Economic Report

SENATE ECONOMIC PLANNING OFFICE

August 2021 ER-2021-02

2021 Midyear Economic Report

A Fragile Recovery

The Philippine economy managed to exit the recession when it posted an 11.8 percent year-on-year GDP growth in the second quarter of 2021, bringing the first semester average to 3.7 percent. As the growth is largely base-driven, economic recovery remains fragile. Downside risks predominate, foremost of which is with the entry of new and more contagious Coronavirus Disease 2019 (COVID-19) variants that could necessitate the reimposition of mobility restrictions. Higher inflation, the natural calamities that usually come in the second semester, as well as the associated risks that come from the divergent pace of recovery amongst the country's trading partners also pose headwinds to growth. Sustaining the recovery is predicated on the fast progression of the vaccination program which would enable greater mobility and confidence, effective implementation of the government's prevention-detection-isolate-treat-reintegrate (PDITR) strategies, and continued targeted fiscal and monetary policy support and interventions that could minimize the scarring effects of the pandemic and other future shocks.

Real Sector

On the production side, all major sectors posted positive growth except agriculture. Among the three main sectors, industry grew the highest in the first half of 2021 at 7.4 percent. All of its subsectors rebounded from the deep plunge recorded in the same period in 2020. Manufacturing grew by double digit (10.4%) with new orders and renewed expansion in pre-production inventories. Less stringent measures and mobility restrictions during the said period helped support the growth of industry. Most of its subsectors remained either fully operational or partially open even during the reimposition of the enhanced community quarantine (ECQ) in March and April this year.

The services sector also expanded in the first semester, albeit at a more subdued pace of 2.6 percent. Wholesale and retail trade/repair of motor vehicles, which accounts for more than a quarter of services, grew by a meager 1.1 percent. The biggest gainers continue to be the information and communications subsector which registered a hefty growth of 10.6 percent, and the human health and social work activities which expanded by 12.7 percent.

In contrast, the transport and the accommodation and food subsectors continued to take a beating, posting -4.8 percent and -2.3 percent growth, respectively, as travel and tourism remains severely depressed. Similarly, the agriculture, fishery and forestry sector contracted by 0.7 percent in the first semester, weighed down by the 21.5 percent contraction of the livestock subsector due to the African Swine Fever (ASF) outbreak.

Table 1. Quarterly GDP Growth Rates, 2020 and 2021 (at Constant Prices)

PARTICULARS	2020				2021		2020	2021
	Q1	Q2	Q3	Q4	Q1	Q2	1st Sem.	1st Sem.
Gross Domestic Product	-0.7	-17.0	-11.6	-8.3	-3.9	11.8	-9.3	3.7
Net primary income from the rest of the world	-9.3	-24.4	-32.6	-55.9	-75.6	-53.8	-16.6	-66.1
Gross National Income	-1.6	-17.6	-13.5	-12.1	-10.6	6.6	-10.0	-2.4
Production								
Agriculture, forestry, and fishing	**-0.3**	**1.6**	**1.2**	**-2.5**	**-1.3**	**-0.1**	**0.6**	**-0.7**
Industry	**-2.5**	**-21.8**	**-17.6**	**-10.6**	**-4.4**	**20.8**	**-12.6**	**7.4**
Mining and quarrying	-21.3	-21.7	-13.0	-16.4	1.0	0.8	-21.5	0.9
Manufacturing	-3.3	-21.2	-10.4	-4.9	0.5	22.3	-12.3	10.4
Electricity, steam, water and waste	4.9	-6.4	0.2	0.6	1.1	9.8	-1.2	5.6
Construction	-0.3	-29.4	-39.7	-26.8	-22.6	25.7	-16.9	0.8
Services	**0.1**	**-17.1**	**-10.6**	**-8.0**	**-4.1**	**9.6**	**-9.1**	**2.6**
Wholesale and retail trade; repair	1.4	-14.1	-6.3	-4.0	-3.4	5.4	-7.1	1.1
Transportation and storage	-11.4	-58.5	-29.5	-20.1	-19.6	23.4	-36.2	-4.8
Accommodation and food service activities	-15.9	-67.1	-54.6	-45.6	-22.5	53.4	-40.5	-2.3
Information and communications	4.7	10.7	3.0	1.9	6.5	14.2	7.8	10.6
Financial and insurance activities	8.8	4.8	4.2	4.3	4.3	4.2	6.7	4.3
Real estate and ownership of dwellings	-2.9	-29.9	-19.2	-14.9	-11.7	16.7	-16.8	0.7
Professional and business services	-2.5	-15.7	-11.1	-8.9	-4.4	11.7	-10.0	4.2
Public administration and defense	5.5	7.1	4.7	1.3	7.5	4.0	6.4	5.5
Education	1.3	-14.5	-16.7	-12.3	0.2	10.0	-7.4	5.2
Human health and social work activities	3.0	-15.4	-3.3	1.5	13.2	12.1	-6.7	12.7
Other services	-9.8	-63.7	-48.7	-43.4	-38.7	39.4	-36.9	-16.1
Expenditure								
Household final consumption expenditure	**0.2**	**-15.3**	**-9.2**	**-7.3**	**-4.7**	**7.2**	**-7.7**	**0.9**
Government final consumption expenditure	**7.0**	**21.8**	**5.8**	**5.1**	**16.1**	**-4.9**	**15.5**	**3.5**
Gross capital formation	**-12.1**	**-51.5**	**-39.5**	**-32.2**	**-14.8**	**75.5**	**-33.1**	**20.2**
Exports of goods and services	**-4.4**	**-33.5**	**-15.1**	**-10.2**	**-8.8**	**27.0**	**-19.5**	**6.6**
Exports of goods	-2.6	-30.6	-1.3	-0.1	2.8	35.4	-17.3	17.1
Exports of services	-6.2	-36.6	-35.4	-24.9	-21.1	17.3	-21.9	-5.0
Imports of goods and services	**-7.4**	**-37.3**	**-20.7**	**-20.2**	**-7.0**	**37.8**	**-22.7**	**11.6**
A. Imports of goods	-8.5	-38.5	-18.9	-13.3	-0.5	46.4	-24.3	19.6
B. Imports of services	-3.0	-30.6	-28.7	-42.4	-31.3	-4.4	-15.2	-21.5

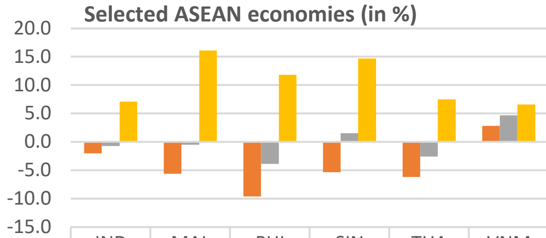
Source: Philippine Statistics Authority

Except for government spending, all expenditure components of the gross domestic product (GDP) registered higher growth rates in the first semester. Household consumption, which accounts for 70 percent of the GDP, finally swung back to positive territory after a year of continued contraction. However, it grew by only 0.9 percent, a far cry from its pre-pandemic average growth of 6.2 percent[1], and a strong indication that consumers are still reluctant to spend more. The growth of public spending, on the other hand, has decelerated to 3.5 percent from 15.5 percent in the first half of 2020. According to the National Economic and Development Authority (NEDA), this is primarily due to base effect as the government spent a relatively huge amount for emergency subsidies for households and displaced workers in the second quarter in 2020. While financial assistance was also given to eligible households during the ECQ in March and April this year, the

[1] This is the average annual growth rate of household consumption from 2015-2019.

earmarked amount of PhP22.9 billion was much lower and the coverage was also smaller as it was limited only to beneficiaries in the National Capital Region (NCR) plus area[2]. Bureaucratic bottlenecks also played a major role for the drop in government spending as agencies were required to enter into an MOU with the Department of Budget and Management (DBM) for covid-19-related procurements. Meanwhile, total investments or gross capital formation grew by 20.2 percent, largely on account of the growth in construction (2.8%) and durable equipment (18.0%). Trade has likewise rebounded with exports and imports both registering positive growth rates from a deep contraction in the same period last year.

Figure 1. GDP Growth Rate of Selected ASEAN economies (in %)



	IND	MAL	PHI	SIN	THA	VNM
2020	-2.0	-5.7	-9.6	-5.4	-6.2	2.8
Q1 2021	-0.7	-0.5	-3.9	1.5	-2.6	4.7
Q2 2021	7.1	16.1	11.8	14.7	7.5	6.6

Source of basic data: Trading Economics

While the growth figure in the first semester is certainly a welcome development, the recovery appears to be fragile since most of it is due to base effects (i.e., small gains translate to stronger growth numbers in the current period because of the very low numbers recorded in the previous period). In fact, the growth momentum is in question as seasonally adjusted data show that the second quarter GDP actually contracted by 1.3 percent on a quarter-on-quarter basis. The reimposition of stricter community quarantine measures for two weeks in August might further derail the growth trajectory which is why the Development Budget Coordination Committee (DBCC) recently cut its 2021 growth target from the previous 6.0-7.0 percent to 4.0-5.0 percent. Such adjustment is in line with the downward revisions made by multilateral agencies. As early as April this year, the Asian Development Bank (ADB) has downgraded its 2021 growth outlook for the Philippines from 6.5 percent to 4.5 percent. Likewise, the International Monetary Fund (IMF) now expects GDP growth to be 5.4 percent this year from its earlier forecast of 6.9 percent, while the World Bank (WB) lowered its outlook to 4.7 percent from its initial forecast of 5.5 percent. International credit rating agency Fitch Ratings has also revised its outlook for the Philippines from stable to negative and changed its growth projections from 5.3 percent to 4.2 percent. Fitch highlighted the risks to the medium growth prospects and the weakening fiscal and external buffers of the country.

Table 2. Growth Forecasts for Selected ASEAN Economies, 2021 and 2022 (in %)

AGENCY	IND	MAL	PHI	SIN	THA	VNM
2021 Forecasts						
ADB	4.1**	5.5**	4.5*	6.3**	2.0**	5.8**
WB	4.4	6.0	4.7	-	2.2	6.6
IMF	3.9	4.7	5.4	-	2.1	-
Fitch	3.9	0.0	4.2	6.1	3.0	5.8
Moody's	4.7	4.7	4.0	-	-	-
2022 Forecasts						
ADB	5.0*	5.7*	5.5*	4.1*	4.9**	7.0*
WB	5.0	4.2	5.9	-	5.1	6.5
IMF	5.9	6.0	7.0	-	6.1	-

*Sources: Philippine Statistics Authority, *ADB Asian Development Outlook April 2021, **ADB Asian Development Outlook Supplement July 2021, World Bank Global Economic Prospects June 2021, IMF World Economic Outlook Update July 2021, Fitch Solutions, Moody's Analytics*

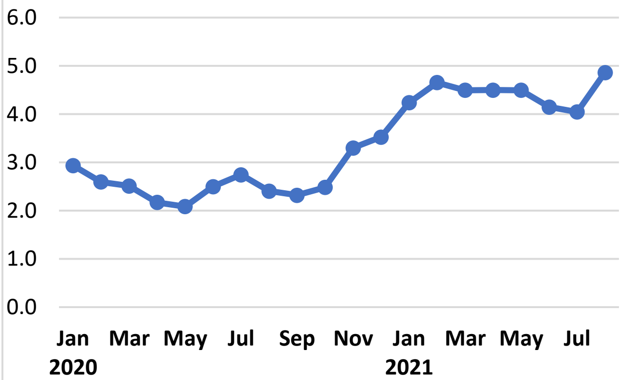
Compared to its ASEAN peers Indonesia and Thailand, the Philippines performed better in the first semester of 2021. It is also poised to have higher growth rate than the two countries for the rest of the year based on the projections of multilateral agencies. The growth projections for the Philippines were based on observable

[2] This includes Metro Manila and the nearby provinces of Rizal, Bulacan, Cavite and Laguna.

factors such as the gradual pick-up in household spending, sustained government spending on infrastructure and social assistance, the improvement (albeit still sluggish) in purchasing managers' index (PMI) and the expected acceleration of the vaccination program in the second semester.

<u>Monetary and Financial Sector</u>

Figure 2. Inflation Rates, 2020-2021



Source: Philippine Statistics Authority

Headline inflation exceeded government target. Prices of goods and services increased by 4.9 percent in August 2021, its fastest pace since December 2018. Average inflation for the first eight months of the year was 4.4 percent, well above the 2.0-4.0 percent target set by the Bangko Sentral ng Pilipinas (BSP). Food inflation, in particular remains high, averaging at 5.7 percent during the period. This is more than double the 2.6 percent in the same period in 2020. Food inflation accelerated faster in August, reaching 6.9 percent, driven mostly by the increase in the indices for meat (16.4%), vegetable (15.7%) and fish (12.4%). Prices of meat continue to be high despite the issuance of Executive Order (EO) No. 128 in April which temporarily reduced the tariff rates on imported pork products. Upside risks to inflation will likely persist in the second semester. This may include higher global commodity (i.e., oil) prices as demand recovers, supply-side factors (e.g., persistence of ASF, supply chain disruptions due to resurgence in COVID-19 cases, typhoons), and a weaker peso.

Monetary authority maintained its accommodative stance to buttress economic recovery. Since the last adjustment (i.e., cut) in November 2020, the BSP maintained the interest rate on the overnight reverse repurchase facility at 2.0 percent as well as the overnight deposit and lending facilities at 1.5 percent and 2.5 percent, respectively. The BSP has earlier announced that it is committed to hold its accommodative stance until such time that the recovery becomes sustainable, which BSP Governor Benjamin Diokno expects to come in the second semester of 2022. As such, the BSP will likely keep policy rate steady through the rest of 2021. However, the acceleration of inflation and the weakening of the Philippine currency could threaten to narrow the policy legroom of the monetary authority.

Bank lending remained subdued despite record-low policy rates, while bad loans continued to increase. Outstanding loans of universal and commercial banks[3] totaled PhP9.1 trillion as of June 2021, 2.0 percent lower than what it was last year. Accounting for 88.2 percent of total loan portfolio (equal to some PhP8.0 trillion), lending for production activities continues to fall but at a slower rate of 0.6 percent. Consumer loans likewise fell by 8.6 percent to PhP818.9 billion owing to the drop in credit card loans (-2.5%) and motor vehicle loans (-14.8%).

The fall in bank lending mainly stems from the banks' risk aversion that comes with increased market uncertainty. Results from the BSP's Senior Bank Loan Officer Survey during the second quarter of 2021 indicated that while there has been a slight increase in the demand for enterprise loans, there was, at the same time, a net tightening of overall credit standards which came in the form of reduced credit line sizes, stricter collateral requirements and loan covenants, and increased use of interest rate floors. The stricter

[3] Net of reverse repurchase placements with the BSP

standard is not surprising given the increasing incidence of loan defaults. Non-performing loans totaled PhP483 billion as of June, increasing by 22.1 percent since January and 73.8 percent higher than what it was in June 2020. This brings the ratio of non-performing loans to total loan portfolio (NPL/TLP) to 4.48 percent which is significantly higher than the average ratio of 2.21 percent in the last five years. Reports cited BSP officials expecting the ratio to reach a little over 5.0 percent this year. Nonetheless, the recent enactment of the Financial Institutions Strategic Transfer (FIST) Act is expected to reduce the average NPL ratio by at least 0.6 percentage points in 2021 until 2025. The FIST Act allows lenders to dispose of distressed assets like bad loans to a separate corporate entity to prevent a broader, system-wide contagion.

External Accounts

Trade deficit widened as economies start to reopen. Export earnings from January to June 2021 amounted to US$35.9 billion, a 21 percent increase from the export value earned over the same period in 2020. The expansion was attributed to the gradual opening of major economies abroad as foreign demand slightly recovered amidst the pandemic. Accounting for around 83 percent of total export value, the value of the top 10 export products expanded by 25.5 percent. Export of electronic products, which accounted for 56.4 percent of total export value, grew by 18.5 percent.

Figure 3. Philippine Exports by Major Type of Goods (FOB Value in US$ billion)

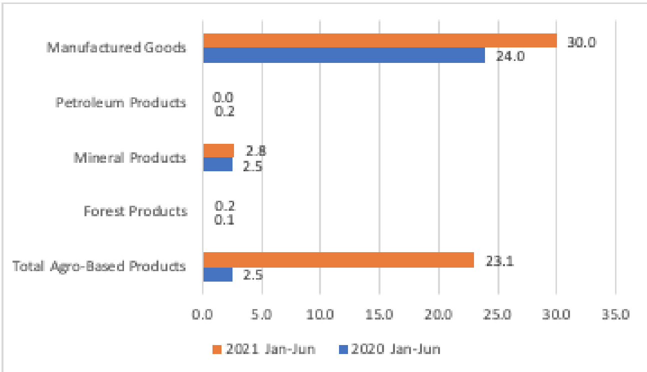
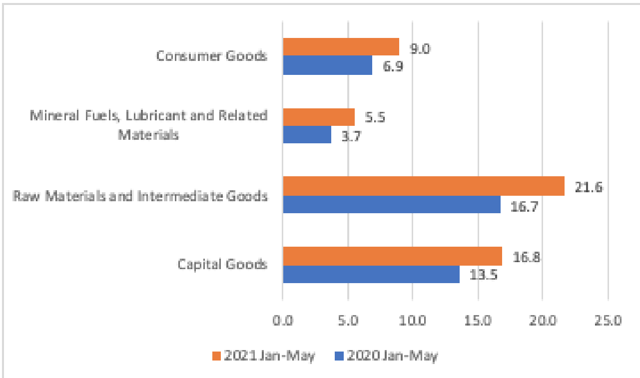


Figure 4. Philippine Imports by Major Type of Goods (FOB Value in USD billion)



Source: Philippine Statistics Authority

Meanwhile, imports summed up to US$53.3 billion, up by 29.8 percent year-on year. Gains were posted across all major types of import goods. The year-to-date import value of capital goods as well as raw materials/intermediate goods expanded by 24.4 percent and 29.7 percent, respectively, which indicated some recovery in the manufacturing sector. These brought the cumulative trade deficit to US$17.4 billion, higher than the cumulative deficit of US$11.4 billion last year.

Trade growth is expected to further bounce back during the second semester, notwithstanding the reimposition of strict community quarantine measures that may adversely affect outbound and inbound shipments and weigh on overall economic activity. The trade deficit is likely to average at around US$3.0 billion (monthly), with imports of capital goods expected to remain subdued this year—albeit with some acceleration in the second semester as infrastructure spending is expected to ramp up ahead of the elections next year. The BSP expects exports and imports to grow by 10 percent and 12 percent, respectively this year.

Cumulative foreign direct investments (FDI) in the first five months of 2021 increased year-on-year. Net FDI inflows in January to May totaled US$3.5 billion, 37.8 percent higher than its level in the same period last year. Much of the increase came as a result of the 76.2 percent increase in debt instruments (i.e., intercompany lending) and reinvestment of earnings which grew by 3.0 percent. However, on a year-to-date basis, equity capital placements declined by 5.4 percent to US$1.0 billion largely on account of the fall in foreign equity towards the manufacturing (-54.8%), information and communications (-93.0%), and construction (-87.7%) industries.[4] Note that FDI levels have been falling for three consecutive years since 2018. Last June 2021, the BSP trimmed down its FDI projections for the year to US$7.5 billion from its earlier projection of US$7.8 billion. Despite it being one of the fastest growing economies in Asia, the Philippines lags behind its peers in terms of attracting foreign investment partly because of foreign ownership restrictions, high power costs, and poor infrastructure. The passage of the proposed amendments to the Public Service Act which is still being deliberated in the Senate is expected to help FDI inflows recover.

Table 3. Foreign Direct Investments (in US$ million)

Particulars	2017	2018	2019	2020	Jan-May		
					2020	2021	Growth (%)
Non-resident investments	10,256	9,949	8,671	6,542	2,530	3,485	37.8
Equity and investment fund shares	4,261	3,242	3,427	2,454	1,281	1,285	0.3
Equity other than reinvestment of earnings	3,398	2,346	2,295	1,476	886	879	-0.9
Placement					1,076	1,018	-5.4
Withdrawals					190	139	-26.7
Reinvestment of earning	863	897	1,132	978	395	407	3.0
Debt instruments	5,996	6,706	5,244	4,089	1,248	2,199	76.2

May not add up due to rounding.
Source: Bangko Sentral ng Pilipinas

Inflow of remittances was aided by the reopening of economies worldwide. Personal remittances in the first semester of the year amounted to US$16.6 billion, 6.7 percent higher than the US$15.6 billion posted in the comparable period last year. Similarly, cash remittances coursed through banks rose by 6.4 percent during the same period, from US$14.0 billion to US$14.9 billion. This is US$16.2 billion (or 108.5%) short than what the BSP expects for this year. With the reopening of economies worldwide, the expansion of remittances is likely to continue through the rest of the year, albeit with some deceleration as the base effect wears out. The steady stream of remittances would support household consumption and it is likely to get a boost in purchasing power as the domestic currency depreciates.

Overall balance of payments (BOP) posted a deficit in the first semester, reflecting the widening of the trade deficit and decreasing international reserves. Cumulative BOP registered a US$1.9 billion deficit as of end-June, a huge turnaround from the US$4.1 billion surplus registered in the same period last year. This is partly explained by the widening of the cumulative trade deficit which reached US$17.4 billion in June. The BOP

[4] While equity capital placements increased in electricity/gas/steam/air conditioning supply (687.2%) and financial/insurance activities (990.0%), and professional/scientific/technical activities (1200.0%).

position likewise reflects the decrease in gross international reserves (GIR) to US$105.8 billion from US$107.2 billion the previous month and from US$110.1 billion in December last year.[5] Nonetheless, the current level of reserves sufficiently covers 12 months' worth of imports and is 7.7 times the country's short-term external debt based on original maturity and 5.1 percent on residual maturity.

The performance of the Philippine peso is threatened by the rise in dollar demand and by an earlier-than-expected rate hike by the United States Federal Reserve (US Fed). On a year-to-date basis, the Philippine peso appreciated against the US dollar by 3.24 percent, averaging at PhP48.69 for the first eight months of 2021. However, the domestic currency has started to weaken since June with the increase in demand for imports and consequently, for foreign exchange. As of August 31, the foreign exchange rate is at PhP50.04 to a US dollar. The weak performance of the domestic stock market may have likewise accelerated corporate demand for US dollars. Moreover, the US Federal Open Market Committee (FOMC) has kept policy rates close to zero in its meeting last July 28 even as it raised its inflation expectation a full percentage point higher than what it projected in March. This gave rise to expectations of a rate hike by the US Fed which could result in a flow of funds towards green-backed assets, precipitating further depreciation of the Philippine peso. The downward revisions to the country's economic outlook are also likely to result in financial outflows that could further spur the weakening of the domestic currency.

Fiscal Position

National government revenue increased year-on-year and was higher than what was programmed for the first semester. For the first semester of 2021, national government revenues amounted to PhP1.49 trillion, exceeding the first semester target set by the DBCC[6] by PhP68.6 billion. It is also PhP37.1 billion or 2.5 percent higher than that collected in the same period last year.[7] Tax revenue accounted for 90.1 percent of total government revenue with collections of the Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) increasing by 7.9 percent and 19.2 percent, respectively. BIR collection was higher mainly due to increases in the collection of individual income tax (by 12.6%), excise tax on alcohol (by 44.3%) and tobacco (by 40.1%), value-added tax (by 12.2%) and documentary stamp tax (by 72.8%).[8] These increases were partially offset by a 71.4 percent fall in the collection of taxes on petroleum products.

Meanwhile, non-tax revenues declined by 37.8 percent year-on-year largely due to the fall in the income of the Bureau of the Treasury (BTr). Non-tax revenues were significantly higher in 2020 as Republic Act No. 11469 or the Bayanihan 1 Law mandated government-owned or -controlled corporations (GOCCs) to remit to the BTr the national government advances as well as unspent subsidies and payments of guarantee fees to bolster the government's COVID-19 response. The Department of Finance (DOF) is actually proposing to further increase the mandatory dividend remittance of GOCCs to 75 percent from 50 percent to raise revenues for the government's additional economic stimulus spending. This would, however, require an amendment of RA No.

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[5] The GIR was US$87.8 billion in December 2019. This was equivalent to 7.6 months' worth of imports.

[6] The disruptions in economic activities due to lockdowns subsequently triggered revisions in the 2021 revenue program of the government. The government initially targeted on May 27, 2020 to collect PhP2,929.0 billion for 2021. This was revised downwards on July 28, 2020 to PhP2,717.4 billion, but was adjusted again upwards to PhP2,881.5 billion on December 3, 2020.

[7] The full-year revenue program already factored in the impact of the Corporate Recovery and Tax Incentives for Enterprises (CREATE) Law, with an updated revenue loss of PhP138.2 billion.

[8] The increase in the collection of excise taxes on alcohol and tobacco products is due to the implementation of Republic Act No. 11467 and Republic Act No. 11346, respectively.

7656 or the Dividend Law. Nonetheless, collection from the BTr income in the first semester this year already surpassed the full-year programmed amount. According to the BTr, the income was derived from bond sinking fund investments and government deposits as well as interest income on advances to GOCCs. The outlook for revenue collection remains muted for the rest of the year with the lingering threat of COVID-19 resurgences which would likely warrant stricter measures that may reduce economic activity and depress revenue collection.

Table 4. National Government Revenue Performance, First Semester 2020-2021 (in PhP billion)

Particulars	Actual First Semester			Growth		First Semester Program 2021*	Variance (Actual vs. Program)
	2019	2020	2021	2019-2020	2020-2021		
Total Revenues	1,547.5	1,453.3	1,490.4	-3.7	2.5	1,421.8	68.6
Ratio to GDP	16.1	17.0	16.4				
Tax Revenues	1,381.0	1,217.7	1,343.5	-2.7	10.3	1,320.1	23.4
Ratio to GDP	14.5	14.2	14.7				
BIR	1,066.3	956.4	1,031.8	-3.2	7.9	1,017.7	14.1
BOC	303.0	253.1	301.7	-0.4	19.2	291.8	9.9
Other Offices	11.6	8.2	9.9	-14.7	21.5	10.6	-0.7
Non-Tax Revenue	166.6	235.6	146.7	-11.9	-37.8	101.7	45.0
BTr Income	87.6	183.2	81.6	-6.9	-55.5	52.2	29.4
Fees and Charges	24.4	14.0	21.9	-10.3	56.6	n.a.	n.a.
Privatization	0.3	0.3	0.2	-33.3	-30.6	n.a.	n.a.
Malampaya Income	13.8	8.9	10.0	-27.5	12.4	n.a.	n.a.
Other Non-Tax	40.4	29.2	32.9	-18.6	12.9	n.a.	n.a.

Source: Bureau of the Treasury
**Based on the program set in May 18, 2021 by the DBCC.*

Government spending accelerated but still fell short of the programmed amount for the first semester of 2021. Disbursements for the first semester amounted to PhP2,206.4 billion, up by 9.6 percent from the same period last year and accounted for almost one fourth (24.2%) of the nominal GDP in the first semester. The higher spending is largely due to infrastructure and other capital outlays expenditures which grew by 43.2 percent to reach PhP426.6 billion. Compared to the programmed spending though, actual disbursement is PhP233.4 billion short of the target. This is attributed primarily to lower expenditures on subsidies and slower spending on maintenance and other operating expenses (MOOE) and personnel services (PS) of various agencies. As reported by the Department of Budget and Management (DBM), the expenditure for subsidies was short of PhP89.9 billion from its programmed amount due to the timing of releases pending submission of special budget requests (SBRs) by GOCCs such as the Philippine Health Insurance Corporation (PHIC), National Irrigation Administration (NIA), Bases Conversion and Development Authority (BCDA), National Housing Authority (NHA) and National Electrification Administration (NEA).

On the other hand, national government agencies (NGAs) such as the Department of Health (DOH) and the Department of Agriculture (DA) ran into procurement issues as the deliveries of goods and supplies under their MOOE budgets were delayed. Outstanding checks were also recorded in the Department of Social Welfare and Development (DSWD), Department of Education (DepEd) and the Commission on Higher Education (CHED). Personnel-heavy agencies like the DepEd and the Philippine National Police (PNP) likewise posted underspending during the said period as the adjustments in their salaries—per the Salary Standardization Law 5 (SSL 5) and other personnel benefits under the Miscellaneous and Personnel Benefits Fund (MPBF) and Pension and Gratuity Fund (PGF)—were given on a later date. Based on the DBM's Statement of Appropriations, Allotments, Obligations, Disbursements and Balances (SAAODB) as of June 30, 2021, unobligated allotments and unreleased appropriations of NGAs amounted to PhP1,388.9 billion and PhP282.1 billion, respectively.

Spending for equity was also below target by PhP10 billion as the Government Financial Institutions Unified Initiatives to Distressed Enterprises for Economic Recovery (GUIDE) Bill is still pending in the Senate. Apparently, the DBM has already set aside funds for this legislative measure.

A welcome development is the smaller spending for interest payments in the first semester as a result of lower rates for the Fixed Rate Treasury Bonds, the rejection of bids, lower interest rates, and exchange rate adjustments.

Table 5. National Government Expenditure Performance
First Semester 2021 (in PhP billion)

Particulars	First Sem. Actual		Growth Y-o-Y (%)	First Sem. Program 2021	Actual vs. Program
	2020	2021			
Interest Payments	187.7	208.5	11.1%	257.9	-49.4
Allotments to Local Government Units (LGUs)	409.2	448.5	9.6%	452.9	-4.4
Tax Expenditures	6.5	15.6	140.0%	8.8	6.8
Net Lending	-29.9	6.8	-122.7%	12.3	-5.5
Equity	0.6	46.0	7566.7%	56.0	-10.0
Subsidy	169.5	88.3	-47.9%	178.2	-89.9
Other Expenditure Accounts	1,270.2	1,392.7	9.6%	1,473.8	-81.1
Total Expenditures	2,013.7	2,206.4	9.6%	2,439.8	-233.4

Source: Bureau of the Treasury and Department of Budget and Management
**Based on the program set in the 179th DBCC Meeting held on May 18, 2021.*

Fiscal deficit continued to grow while the ratio of the debt stock-to-GDP soared. The need to spend for the country's COVID-19 response has pushed the fiscal deficit deeper into the red as it reached 7.6 percent of GDP in 2020. This further increased to PhP716.0 billion or 7.9 percent of GDP as of June 2021, much higher than the pre-pandemic average of 3.0 percent-to-GDP ratio that was historically perceived to be manageable. Note that the increasing deficit consequently entails a rise in debt levels. As of June 2021, the outstanding debt of the national government stood at PhP11.2 trillion, accounting for 60.4 percent of the estimated FY 2021 nominal GDP and 23.3 percent more than what it was in June last year. Of the total debt stock, 71.1 percent (PhP7.9 trillion) are domestic borrowings, while 28.9 percent (PhP3.2 trillion) were from external sources.

Employment and Poverty

Labor market improved but job quality continues to be a cause for concern. Average labor force participation rate (LFPR) increased in the first seven months of 2021 to 63.1 percent from 59.8 percent in the same period in the previous year. This is equivalent to some 47.3 million individuals. In July, however, many dropped out of the labor market with the LFPR falling again to 59.8 percent. Of those in the labor force from January to July, 92 percent are employed while 8.0 percent are unemployed. In absolute terms, 3.76 million Filipinos were without jobs from January to July of 2021.

Table 6. Selected Labor Market indicators, 20202-2021 (in thousands)

Particulars	FY 2019	FY 2020	Jan-Jul 2019 Average	Jan-Jul 2020 Average[a]	Jan-Jul 2021 Average[b]
Labor Force	44,219	43,878	44,098	43,954	47,250
Employed	41,934	39,378	41,733	39,255	43,494
Underemployed	5,792	6,395	5,910	6,611	7,117
Unemployed	2,259	4,500	2,330	4,729	3,755
Not in the Labor Force	27,959	29,854	27,938	29,587	27,647
Labor Force Participation Rate (%)	61.3	59.5	61.2	59.8	63.1
Employment Rate (%)	94.9	89.6	94.7	89.0	92.0
Underemployment Rate (%)	13.8	16.4	14.2	17.0	16.4
Unemployment Rate (%)	5.1	10.4	5.3	11.0	8.0
Selected Occupational Groups (% Share):					
Managers	11.4	9.0	11.4	9.1	8.0
Technicians & Associate Professionals	4.2	3.8	4.3	3.7	3.8
Elementary Occupations	26.5	27.3	26.7	27.8	28.6
Class of Workers (% Share):					
Wage and Salary Workers	64.7	62.8	64.6	62.9	62.4
Self-Employed	26.8	28.4	26.8	28.1	28.2
Unpaid Family Worker	5.7	6.3	5.7	6.7	7.1
Worked Less than 40 Hours	12,517	13,552	12,438	13,668	16,199

Source: Philippine Statistics Authority

[a] *Average of the January, April and July quarterly Labor Force Survey (LFS)*

[b] *Average of the January to July monthly LFS. For 2021, the Philippine Statistics Authority started to conduct monthly Labor Force Survey (LFS) in between the regular quarterly LFS amidst the call for higher frequency statistical information that will enable better monitoring and understanding of the current labor market situation.*

Data likewise suggest a deterioration in the nature or quality of jobs. The share of wage workers among the employed declined to 62.4 percent from 62.9 percent in January to July 2020. In contrast, the proportion of unpaid family workers increased to 7.1 percent from 6.7 percent while the share of self-employed workers rose to 28.2 percent from 28.1. Skilled workers were also forced into low-skilled jobs as evidenced by the falling share of managers and technicians/associate professionals coupled with the increasing number of those in elementary occupations and service/sales workers. There is also a considerable increase in the number of workers who worked less than 40 hours. Moreover, while the average underemployment rate improved in the seven-month period, the latest labor force survey show that underemployment rate has risen to 20.9 percent in July 2021. This is even worse compared to the 18.9 percent underemployment rate recorded in April last year at the height of the pandemic lockdown. These shifts in the labor market will certainly have bearing on the country's poverty incidence. They highlight the scar that the COVID-19 pandemic has left and healing may take longer than expected.

Self-rated hunger and poverty slightly eased but remained elevated compared to pre-pandemic levels. Self-rated hunger dropped to 13.6 percent in June from 16.8 percent in May 2021. This is equivalent to around 3.4 million families who experienced hunger due to the lack of food to eat. The hunger incidence is lower than 2020's annual average of 21.1 percent, but much higher than the pre-pandemic level of 9.4 percent. Mindanao and Balance Luzon experienced the worst hunger rate at 15 percent, followed by the NCR at 14 percent, and Visayas at 8.3 percent.

Similarly, the proportion of Filipino families who identify themselves as poor increased to 48 percent in June much higher than the pre-pandemic level of 44.8 percent in 2019. This is one percentage point lower than the preceding survey (May 2021) and is equivalent to the full year 2020 level[9] of the total 12 million poor families wherein 1.8 million were newly poor. Both the NCR and Visayas exhibited an increase in self-rated poverty from 38 percent and 56 percent in May to 43 percent and 70 percent in June, respectively.

Table 7. Self-Rated Hunger and Poverty (in %)

Rates (%)	2019 Ave.	2020 Ave.	2020				2021	
			May	Jul	Sep	Nov	May	Jun
Self-Rated Hunger	9.4	21.1	16.7	20.9	30.7	16	16.8	13.6
Self-Rated Poverty	44.8	48	-	-	-	48	49	48

Source: Social Weather Stations

<u>Prospects, Risks and Policy Implications</u>

The upturn in the country's GDP in the first semester of 2021 points to an economic recovery, but one that is fragile and fraught with uncertainty. Downside risks predominate. First, is the rising threat of new and highly transmissible COVID-19 variants which would make the country vulnerable to resurgences. The record number of COVID-19 cases registered in recent weeks is exerting too much pressure on the already-stretched health care system. According to the government, it is on track with its COVID-19 vaccination program with a total of 31.1 million doses (17.8 million for the first dose and 13.3 million for the second dose) already administered as of August 24. During the Senate Blue Ribbon Committee hearing last August 25, Secretary Carlito Galvez Jr. reported that the expected deliveries before the year ends would be enough to fully vaccinate

[9] The SWS was able to conduct a self-rated poverty survey only once in 2020, instead of the regular quarterly surveys, as it was only in November when the agency was able to resume face-to-face interviews since the onset of the pandemic.

some 69.8 million individuals.[10] The government is aiming to vaccinate 70 percent of the population to achieve herd immunity. However, with the emergence of the highly contagious variants, public health experts[11] state the need to raise the target to around 85 to 90 percent of the population, making it a more challenging goal. Moreover, with some countries mulling to administer booster shots, there are fears that global vaccine supplies would again be constrained.

Another risk is the rising inflation. Inflation is seen to breach the target in 2021. Though it is likely to be temporary, the acceleration in prices of goods and services would shrink even more the purchasing power of Filipinos and make the cost of living more expensive. This would further drag down consumer spending and potentially imperil economic recovery. High inflation may also constrain the BSP's ability to ease monetary policy to support growth.

Rising indebtedness along with increased uncertainty and risk aversion may likely inhibit investment. The deterioration of banks' asset quality may still increase until such time that forbearance policy measures[12] are allowed to unwound. In addition, significant fiscal support that could further accelerate inflation in the US may prompt the US Fed to raise policy rates earlier—with spillover in the form of downward pressures on the Philippine peso. The reopening of the economy is likewise expected to widen the current account deficit, exerting more pressure on the peso.[13] The Philippines' elevated debt level makes it vulnerable to the associated risks that come with the divergent pace of recovery amongst trading partners. For instance, rising yields in the US could reflect in steeper yield curves in the Philippines and domestic credit conditions may tighten further if US yields were to rise even more. Indeed, the re-emergence of the so-called twin deficits (i.e., fiscal and current account deficits) could force the BSP into reversing its accommodative stance sooner than expected, abating the downward pressure on the peso but at the same time, undermining the economy's growth prospects.

Natural calamities that usually come in the second semester, as well as the associated risks that come from the divergent pace of recovery amongst the country's trading partners also pose headwinds to growth.

On the upside, economic growth for the rest of the year will likely be aided by higher consumer spending as more people get vaccinated and as the usual holiday spending kicks in in the fourth quarter. Public infrastructure spending is also expected to be ramped up ahead of the election ban.

As the country continues to grapple with the pandemic, strategic interventions are needed to nurture the recovery by managing the risks and mitigating economic scarring. First, given the heightened uncertainty and dwindling fiscal resources, fiscal policies need to be most pragmatic. While it is understandable to be concerned about the fiscal deficit, a premature turn towards fiscal austerity may impede economic

[10] Presented by Secretary Galvez Jr. during the hearing of the Committee on Accountability of Public Officers and Investigations (Blue Ribbon) on August 25, 2021.

[11] As the more contagious Delta variant circulates, public health experts say herd immunity has become an even more distant goal. Market Watch (August 4, 2021). Retrieved from: https://www.marketwatch.com/story/as-the-more-contagious-delta-variant-circulates-public-health-experts-say-herd-immunity-has-become-an-even-more-distant-goal-11628102212.

[12] Banks were given regulatory relief to enable them to grant equivalent financial relief to their borrowers in the form of more flexible and favorable lending terms, or to restructure loan accounts.

[13] Recall that in 2018, the widening of the current account deficit (which put the Philippine peso on a depreciating trend) and surging inflation has prompted the monetary authority to raise its policy rate by a total 175 bps that year. The rate hikes had the effect of slowing capital formation and contributed to the deceleration of the growth momentum in 2019.

recovery. The annual 2022 national budget which prioritizes the strengthening of the health care system and protecting the vulnerable must be passed in a timely manner. Alongside this is the effective implementation of the government's PDITR strategies to enable increased mobility and boost market confidence.

Infrastructure spending must likewise continue to gain headway particularly on infrastructure projects that promote physical and digital connectivity. The pandemic has highlighted the country's weakness in digital connectivity even as schools and businesses are forced to go online. Related to this is the need to accelerate the registration process for the national identification system to help strengthen public service delivery for social assistance. While there are still many without jobs, social amelioration programs (i.e., cash aid) might still be needed, although on a more limited scale than previous ones. Policies that will enable workers to keep their jobs are preferred over unconditional cash transfers. The institutionalization of wage subsidies and/or unemployment benefits is/are worth considering.

Sustaining the reform momentum would aid in re-igniting investment appetite. To this end, the passage of the proposed amendments to the Public Service Act, Retail Trade Liberalization Act, and Foreign Investments Act must be fast-tracked. In addition, the proposed GUIDE Act would seek to strengthen the capacity of government financial institutions (GFIs) to provide financial assistance to distressed enterprises. Moreover, there is also a need to ensure the effective implementation of the Ease of Doing Business and Efficient Government Service Delivery Act. Furthermore, while the BSP may eventually have to face the tradeoff between financial stability and the need to support domestic enterprises, the IMF has recommended that the BSP maintain its accommodative stance and to let extraordinary monetary policies be unwound first.[14]

Lastly, as the global community faces a virus that continues to evolve, forward-looking and long-term measures must be put in place for the country to be able to better withstand future shocks. The pick-up in global trade is expected to give economic recovery a boost. To seize this opportunity after almost a decade of slow trade growth, the country needs to introduce policies that will reduce trade costs. In November last year, the Philippines signed the Regional Comprehensive Economic Partnership (RCEP) Agreement which is expected to lower the cost of trade as it reduces tariffs amongst member countries and provides for standardized and harmonized trade requirements. Once the Executive officially transmits the RCEP Agreement to the Legislature, the Senate is expected to concur with its ratification.

There is also a need to mitigate the effects of learning loss. The Department of Education (DepEd) estimates that around 1.9 million children were affected by the closure of schools in 2020. The experience in the past year has highlighted the limitations of remote learning and some studies suggest[15] that short-term learning losses could continue to accumulate even when children return to school. Education reform should hence be included at the core of the recovery framework. Aside from exploring the option of limited face to face classes, improvements in the curricula and assessment metrics should continuously be introduced as well as provision

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[14] As part of the whole-of-government response to the COVID-19 pandemic, the BSP has extended provisional advances to the national government on a time-bound basis and within the limits prescribed by law. The BSP has also been purchasing government securities in the secondary market to help shore up domestic liquidity and restore market confidence to continue participating in the primary auctions for government securities.

[15] Kaffenberger, M. (2020). Modelling the long-run learning impact of the Covid-19 learning shock: Actions (to more) than mitigate loss. International Journal of Educational Development Vol.81.
https://www.sciencedirect.com/science/article/pii/S0738059320304855?via%3Dihub

for acceleration, remedial and enrichment programs that will allow children to catch up on missed learning. Investments and support for distance learning modalities should be strengthened. To help narrow the digital divide, the enactment of the proposed Open Access in Data Transmission Act would lower the barriers to entry for data-only service providers and thus lower the price of their services. This legislative proposal may also be taken in conjunction with the proposed amendments to the Public Telecommunications Policy Act, which aims to strengthen the National Telecommunications Commission (NTC) as a regulator especially with respect to spectrum management and tariff setting.

Furthermore, for the longest time, there have been recommendations to increase public spending on innovation and research and development (R&D). It is high time to consider developing a national framework for R&D that includes not only the provision of fiscal incentives for R&D activities but also improving on existing science-based school curriculum, provision of incentives for scientists/inventors, as well as better intellectual property rights protection. This translates considerably to better production and certification standards and therefore, products. This will not only be true for the pharmaceutical industry (which, incidentally, lacks the capacity to produce its own vaccine supply), but also for agriculture and other manufacturing sectors as well.

This Economic Report was principally prepared by the Macroeconomics Sector with inputs from its Sector Head, under the supervision of SEPO's Directors and the overall guidance of its Director General.