Economic Report

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The domestic economy exceeded expectations by expanding 6.6 percent in 2012. Strong macroeconomic fundamentals and improved governance helped propel the economic growth. Some facets of the economy, however, have yet to improve.

While optimism is high that growth will be sustained in 2013, downside risks remain.

The key challenge is sustaining the growth momentum and making it more inclusive. This requires structural and policy reforms that will further increase investments and generate gainful employment opportunities for the people.

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.

2012 YEAR-END REPORT

On the cusp of economic resurgence

Introduction

2012 appears to be a banner year for the Philippines. After recording a subdued 3.9 percent growth in 2011, the domestic economy expanded by 6.6 percent, exceeding market expectations and beating the government's own forecast of 5 to 6 percent GDP growth. That it happened on a non-election year and amidst a tepid global environment makes it seem all the more impressive. Citing the steady upturn in the country's finances and strong macroeconomic fundamentals, credit rating agencies have likewise upgraded the country's' sovereign rating outlook from positive to stable, with high likelihood of being elevated to investment grade in the near term.[1] From being the "sick man of Asia", the Philippines is now regarded as one of the brightest spots in the region.[2]

Notwithstanding this sanguine backdrop, some facets of the economy have yet to improve. The higher growth, for instance, was not matched by an expansion in employment and while "hot money" came in droves, the country remained a laggard in investments of the more permanent kind, as it received the least foreign direct investments (FDIs) among East Asian countries in 2012. Self-rated poverty and hunger rates have also stagnated, if not worsened.

With new opportunities as well as risks in the offing, will 2013 be a better year? This Economic Report reviews how the economy fared in 2012 and discusses the prospects it is facing in 2013.

Highlights of the 2012 Economic Performance

A. Real Sector

The industrial sector posted vigorous growth but services remained as the main growth driver. Agriculture expanded modestly. As in the past years, the services sector provided the impetus for heightened economic activity in 2012. Of the 6.6 percent gross domestic product(GDP) growth, services contributed 4.2 percentage points. Among its subsectors, Transport, Storage & Communication, Financial Intermediation, and Trade registered the highest growth rates. The real estate, renting and business sector also grew substantially, but its growth decelerated to 7.9 percent from 9.3 percent in 2011. The government attributed this mainly on the weaker global environment.

[1] The Philippines is currently rated just one notch below investment grade by all three major international credit watchdogs, namely Moody's Investors Service, Fitch Ratings, and Standard & Poor's.

[2] The World Bank Philippine Office country director Motoo Konishi tagged the Philippines as Asia's "rising tiger" at the Philippine Development Forum on February 5, 2013.

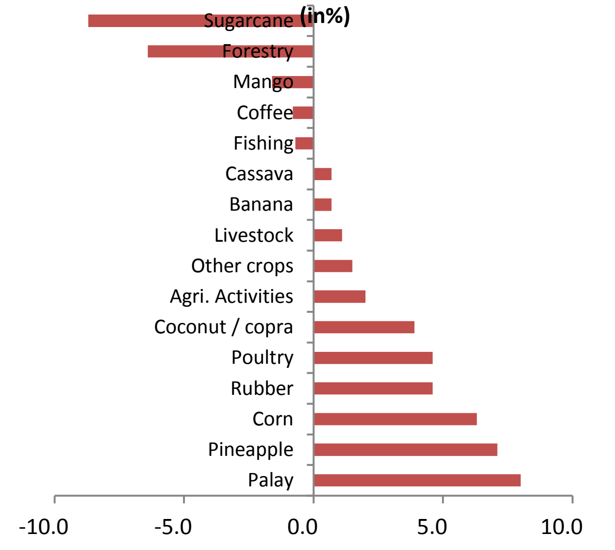
Table 1. Gross National Income and Gross Domestic Product, 2011-2012, at Constant 2000 Prices, Growth Rates (in %)

	2011	2012
Gross Domestic Product	3.9	6.6
Gross National Income	3.2	5.8
Production side		
Agriculture, Hunting, Forestry & Fisheries	2.7	2.7
Agriculture and forestry	4.5	3.5
Fishing	-4.1	-0.7
Industry Sector	2.3	6.5
Mining & Quarrying	7.0	-3.7
Manufacturing	4.7	5.4
Construction	-7.3	14.4
Electricity, Gas & Water Supply	0.6	5.1
Services Sector	5.1	7.4
Transport, Storage & Communication	4.3	9.1
Trade and Repair of Motor Vehicles Motorcycles, Personal& Household Goods	3.3	7.5
Financial Intermediation	5.2	7.8
Real Estate, Renting & Business Activities	9.3	7.9
Public Administration & Defense; Compulsory Social Security	0.3	3.3
Other Services	6.6	7.2
Expenditure side		
Household Final Consumption Expenditure	6.3	6.1
Government Final Consumption Expenditure	1.0	11.8
Capital Formation*	8.1	-4.4
Construction	-6.2	13.7
Durable Equipment	5.2	5.7
Breeding stock & Orchard Development	-0.3	1.4
Intellectual Property Products	11.8	16.9
Exports	-6.0	8.4
Imports	0.2	4.2

Source: NSCB

**Includes capital and change in inventories*

Fig. 1 2012 GVA in Agriculture, Growth Rate (in%)



Source: NSCB

With the exception of mining, all of the service subsectors performed positively. Construction, in particular, turned around from a contraction in the previous year to a double digit growth in 2012, supported by both public and private sectors. With the rise in the level of economic activity, the electricity, gas and water (EGW) sector grew 5.1 percent as against 0.6 percent in 2011. Manufacturing also benefited from the upbeat local mood as well as the relatively stronger export demand. Food manufactures, wearing apparel and non-metallic mineral products were the leading contributors to the growth of the manufacturing sector. On the other hand, with the absence of a new and clear mining policy, the mining sector continued to be weighed down by investor uncertainty.

Due to weather disturbances last year, the agriculture, fisheries and forestry sector contributed a mere 0.3 percentage points to the GDP growth. The sector grew by 2.7 percent, same as in 2011. Farm output was bolstered by the growth in the production of palay (8.0%), pineapple (7.1%), corn (6.3%), and coconut (3.9%). However, agriculture's growth was fettered by the fisheries sector which output continued to contract. Philippine fisheries production has shrunk over the years due to overfishing, pollution and climate change. Municipal fisheries production, in particular, went down by 3.88 percent in 2012.[3]

On the expenditure side, growth was buoyed by the robust spending of households and government. Private spending contributed 4.3 percentage points to the GDP growth, propped up by the low inflation and the continuous influx of remittances from overseas Filipino workers (OFWs).

Unlike in 2011 when severe government underspending sapped the growth of the domestic economy, public spending increased by 11.8 percent in 2012 as the government accelerated its disbursements for infrastructure projects and other programs such as the conditional cash transfers(CCT). The hefty state spending in the first two quarters of the year and the steady rollout of construction projects by the private sector especially in the last two quarters also helped

[3] According to the Bureau of Agricultural Statistics, commercial fisheries recovered to 0.23 percent output increase in 2012 from its negative growth in 2011 while aquaculture recorded a 2.85 percent increase in production.

Fig.2 GVA in Construction Q1 2011 to 4Q 2012 Growth Rate (in %)

Source: NSCB

Table 2. Top 5 and Bottom 5 Export of Goods, 2012

	Growth Rate (in %)	Contn to Growth (in ppt)
Contributors to growth		
Metal Components	196.6	2.2
Telecommunications	465.4	1.2
Control Instrumentation	953.9	1.1
Components/Devices(semiconductors)	1.6	0.8
Office equipment	151.5	0.7
Contributors to the Decline		
Electronic Data Processing	-27.9	-2.4
Automotive electronics	-81.5	-1.2
Articles of Apparel and clothing accessories	-19.0	-0.7
Sugar	-79.2	-0.5
Other products manufactured from materials on consignment basis	-41.1	-0.4

Source: NSCB

Table 3. Overseas Filipinos Personal Remittances 2010-2011 and Jan-Nov 2010-2012

Year	Level (in million US$)		Growth rate(in%)	
	Full year	Jan. to Nov.	Full year	Jan. to Nov.
2010	20,744	18,872	7.8	7.9
2011	22,349	20,351	7.7	7.8
2012	n.a	21,592	n.a	6.1

Source: BSP

pull up the growth of fixed capital formation. Increased investments in durable equipment such as road vehicles, telecommunications, and sound recording equipment, and mining and construction machineries were likewise registered. These brought the country's investment-to-GDP[4] ratio to 19.4 percent. The government is envisioning total investments to account for 22 percent of the GDP by 2016.

Because of the sluggish growth in the country's major trading partners (i.e. United States, Eurozone and Japan), the export sector missed its 2012 growth target of ten percent. Shipments of semiconductors, the country's dominant export, grew by a measly 1.6 percent growth as demand for consumer electronics remained weak. Nonetheless, the total export growth of 8.7 percent in 2012 is a sharp contrast with the contraction registered in the previous year. Exports of goods rebounded to 8.4 percent with the decline in electronics export compensated by the high growth in other export commodities such as metal components, telecommunications and control instrumentation among others. Export of services, which includes the business process outsourcing (BPO) industry, also proved to be resilient. Despite the generally poor global climate and the appreciation of the peso, export of services grew 9.8 percent, twice as fast than it did in 2011. Similarly, imports of goods and services posted a substantially higher growth compared to the previous year. However, the expansion is far from the 12 percent growth the government has targeted for 2012.

B. External Accounts

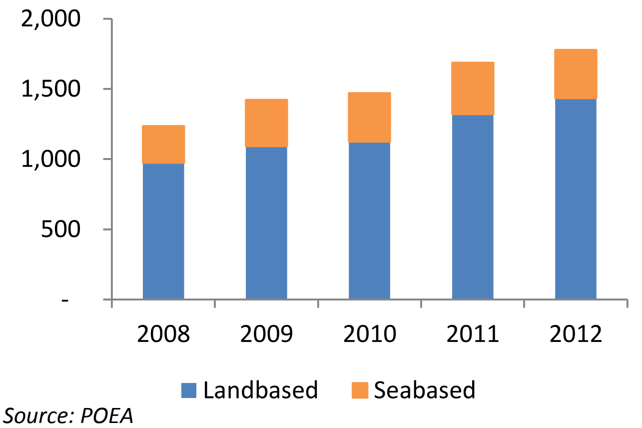
The Philippines continued to enjoy a remarkably comfortable external position. The rebound in export of goods, high receipts from BPO services, a surge in capital inflows, and a buoyant inflow of remittances brought the country's balance of payments (BOP) position to a surplus of US$9.2 billion in 2012.[5] Latest remittance data from the Bangko Sentral ng Pilipinas (BSP) show that as of November 2012, personal remittances[6] have reached US$21.6 billion, up by 6.1 percent than the level recorded in the same period in

[4] Investment here is gross capital formation (including inventories) in real terms.

[5] The BoP shows the flow of payments between a country and the rest of the world. The BOP components include the export and import of goods and services, the transfer of income in and out of the country, all capital transactions (e.g. international loans and borrowings) and all changes in official settlements. A BOP surplus means that more funds flowed into the country than those which got out.

[6] In June 2012, the BSP started to release data on personal remittances that comprehensively capture transactions in remittances from overseas Filipino. Personal remittances is broader in scope, as it includes cash and non –cash items that flow through both formal (via electronic wire) and informal channels (such as money or goods carried across borders).

Table __. Number of Deployed Overseas Filipino Workers, 2008-2012 (in '000)



Source: POEA

Table 4. PSE Index 2012		
	Closing Level (2012)	GrowthRate (in %)
PSEi	5,812.73	33.0
All Shares Index	3,698.98	21.5
Financials Index	1,525.95	57.5
Property Index	2,304.63	55.6
Holding Firms Index	5,150.76	47.0
Industrial Index	8,877.29	25.5
Services Index	1,724.65	6.7
Mining and Oil Index	19,408.38	-17.4

Source: Philippine Stock Exchange

Table 5. FDI inflows, 2011-2012 (in billions of US$)			
Region / Economy	**2011**	**2012**	**Growth Rate(in %)**
World	**1,604.2**	**1,310.7**	**-18.3**
Developing Economies	702.7	680.4	-3.2
East Asia	237.5	213.1	-10.3
China	124.0	119.7	-3.4
Hong Kong,	96.1	72.5	-24.6
Korea, Republic of	10.2	9.0	-11.9
South Asia	39.6	32.3	-18.4
India	31.6	27.3	-13.5
South-East Asia	115.0	106.5	-7.3
Cambodia	0.9	1.8	104.3
Indonesia	19.2	19.2	-0.1
Malaysia	12.0	10.0	-16.8
Myanmar	1.0	1.9	90.0
Philippines	1.3	1.5	15.5
Singapore	64.0	54.4	-15.1
Thailand	7.8	8.1	3.9
Vietnam	7.4	8.4	12.5

Source: UNCTAD

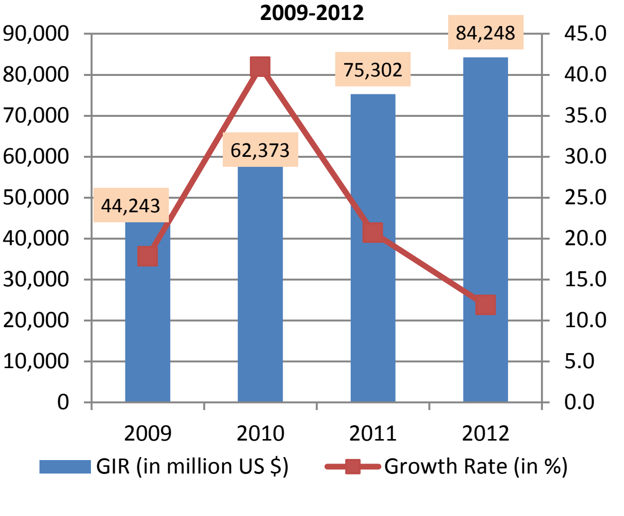
2011. However, the pace of growth is noticeably slower than the previous years. Growth was spurred by innovations in remittance services by banks and other financial institutions as well as the continuous deployment of OFWs abroad. Preliminary data from the Philippine Overseas Employment Agency(POEA) shows that 1.78 million overseas workers were deployed in 2012, up by 5.4 percent from 2011.

Also contributing to the higher BOP surplus is the brisk inflow of capital. Portfolio investments soared to US$18.5 billion in 2012, the highest in the last ten years. The BSP reports that minus the outflows, overall net inflow of portfolio investment was US$3.9 billion, about 4.7 percent lower than that recorded in 2011 due to lower investments in government securities as well as increase in withdrawals from interim Peso deposits. Portfolio investments peaked in July after Standard and Poor (S&P) upgraded the country's credit rating to a "BB+", just a notch below investment grade.

On the back of improved investor confidence, the Philippine Stock Exchange (PSE), which accounts for more than three fourths of portfolio investments entering the country, was ranked the second-best performer in Asia, next only to the Stock Exchange of Thailand (SET) Index. Net foreign buying was almost double that of the previous year at PhP109.98 billion while a record PhP219.1 billion in capital was raised, twice the 2011 level. The local bourse finished at 5,812.73, and except for mining and oil, all of the sectoral indices ended in positive territory.

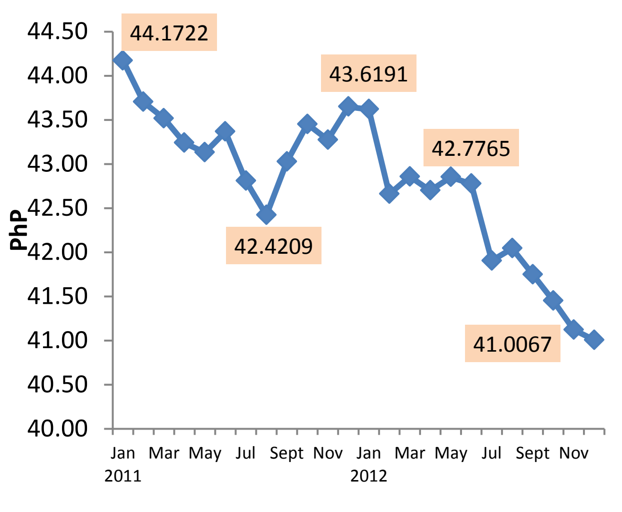
A surge in last year's FDIs was likewise recorded. Data from the 2013 Global Investment Trends Monitor of the United Nations Conference on Trade and Development (UNCTAD) show that the Philippines received US$1.5 billion worth of FDIs in 2012, 15.5 percent higher than in 2011. The figure somehow reflects a base effect as the Philippines is one of the countries which historically receive the lowest FDIs in Asia. In fact, even with the big jump in FDIs in 2012, the Philippines is still trailing its neighbors, even those with lower incomes such as Cambodia and Myanmar.

Fig.3. Philippines Gross International Reserves 2009-2012



Source: BSP

Fig. 4. Peso-Dollar Exchange Rate Monthly Average, Jan. to December 2011 and 2012



Source: BSP

Table 6. Loans Outstanding for Universal and Commercial Banks Jan.- Nov. 2011 to Jan.-Nov. 2012

(In billion PhP)

	2011	2012	Change(%)
For Production Activities	2,496	2,860	14.6
For Household Consumption	225	252	12.1
Under RRP's Arrangement	242	255	5.5
TOTAL	2,963	3,368	14

Source: BSP

With the continuous influx of foreign currency from exports, remittances and investments, the country's level of foreign exchange reserves, already high by international standards, improved even further. The BSP reports that as of end-December 2012, the Philippines' gross international reserves (GIR) reached an all-time high of US$84.2 billion, higher by 11.8 percent compared to the GIR in 2011 and well above the government forecast of US$77.5-80.0 billion for the year. The current reserve level can cover over a year's worth of imports of goods and services and is equivalent to 10.5 times the country's short-term external debt based on original maturity and 5.8 times based on residual maturity.[7] This indicates that the country has more than enough resources to serve as buffer against external turbulence.

Another consequence of the steady stream of foreign exchange into the country is the strengthening of the local currency. The peso appreciated against the US dollar by 6.8 percent and closed at 41.05/US$1 on 28 December 2012. The Development Budget Coordination Committee (DBCC) has previously set exchange rate to fall within the PhP42 to PhP45 range in 2012. The BSP utilized a variety of instruments to help temper the strength of the peso and prevent large disruptions in economic activity.

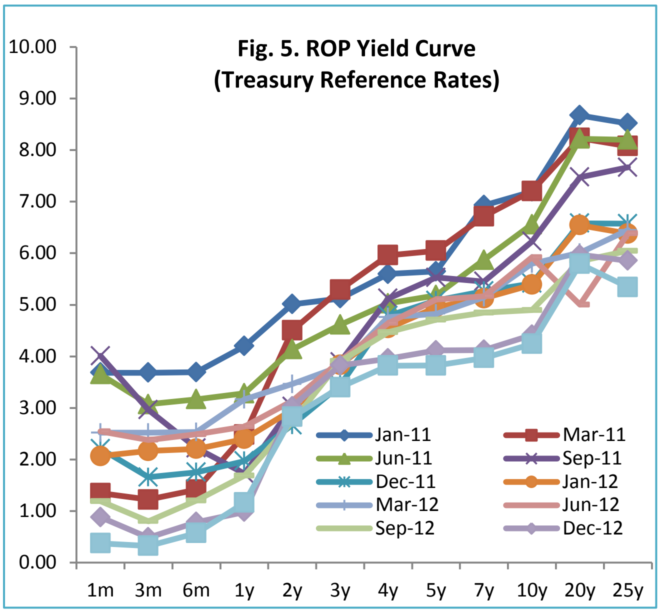
C. Monetary and Financial Sector

Inflation was benign for the whole of 2012 and provided the government an increased scope to further ease monetary policy. Inflation averaged only 3.2 percent, well within the lower bound of the government target range of 3 to 5 percent.

The subdued increase in prices enabled the Monetary Board to continue with its accommodative monetary stance and implement policies that will further boost economic growth. The BSP cut its key policy rates four times in 2012, totaling to 100 basis points. The BSP's overnight borrowing rate and overnight lending rate stood at historic lows of 3.5 percent and 5.5 percent respectively, at the end of the year.

Supported by the favorable interest environment, bank lending grew by 14 percent in the first 11 months of 2012. Universal and commercial bank loans stood at PhP3.314 trillion. Loans for production activities for the period amounted to PhP2.860 trillion which was driven by credit to public administration and defense. Likewise, consumer loans reached PhP252.116 billion, led by auto loans and credit card collection.

[7] The conventional benchmark is for countries to hold reserves that can cover 100 percent of its short-term debt or the equivalent of three months worth of imports.



Source: Bureau of Treasury

Given the stable macroeconomic variables, alongside the upgrades from credit rating agencies, market players were encouraged to invest in the country's government papers, thus an increase in the volume of tenders, which brought the yields down. This afforded the government to reduce its borrowing cost. Short-term rates, such as the 91-day T-Bill rate slid to a 0.20 percent in December 2012 from 1.54 percent at the start of the year.

D. Fiscal Sector

Fiscal position improved as both revenues and spending increase but significant room for improvement remains. Fiscal underspending was considered to be the main factor for the lackluster growth in 2011. To prevent a repeat scenario in 2012, the government increased its provision and accelerated its pace of disbursements for infrastructure and social services. Fiscal spending from January to November 2012, grew by 14.1 percent from PhP1.35 trillion in the same period in 2011. Marked increases were seen in the spending for personal services with the implementation of the last tranche of the Salary Standardization Law III, and in Capital Outlay as the government embarked on key infrastructure projects. Expenditures for Maintenance and Other Operating Expenses (MOOE) jumped by almost 50 percent while PhP282.3 billion was released for interest payments. Total government disbursements amounted to PhP 1.54 trillion, and accounted for 83.5 percent of the programmed spending for the whole year.

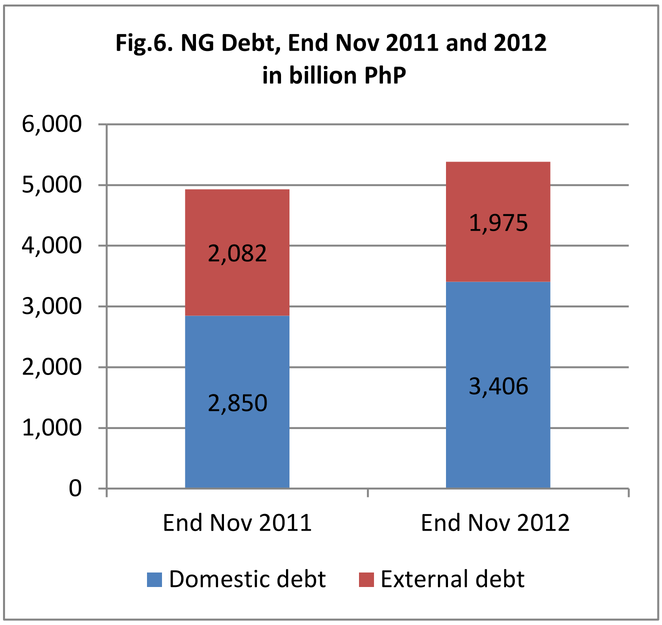
Table 7. Cash Operations Report
Jan.-Nov. 2011 to Jan.-Nov. 2012 (in million PhP)

Particulars	Jan-Nov 2011	Jan-Nov 2012	Growth Rate(%)	2012 Program	% of Program
Revenues	1,249.77	1,408.58	12.71	1,560.62	90.3
Tax revenues	1,104.96	1,247.00	12.85	1,427.43	87.4
BIR	849.52	969.34	14.11	1,066.12	90.9
BOC	242.96	264.34	8.80	347.07	76.2
Other offices	12.49	13.32	-0.46	14.24	93.6
Non Tax revenues	144.76	161.48	11.55	133.20	121.2
Expenditures	1,346.00	1,535.88	14.11	1,839.73	83.5
Current Operating Exp.	1,127.10	1,258.2	11.63	1,442.58	87.2
Personal Services	449.2	496.1	10.44	585.72	84.7
MOOE	151.3	226.5	49.70	254.57	89.0
Subsidy	37.3	25.6	-31.37	31.76	80.6
Allotment to LGUs	210.4	200.4	-4.75	218.65	91.7
Interest payments	251.5	282.3	12.25	317.65	88.9
TEF	27.4	27.1	-1.09	34.22	79.2
Capital Outlays	201.9	248.7	23.18	374.15	66.5
Infra & Other CO	118.2	185.6	57.02	298.23	62.2
Equity	12.4	1.2	-90.32	2.08	57.7
Capital Transfers to LGUs	63.4	62.0	-2.21	71.34	86.9
CARP-LO	7.9	-	-	2.50	-
Net Lending	17.1	29.0	69.59	23.00	126.1
Surplus/(Deficit)	1,346.00	(127.30)	-109.46	279.11	-45.6

Source: Bureau of Treasury and Department of Budget and Management

It must be noted though that despite the increase, the spending for Capital Outlay remains significantly below than what is programmed for the year. With only one month to account for and still about PhP125 billion of the budget to be used up, it is highly unlikely that the expenditure program for Capital Outlay will be met. This is a serious concern as the Philippines has long been criticized for underspending in public infrastructure.

Similarly, aggregate revenues during the said period registered a double digit increase from the 2011 collections. It stood at PhP1.41 trillion as of November 2012, which is 90.3 percent of the revenue program for the year. Non-tax revenues have surpassed the target set by the DBCC by more than 20 percent as the



Source: BTr

Table 8. Selected Labor and Employment Indicators (in '000, unless otherwise stated)		
Indicators	**2011 Average**	**2012 Average**
Household Population (15y. old & over)	61,882	62,976
Labor Force	40,006	40,446
Employed	37,192	37,622
Underemployed	7,163	7,512
Unemployed	2,814	2,833
Labor Force Participation Rate (in %)	64.6	64.2
Employment Rate (in %)	93.0	93.0
Underemployment Rate (in%)	19.3	20.0
Unemployment Rate (in %)	7.0	7.0
Employment by Industry		
All Industries	37,192	37,622
Agriculture	12,309	12,115
Industry	5,508	5,766
Services	19,224	19,751
Employment by Class of Workers		
Wage and Salary Workers	**20538**	**21294**
Self-employed without any paid employee	10994	10854
Employer in own family-operated farm or business	1354	1364
Unpaid Family Workers	4306	4101
Employment by Number of Hours Worked (in %)		
Less than 40 hours	14072	13174
40 hours and over	22851	22647
With a job, not at work	525	508
Mean hours worked	40.7	41.0

Source: NSO
**Average for January, April, July and October rounds of the Labor Force Survey*

Bureau of Treasury posted higher-than-expected income. Proceeds from privatization, particularly the sale of a part of Food Terminal Inc.(FTI) property, also contributed to the higher non-tax revenue. However, the revenue target from tax sources, is in danger of not being met. The Bureau of Customs (BoC) and the Bureau of Internal Revenue (BIR) need to collect PhP347 billion and PhP1.067 trillion, respectively, as set by the DBCC. The BIR will likely meet its target given the higher-than-expected GDP but the BoC will likely miss its goal as its January to November collection accounted for only 76.5 percent of the full year target. The BoC has identified the implementation of zero duties on oil products and imported motor vehicles, the weak international trade, peso appreciation, and leakages from smuggling and corruption as the reasons for the lower collection

Notwithstanding the shortfalls in the revenue side, the country's fiscal deficit level for the period was contained at PhP127.30 billion, barely half of the full-year deficit target. Netting out interest payments, the National Government (NG) posted a primary surplus amounting to PhP155.037 billion, roughly the same as in 2011.

NG debt, on the other hand, climbed to PhP5.4 trillion as of end November 2012, higher by 5.1 percent from end-November 2011. Local borrowings dominated the borrowing mix, with PhP3.41 trillion or 63 percent of the total NG debt owed to domestic creditors. External debt declined mainly due to the appreciation of the local currency as well as the net depreciation of third currencies against the US dollar. The NG debt portfolio remained predominantly medium to long-term (MLT) in tenor, with only 5 percent of the debt maturing in the short term. This gives the Philippines a longer period of time to schedule its debt payments.

E. Employment, Hunger and Poverty

The high economic growth did not translate into more jobs and quality of life is perceived to have worsened. Even as the pace of growth quickened significantly, other economic indicators that are regarded to be more meaningful to ordinary Filipinos remained stagnant. Labor market conditions did not improve as the number of jobless Filipinos increased from 2.81 million to 2.84 million. Unemployment rate was unchanged at 7.0 percent.

Cognizant of the impact of jobs to poverty reduction, the government, in its 2011-2016 Philippine Development Plan, has targeted to generate at least one million jobs every year. However, in 2012, only an average of 430,000 jobs were created. The agriculture sector, where most of the poor and the unskilled are, even shed an average of 194,000 jobs. The quality of employment has also deteriorated. The underemployment rate increased to 20.2 percent from

Table 9. Self-Rated Poverty and Hunger Rate* (in %) 2010-2012				
Year	**Self-Rated Poverty**	**Overall Hunger**	**Moderate Hunger**	**Severe Hunger**
2010	48.0	19.1	15.8	3.3
2011	49.0	19.9	16.1	3.7
2012	52.0	19.9	15.6	4.3

*Source: SWS *Average of four quarters*

Table 10. Philippines Ranking in Global Competitiveness (2010-2012)		
Year	Rank	Countries Included
2012-2013	65	144
2011-2012	75	144
2010-2011	85	144

Source: World Economic Forum Global Competitiveness Index

Table 11. Philippine Ranking in Corruption perception Index, (2010-2012)		
Year	Rank	Countries Included
2012-2013	105	176
2011-2012	129	183
2010-2011	134	178

Source: 2012 Transparency International

19.3 percent in 2011 and the proportion of part-time workers or those who have worked less than 40 hours a week rose from 36.1 percent to 37 percent.

Perception surveys conducted by the Social Weather Stations (SWS) likewise show that the benefits of higher growth were not felt by the people. The average annual self-rated poverty, or the average percentage of families who consider themselves poor has increased in the last three years from 48 to 52 percent. Despite increased coverage and budget for the CCT program of the government, families who have experienced hunger jumped from 19.1 to 19.9 percent.

E. Governance and Institutions

Governance reforms have helped boost investor confidence and create an enabling environment for economic growth. Efforts to improve governance have been cited as one of the reasons for the country's remarkable climb in the latest Global Competitiveness Report of the World Economic Forum. In 2012, The Philippines is considered as one of the "most improved" economies and is now in the upper 45 percentile of the countries covered. The country's ranking jumped 10 notches, to 65th from 75th in 2011.

The report noted that aside from the macroeconomic environment which were the strongest aspects of the country's performance, the Philippines also made substantial progress with respect to its public institutions (94th, up 23 places), trust in politicians (95th, up 33 places) corruption (108th, up 11 places) and red tape (108th, up 18 places). The report came with an important reminder that despite the significant improvement, many weaknesses remain to be addressed.

The positive trend with regards to corruption is also shown in the 2013 Corruption Perception Index(CPI) of Transparency International. In the 2012 index, the Philippines ranked 105th overall, and has overtaken the scores of countries such as Bangladesh, Vietnam and Indonesia which all got higher scores than the Philippines in the previous year.

Political and institutional factors have likewise underpinned the rating upgrades received by the Philippines. According to the S&P, "the current administration possesses a level of legitimacy, support, and stability that reduces political uncertainty and allows for improved legislative efficiency."

In 2012, two major measures, the Reproductive Health bill and the Sin Tax Reform bill that have long been languishing in the legislative mill were finally passed into law. It was also in 2012 that the country witnessed the successful closure of the impeachment case of the Chief Justice of the Supreme Court. Aside from increasing the people' awareness on the need to demand for more transparency and accountability among its public officials, the completion of the said case was an indication that the country's democratic institutions are functioning. The government's signing of the framework peace agreement with the Moro Islamic Liberation Front (MILF), is another landmark deal that is seen to help end the long-running insurgency and foster economic growth in Mindanao.

III. Outlook and Challenges

The growth momentum is expected to continue in 2013 as government targets a more bullish growth goal of 6 to 7 percent. Development agencies and market players share the bright outlook, with the World Bank and the International Monetary Fund expecting the GDP to grow by 6.2 and 6.0 percent, respectively. The ADB, on the other hand, sets it at 5 percent.

The government hinges its outlook on the continuing resilience of consumer spending underpinned by the stable increase in prices, sustained growth in BPO receipts and OFW remittances, and the continuous implementation of its social protection programs. In the absence of inflationary shocks, the BSP sees inflation settling between 3 to 5 percent this year. With manageable inflation, interest rates will also likely remain low.

The incoming midterm elections will likewise bolster spending and boost GDP growth in 2013. GDP growth rates in the last three election years have all exceeded 6 percent. Real GDP growth was 6.7 percent in 2004, 6.6 percent in 2007 and 7.6 percent in 2010.

The slightly improved growth prospect in advanced economies is expected to lift exports as well as the growth of the manufacturing sector. The construction sector will gain from public infrastructure spending and implementation of public-private projects. According to the Public-Private Partnership (PPP) Center, after rolling out eight infrastructure projects in 2012, 16 more big-ticket items that are already in the advanced stages of project review, will be added to the list of projects for bidding. Increased foreign investments is also anticipated on the back of expectations that the country will finally receive the much coveted investment grade rating.

Similarly, agricultural growth is expected to be more vibrant in 2013 with a more favorable weather condition.[8] The services sector is expected to continue to benefit from robust private consumption and investment. The government in particular is banking on a more upbeat tourism industry after the Philippines' inclusion in the top destination lists of reputable international traveler publications. The tourism industry targets a 25 percent increase in foreign tourist arrivals in 2013.

The government has also announced that it will tap the full potential of other regions in in the country, and that the development of Mindanao will be a priority.

Risks to Growth

While optimism is high that growth will be sustained, some factors may undermine the expansion of the domestic economy in 2013.

First, is the continuing uncertainty in the global market. While major risks have declined, the global economy remains frail. In particular, the lack of credible policy particularly in advanced economies—the lingering debt problems and the sluggish growth in the Eurozone as well as the deficit issues in the United States, can potentially impact the country's exports and investment prospects. It will be challenging in particular to the electronics sector. To lessen the country's vulnerability to adverse external developments, the diversification of the country's exports should be continued. In 2012, the share of electronic components to total exports has gone down to 55.5 percent from 71.1 percent in 2010. A more robust intraregional trade should also be pursued to compensate for the muted demand from the advanced economies.

Another pressing concern is the huge volume of capital flowing into the country. While it strengthens the country's external position and helps in making the capital market vibrant, a surge in capital inflow, if not properly managed, can also threaten the stability of the macroeconomy.

The large inflow of foreign exchange, for instance, has been placing upward pressure on the peso. While a strong peso may be helpful in maintaining a stable inflation, it also reduces the competitiveness and income

[8] NEDA reports that as per PAGASA's latest update, a more favorable weather condition awaits the agricultural sector, as El Niño is likely to slow down and El-Niño-Southern Oscillation (ENSO)-neutral conditions, described as the absence of either El Niño or La Niña, will likely prevail over the next several months.

of Filipino exporters, particularly those in the manufacturing sector. The rise of the peso against the US dollar will likewise affect Filipino households which depend on remittances. The impact, however, will likely be less, because of the so-called "remittance effect", wherein OFWs remit a higher amount of dollars to offset the strong peso. The appreciation of the currency also poses a real challenge to the long-term growth prospect of the outsourcing industry as it increases the cost of labor and consequently reduces the industry's revenue margins.

To temper the peso appreciation, the BSP has been engaging in sterilization and mopping up excess liquidity through the use of open market operations. It has also been prepaying the country's foreign liabilities and has further liberalized foreign exchange regulations. Moreover, the BSP cut its policy rates several times to manage the entry of foreign capital into the country. Analysts, however, point out that the lower costs of borrowing could encourage speculative activity particularly in the property market and might potentially result in an asset bubble. For this, the BSP needs to be vigilant, especially in monitoring the banks' exposure to real estate loans.

On the cusp of economic resurgence

The favorable developments happening in the country-- robust economic growth, strong macroeconomic fundamentals and improved governance raise high hopes of an economic revival in the Philippines.

The key challenge is sustaining the growth momentum and making it more inclusive. Economic growth should be felt on the ground and its benefits should be shared by all.

Employment is one transmission channel through which people can enjoy the benefits of high economic growth. As such, the kind of growth the country should be pursuing is one which produces gainful employment for as many people as possible. However, most of the fastest growing sectors of the economy in recent years have relatively low employment intensity.

For the past three decades, the Philippines' main growth driver has been the services sector. In 2012, the services subsectors which posted the highest growth rates were transport and communication, financial intermediation, and the real estate sectors. They accounted for only 7.0 percent, 1.2 percent, and 0.5 percent of the total employment in the country, respectively. On the other hand, the agriculture and fisheries sector which accounted for about one third of the country's total employment posted a gross value added of only 2.7 percent in 2012 while manufacturing, which employed around 3.1 million people, grew by 5.4 percent, a slight improvement from 4.7 percent in the previous year.

Increasing and sustaining the growth in agriculture and manufacturing should be ensured as they can absorb most of the country's surplus labor, particularly those with low skills and limited education. In addition, these sectors have backward and forward linkages with the rest of the economy, which means that they could stimulate the growth of other sectors.

The agriculture sector will benefit from productivity increases by way of improvements in rural infrastructure, research, and technology diffusion. Land reform efforts should also be fast tracked. Moreover, because it is highly vulnerable to weather conditions, the agriculture sector should continue building resilience for adaptation to climate change.

The Philippines, according to the ADB, has enormous potential to become a key production base within Asia (Usui, 2012). To boost industrial growth, particularly, in the manufacturing sector, there is a need for proactive public sector support. Aside from electronics and auto seat assemblies, industries and products with latent comparative advantage should be identified, and government should ascertain the constraints and implement clear-cut measures that will help the private sector invest in the manufacture of these products. The Department of Trade and Industry(DTI), together with the government's think tank, the Philippine Institute for Development Studies (PIDS), have already taken the lead in the crafting of a manufacturing industry roadmap together with the private sector. The said roadmap is set to be completed in the first quarter of 2013 and is expected to steer the country's re-industrialization.

Since employment is closely tied to investments, there is a need to further strengthen the country's investment climate. While there has been some progress in reducing the cost of doing business in the country, as reported in the latest Global Competitiveness Report of the World Economic Forum, there is significant scope for improvement, particularly in the areas of power, and transport infrastructure (i.e ports and airlines). Limited competition in these sectors has resulted in expensive inputs, and in turn, hindered investments (Bocchi, 2008). An anti-trust or a competition policy will do well in encouraging investments in these sectors.

To continue financing the government's infrastructure projects and social protection programs, more revenues, through stronger tax administration and tax policy reform, are needed. One particular legislation that should be pursued is the rationalization of fiscal incentives. Public spending efficiency is also essential.

In addition, the recent spate of robberies in the metropolis and other high-profile crimes have put the country in a bad light and may discourage tourism and investment activity. Measures that will address governance concerns such as the peace and order problem as well as the slow dispensation of justice should be continuously implemented and improved.

Moreover, while efforts to reduce corruption seem to be gaining traction, the perception of corruption in the country, remains high. Smuggling, in particular, still appears to be rampant. A well-crafted law that will allow people's access to public documents and information and engender transparency and accountability among public officials hopefully sees the light of day in the incoming Congress.

Unless these structural and policy reforms are put in place, the Philippines will always be on the cusp of economic resurgence, but never fully realizing it.

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