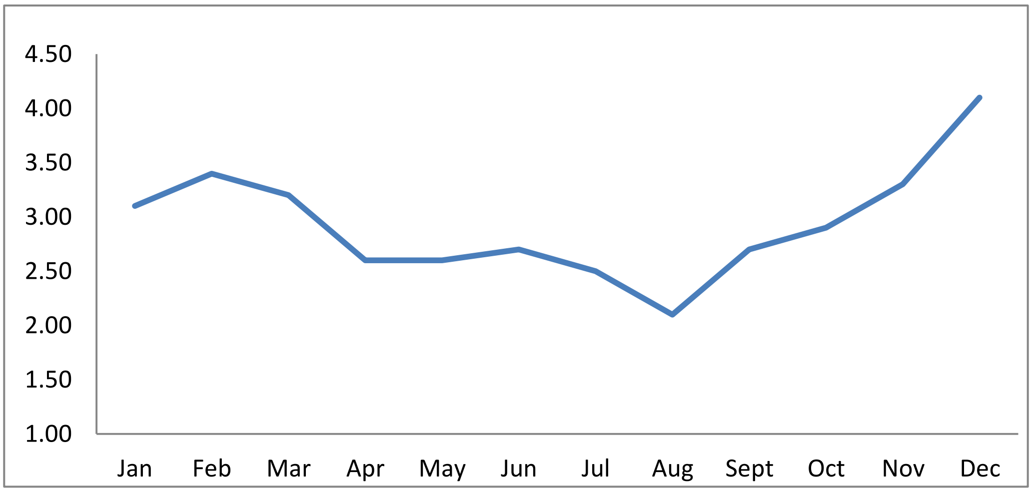
Figure 3. NG Revenue Performance Growth Rates, Year-on-Year



Source: BTr

Inflation rose in the 4th quarter but full-year rate still settled within range. Headline inflation climbed to 3.4 percent in the 4th quarter from 2.4 percent in the 3rd quarter. This is, for the most part, cyclical as prices of food, electricity and petroleum products rise on the back of stronger demand pressures during year-end but the disruptions in the supply chain brought on by the natural calamities could also have contributed. Despite the spike, full-year inflation of 3.0 percent remained to be within the Bangko Sentral ng Pilipinas' (BSP) target of 3.0 to 5.0 percent.

Figure 4. Inflation Rate, 2013

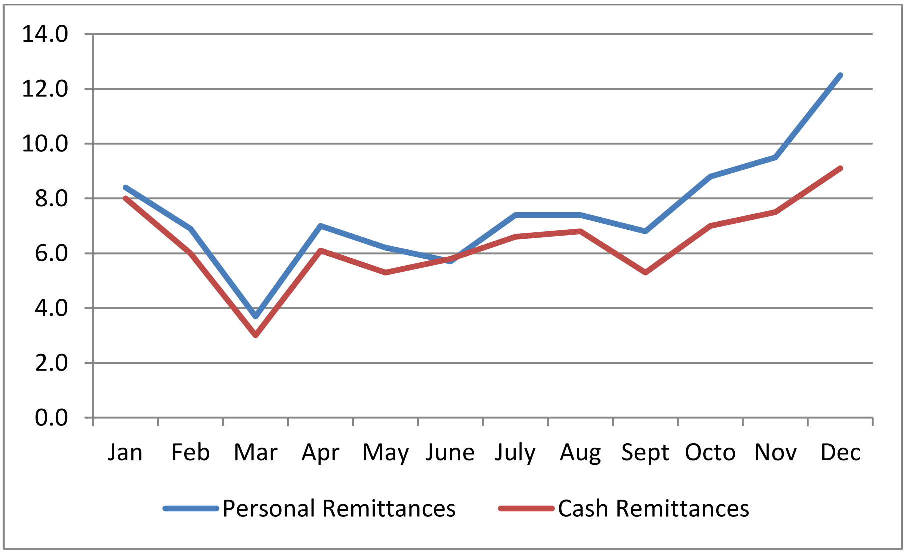


Source: BSP

Key policy rates unchanged. The Monetary Board of the BSP maintained key policy rates at 3.5 percent for the overnight borrowing or reverse repurchase (RRP) facility and 5.5 percent for the overnight lending or repurchase (RP) facility, on the back of a benign inflation environment. Likewise, interest rates on term RRPs and RPs, and reserve requirement ratios were kept. In May 2013, the BSP issued Memorandum Circular M-2013-021 limiting the access of banks to the Special Deposit Account (SDA). The SDA is one of the BSP's tools intended to mop up excess liquidity in the market. Such SDA restrictions were meant to encourage banks to lend more to businesses engaged in job-generating activities, thereby spurring the economy.

Personal and cash remittance flows remained strong. Personal remittances, which include cash and non-cash items, reached US$25.1 billion in 2013. Cash remittances coursed through banks reached US$22.8 billion, increasing by 6.4 percent since 2012. This exceeded the BSP's 5.0 percent growth projection for the year. The growth in remittances was buoyed by the sustained supply of—and demand—for Filipino workers abroad. Though preliminary data from the Philippine Overseas Employment Administration (POEA) show a decline in Filipinos deployed overseas in 2013[1] compared to the previous year, the development in bank and non-bank channels, and the depreciation bias of the peso in the medium term supported the growth in remittances. Strong remittances coupled with the mild peso depreciation, helped stimulate the domestic economy. The same stimulus is expected to ensue in the 1st quarter of 2014 on the back of continued peso depreciation and expected inflow of remittances (to support the victims of Typhoon Yolanda). The major sources of remittances in 2013 were the United States, Saudi Arabia, United Kingdom, United Arab Emirates, Singapore, Canada and Japan.

Figure 5. OFW Remittances 2013 (US$), Year-on-Year Growth (%)

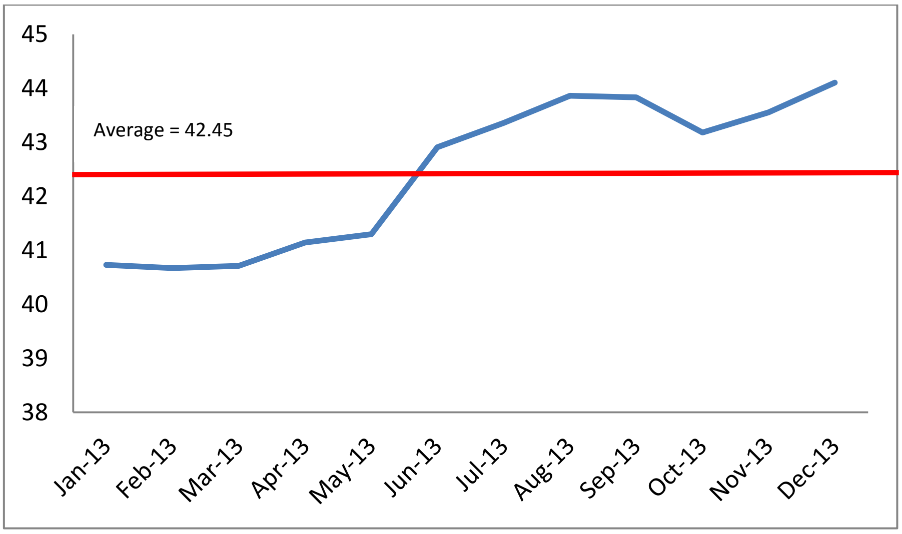


Source: BSP

[1] A total of 1,703,911 Filipinos in 2013 were deployed for overseas employment, lower than the 2012 deployment of 1,802,031.

Peso further weakened. The peso depreciated along with its regional counterparts due mainly to the uncertainty about the US Federal Reserve's (US Fed) exit from its monetary policy stimulus. The peso averaged PhP43.61 in the 4th quarter of 2013. It depreciated by 7.5 percent during the year, completely reversing the 6.8 percent gain it posted in 2012. Volatility in global financial markets is expected to continue in the coming months. The depreciation of the peso, however, will be tempered by the still-strong foreign exchange inflows from overseas Filipino workers' (OFW) remittances.

Figure 6. Average PhP/US$ Rate



Source: BSP

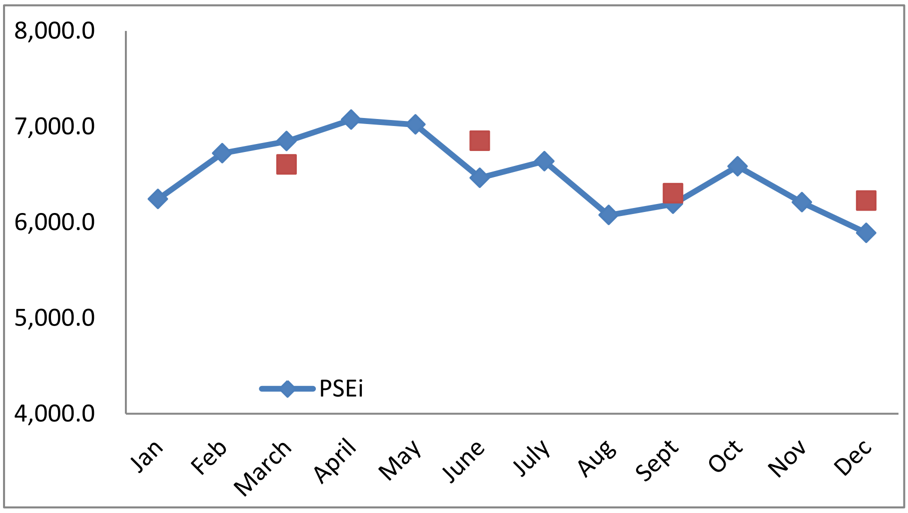
Philippine bourse set record-high gains but they were dissipated at the end of the year. After peaking in the first five months of 2013, the Philippine Stock Exchange index (PSEi) ended 2013 with a subdued 1.3 percent gain. There was a substantial capital outflow following the US Fed's announcement that it will begin to taper its quantitative easing (QE) program. Despite this, the local bourse still ended with net foreign buying that is 55 percent higher than the previous year.

Table 4. Stock Market Growth

Country	2013
Thailand	-6.70
Indonesia	-0.98
Singapore	0.01
Philippines	***1.33***
Hong Kong	2.87
United States	29.60

Source: Bloomberg

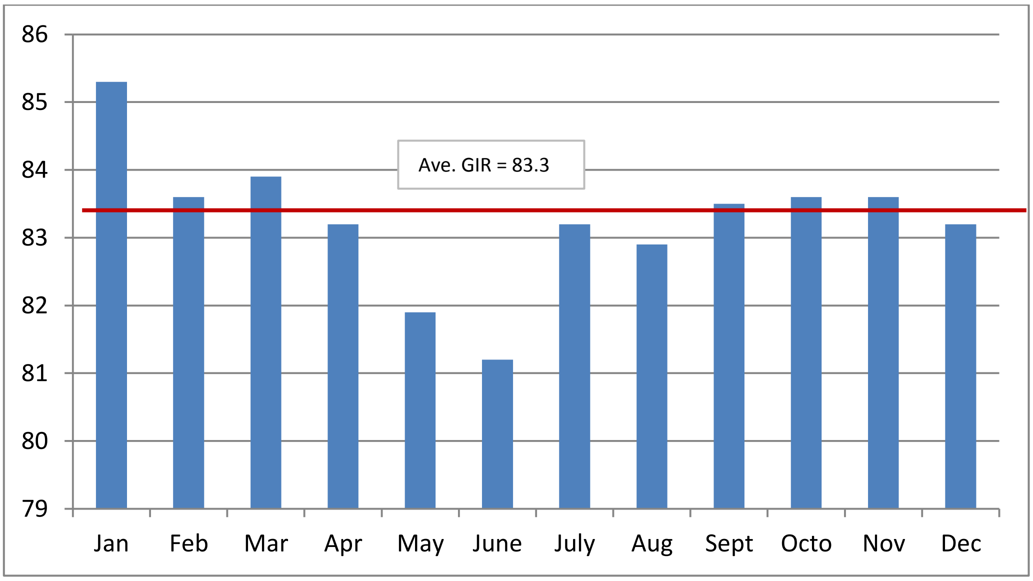
Figure 7. Philippine Stock Exchange Index, 2013



Source: NSCB

BSP missed out on GIR target. The BSP failed to meet the US$85 billion gross international reserves (GIR) target for 2013, with the end-2013 GIR level finishing off at US$83.19 billion. The weak price of gold in the international market had eroded the value of the BSP's gold holdings, pulling down the country's GIR. Despite the decrease, the BSP's foreign exchange operations and income from investments abroad, as well as foreign currency deposits of the national government continue to support GIR levels. The GIR level remains sufficient to cover 11.9 months' worth of imports. It is also equivalent to 8.3 times the country's short-term external debt based on original maturity and 5.7 times based on residual maturity—ample cushioning from external volatilities.

Figure 8. Gross International Reserves, 2013



Source: BSP

Unemployment and poverty incidence still lingered. Despite the economy's expansion, the unemployment rate rose marginally by 7.1 percent equivalent to 2.9 million individuals, while underemployment rate stood at 19.3 percent or 7.3 million individuals. The government also failed to reach its official goal of adding 1.0 million new jobs each year to absorb new entrants and lower unemployment, with only 317,000 new jobs generated for 2013.[2] According to the World Bank, with 1.15 million individuals entering the workforce every year until 2016, there is a need to generate almost 15 million jobs to fill the gap.[3] The dismal employment figures have undermined the efforts to alleviate poverty in the country. Figures from the 2012 Family Income and Expenditure Survey (FIES) show that the percentage of poor families has remained practically unchanged from 20.5 percent in 2009 to 19.7 percent in 2012. Also, with the nearing ASEAN economic integration, the Philippines would benefit more from strengthening its job-generation efforts for local residents and making its workers more competitive so as to avoid further labor displacement.

III. Outlook and Risks

Analysts, as well as business groups maintain their positive outlook for the Philippines in 2014. The World Bank estimates that the economy will expand by 6.5 percent, while the International Monetary Fund (IMF) projects a more conservative 6.3 percent growth—lower than their respective 7.0 and 6.8 percent projections last year. Meanwhile, the government has retained its growth projection at 6.5 to 7.5 percent. Bright prospects for growth are up ahead considering that domestic demand remains intact, while external demand is expected to pick up.

High public sector investment, strong consumer spending, and higher private investments should support this growth path. Reconstruction efforts in the typhoon-stricken areas are also expected to provide a boost in public infrastructure spending in 2014. Likewise, expansion in the United States and the Eurozone, albeit moderate, is projected to bode well for the exports sector and should further stimulate domestic activity.

Table 5. Global Growth Forecasts, 2014

	IMF	World Bank	ADB
Global	3.7	3.2	3.4
United States	2.8	2.8	2.4
Eurozone	1.0	1.1	1.2
Japan	1.7	1.4	1.4
China	7.5	7.7	7.4
Philippines	***6.3***	***6.5***	***6.1***
Indonesia	5.6	5.3	6.0
Malaysia	4.8	4.8	5.0
Thailand	4.2	4.5	4.9
Viet Nam	2.0	5.4	5.5

Sources: IMF, WB, ADB

[2] Data from the Bureau of Labor and Employment Statistics (BLES). http://www.bles.dole.gov.ph/.

[3] As discussed in the World Bank's Philippine Development Report 2013: Creating More and Better Jobs, which was released last September 2013.

Risks, both domestic and external, continue to be present. In the domestic front, the power situation, specifically the prospect of severe power shortages could discourage potential investors and pull down economic growth. Also, the recent reduction in the US Fed's stimulus program has triggered volatility and outflows from emerging economies like the Philippines.[4] Nonetheless, the country's strong macroeconomic fundamentals will serve to buttress the economy from such shocks.

Sustaining and improving the economy's productive capacity remains to be one of the biggest challenges. To this end, structural transformation is necessary to facilitate the transformation from being consumption-driven to an investment-led and employment-oriented economy. It is thus imperative to continue reviving the manufacturing sector and create new growth drivers. These measures must come simultaneously with increased investments in infrastructure, human capital and on research and development (R&D). Only when the employment and poverty figures improve will the Philippine economic growth become more inclusive.

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This Economic Report was prepared by Ms. Carole Kaye C. Malenab with inputs from Macroeconomics Sector Head Maria Kathreena D. Tan, under the supervision of the SEPO Directors and the overall guidance of its Director General.

[4] In January 2014, foreign portfolio investment or "hot money" reversed to a net outflow of US$1.84 billion from a net inflow of US$1.27 billion in the same month last year. This marks the country's biggest portfolio investment outflow in a month. The Philippine peso also breached the PhP45=US$1 mark in January, the first time since August 2010.