



# Monitoring the Philippine Economy

## Second Quarter Report for 2017

### Project of Angelo King Institute

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### Second quarter economic performance: sustained growth from the previous quarter but slower growth than in the previous year.

**Philippine economy registers slower growth.** Second quarter growth in 2017 slowed to 6.5 percent from 7.1 percent the previous year. Growth deceleration in household consumption, domestic investment, and government spending, even with lower total imports, contributed to the sluggish growth pace. Moreover, lower growth rates of industry and services, which offset growth in agriculture, resulted in the decreased growth rate.

- **Major components of aggregate demand**
  - **Household spending remains sluggish.** Private consumption in the second quarter grew at 5.9 percent year-on-year (y-o-y) compared to its 7.5 percent growth the previous year. The Philippine Statistics Authority (PSA)<sup>2</sup> reported growth increases in some components of Household Final Consumption Expenditure (HFCE) such as clothing and footwear (-2.1 percent to 1.1 percent y-o-y), restaurants and hotels (9.0 percent to 11.4 percent y-o-y), and Furnishings, household equipment and routine household maintenance (2.2 percent to 3.1 percent y-o-y). These were offset, however, by the growth declines in recreation and culture (14.8 percent to -1.1 percent y-o-y), alcoholic beverages and tobacco (6.6 percent to 0.6 percent y-o-y), and communication (6.0 percent to 1.6 percent y-o-y).
  - **Substantial surge in intellectual property products boosted domestic investment growth.** According to PSA<sup>3</sup>, investments in Intellectual Property Products (IPP) surged from 34.2 percent to 68.3 percent growth rate y-o-y. Durable equipment, construction, and breeding stock & orchard development recorded a y-o-y growth of 8.7 percent, 7.3 percent, and 4.5 percent, respectively.
  - **Contraction in growth of fiscal expenditures due to absence of election-related spending during the period.** From a high Government Final Consumption Expenditure (GFCE) growth of 13.5 percent the previous year, Q2 2017 reflected a slower growth of 7.1 percent. GFCE growth slowed probably because of the

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<sup>2</sup> <http://psa.gov.ph/nap-press-release/sector/Household%20Final%20Consumption>

<sup>3</sup> <http://psa.gov.ph/nap-press-release/sector/Capital%20Formation>

absence of election-related expenditures and decrease in maintenance and other operating expenditures of various government line agencies.<sup>4</sup>

- **Trade balance in goods improves.** At the end of June, exports and imports were recorded at 4.9 billion USD (0.8 percent growth y-o-y) and 7.1 billion USD (-2.5 percent growth y-o-y), respectively. Major contributors in the expansion of export sales were electronic equipment and parts (28.6 percent growth y-o-y) and metal components (18.7 percent growth y-o-y). On the other hand, decrease in imports were largely caused by iron and steel (-18.2 percent y-o-y) and electronic products (-10.4 percent y-o-y). Second quarter set a trade balance of -2.2 billion USD.

- **Major components of aggregate supply**

*In this report, we present results from an alternative to the “traditional” (TRAD) method of decomposing growth of GDP in constant prices into sector contributions. This alternative method is a “generalized” (GEN) growth decomposition that applies to GDP in constant prices (e.g., in the Philippines) and to GDP in chained prices (e.g., in Canada and the US). While TRAD recognizes only “quantity” growth as the source of a sector’s contribution to GDP growth, GEN posits that a sector’s contribution comes from “quantity” growth and from “real price” growth where this price is, by definition, the ratio of a sector’s deflator to the overall GDP deflator. The GDP deflator as the common denominator of the above ratio makes real GDP the numeraire and, thus, this ratio is the relative price or exchange value of the GDP of a sector in “GDP units,” i.e., the “real price” of a sector’s GDP. Therefore, a sector’s positive “quantity” growth contribution will be diminished if accompanied by a negative “real price” growth of the same sector that may even result in a negative net contribution by the sector to GDP growth. On the other hand, a sector’s positive “quantity” growth contribution will be enhanced if accompanied by a positive “real price” growth (see Table 3).<sup>5</sup>*

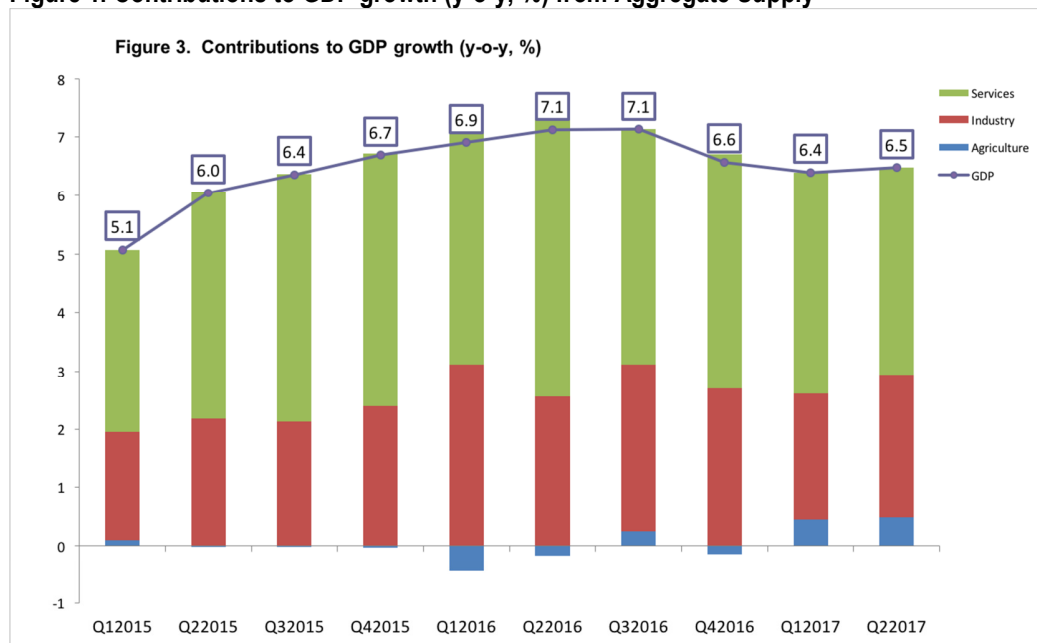
- **Services sector maintains its role as the major contributor of the supply-side growth.** Services sector registered highest contribution to growth, with 5.28 percentage points from positive quantity and real price growth (see Table 3). Although the sector grew 6.1 percent, which was lower compared to the previous year’s impressive 8.2 percent growth, its share to GDP still remains at a robust rate of 58.1 percent from last year’s 58.3 percent. Top contributors for service sector for Q2 2017 remained the same as the previous quarter and year: trade and repair of vehicles, personal, and household goods (TR), real estate renting and business activity (RERBA), and other services (OS) with 27.6 percent, 20.2 percent, and 18.9 percent, respectively.

<sup>4</sup> <http://psa.gov.ph/nap-press-release/sector/Government%20Final%20Consumption>

<sup>5</sup> The results in Table 3 are AKI-DLSU *Philippine Economic Monitor* calculations by applying the data in Table 1 to a “generalized” (GEN) exactly additive decomposition of GDP growth into *pure growth effect* (PGE) and *price change effect* (PCE) as an alternative to the “traditional” (TRAD) GDP growth decomposition. Analytically, PGE is the result of real GDP or “quantity” growth holding real price constant and PCE is the result of relative price or “real price” growth holding quantity constant. The GEN formulas for PGE and PCE and the TRAD formula are given, respectively, by equations (12), (13), and (17) in Dumagan, Jesus C. (2016), “Effects of Relative Prices on Contributions to the Level and Growth of Real GDP,” Working Paper Series No. 2016-036, Angelo King Institute for Economic and Business Studies, De La Salle University, Manila. This alternative framework follows from the decomposition of “aggregate labor productivity” (ALP) growth in Dumagan, Jesus C. (2013), “A Generalized Exactly Additive Decomposition of Aggregate Labor Productivity Growth,” *Review of Income and Wealth*, 59 (Issue 1): 157-168, where ALP is the ratio of GDP to total labor employment. Thus, by removing the labor variable, the decomposition of ALP growth in the latter paper yields the decomposition of GDP growth into PGE and PCE in the former paper which is implemented in Table 2.

- Manufacturing continues to lead industry sector.** The industry sector grew by 7.3 percent, slightly lower than the 7.6 percent growth the previous year. The sector contributed 2.5 percentage points to GDP growth. Manufacturing (MAN) is the top contributor to the industry, with 65.9 percent share in the sector while construction is the largest contributor in the group with 1.07 percentage points to total GDP growth (Table 3).
- Agriculture sector achieves high growth in six years.** With favorable weather conditions, agriculture sector showed its potential after realizing growth of 6.3 percent in Q2 2017, a high recorded sector growth rate since Q2 2011 (8.1 percent). From a negative growth of 2.0 percent the previous year, the sector progressed by exhibiting positive growth of 6.3 percent (see Figure 1). Nonetheless, the share of the sector remained low at 7.8 percent from last year's 7.9 percent. Agriculture sector manifested low contribution to growth, with 0.80 percentage points from positive quantity and real price growth (see Table 3).

**Figure 1. Contributions to GDP growth (y-o-y, %) from Aggregate Supply**



Source: Author's calculations based on data in Table 3 below.

**Challenges facing the economy**

- **Peso depreciates against the US dollar<sup>6</sup>.** The peso appreciated by 0.27 percent to average ₱49.86/US\$1, on a quarter-on-quarter basis, from the previous average of ₱49.99/US\$1. The appreciation was mainly caused by the expectations of upbeat Philippine GDP growth for the 1Q 2017 and optimistic prospects regarding the tax reform efforts of the Philippine government. Furthermore, on a year-on-year basis, peso depreciated by 6.70 percent, from the previous year's ₱46.52/US\$1 average.
- **Unfavorable economic factors may threaten the economy<sup>7</sup>.** Depreciation of the peso, proposed tax reform (eg: vehicle excise taxes and fuel), transport fare hike, another Fed rate hike anticipated in the second half of 2017, and US protectionism remain as challenges the Philippine economy has to face.
- **Weather disturbances serve as an adversity to the Philippine economy.** Unexpected inclement weather conditions, natural disasters, and the like may interrupt agricultural activities in the country. These harsh conditions may worsen poverty and threaten food security, especially for the poor Filipinos. Infrastructural improvements are deemed vital to augment agriculture sector's resiliency.

#### **Other economic news**

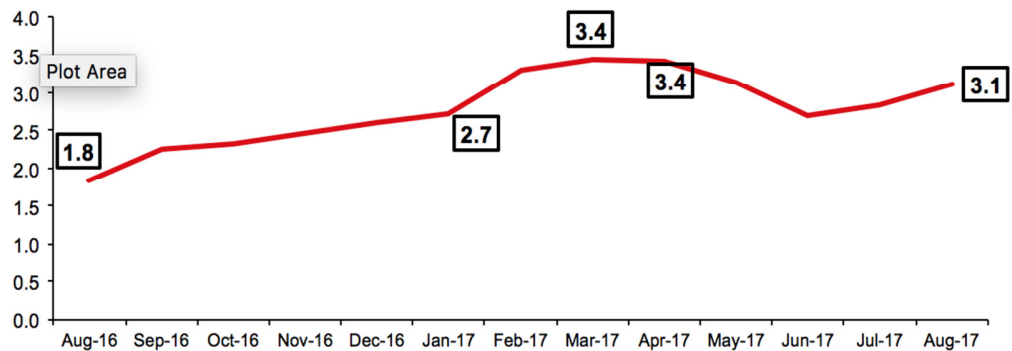
- **Stock market reports increase PSEi<sup>8</sup>.** For the second quarter, PSEi increased quarter-on-quarter by 7.1 percent to average 7,770.8 index points. Withstanding external volatilities, the country's tax reform program and sustained growth for the first quarter slightly boosted investor confidence.
- **Inflation level stays within target range.** With the consumer price index rising by 3.1 percent in 2Q 2017, BSP reports that it is within the national government's target range of 3.0 percent  $\pm$  1.0 percentage point (Figure 3). The lower inflation expectations for the years 2017 and 2018 could be because of the slower rate of increase in global oil prices even though prices of basic commodities have been continually rising. National Economic and Development Authority (NEDA) notes that one source of non-food price inflation was a rise in railway transport prices. The rise was the first fare adjustment in 20 years for the Philippine National Railways. Meanwhile, food subgroup inflation slowed down because of slower price adjustments for oils and fats, meat, fruit, sugar, honey, vegetables, and rice. However, diminishing rice stocks may trigger upward pressures on food prices in the upcoming quarter.

#### **Figure 2. Consumer price index (y-o-y, %)**

<sup>6</sup> <http://www.bsp.gov.ph/downloads/Publications/FAQs/exchange.pdf>

<sup>7</sup> [http://www.bsp.gov.ph/downloads/Publications/2017/IR2qtr\\_2017.pdf](http://www.bsp.gov.ph/downloads/Publications/2017/IR2qtr_2017.pdf)

<sup>8</sup> [http://www.bsp.gov.ph/downloads/Publications/2017/IR2qtr\\_2017.pdf](http://www.bsp.gov.ph/downloads/Publications/2017/IR2qtr_2017.pdf)



Source: Graph prepared by author based on Philippine Statistics Authority data.

- Consumer confidence record hits double-digit high<sup>9</sup>.** 2Q 2017 is the fourth consecutive quarter wherein consumer confidence showed rising optimism. BSP reported that increasing optimism levels are caused by improvements in the peace and order situation, additional family income due to higher salary and stronger business activity, availability of more jobs and increase in the number of employed family members, and effective government policies. Additional contributors include improved government assistance (eg: 4Ps and increased pensions), expected higher OFW remittances, and anticipated good harvest.

<sup>9</sup> <http://www.bsp.gov.ph/publications/media.asp?id=4377>

**Table 1. Philippine Economic Indicators**

<b>Monthly Leading Indicators</b>	<b>Oct-16</b>	<b>Nov-16</b>	<b>Dec-16</b>	<b>Jan-17</b>	<b>Feb-17</b>	<b>Mar-17</b>	<b>Apr-17</b>	<b>May-17</b>	<b>Jun-17</b>	<b>Jul-17</b>	<b>Aug-17</b>
Industrial Production (y-o-y, %)	9.9	15.1	21.8	14.8	9.6	12.3	3.0	9.3	6.8	-1.1 ...	
Consumer Price Index (y-o-y, %)	2.3	2.5	2.6	2.7	3.3	3.4	3.4	3.1	2.7	2.8	3.1
Retail Sales (y-o-y, %)	11.5	15.6	21.8	20.7	18.6	19.7	0.6	3.2	-0.9 ...		
Exports (y-o-y, %)	7.6	-7.5	6.3	22.0	8.7	18.1	19.1	14.0	5.8	10.4 ...	
Imports (y-o-y, %)	5.9	19.7	13.8	12.2	15.2	18.0	-0.1	16.6	-1.3	-3.2 ...	
Trade Balance, US\$ million	-1,983	-2,566	-2,158	-2,469	-1,768	-2,297	-1,754	-2,737	-1,992	-1,646 ...	
Total Reserves (less gold), US\$ billion	77	74	73	74	74	73	74	74	73	73	73
Policy Rate	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0	3.0
Fiscal Balance (million pesos)	-2,345	-19,145	-118,229	2,222	-23,724	-61,471	52,797	-33,421	-90,873	-50,512 ...	
<b>Quarterly/Annual Economic Indicators</b>	<b>2014</b>	<b>1Q2015</b>	<b>2Q2015</b>	<b>3Q2015</b>	<b>4Q2015</b>	<b>1Q2016</b>	<b>2Q2016</b>	<b>3Q2016</b>	<b>4Q2016</b>	<b>1Q2017</b>	<b>2Q2017</b>
Real GDP (y-o-y, %)	6.1	5.1	6.0	6.4	6.7	6.9	7.1	7.1	6.6	6.4	6.5
- Private Consumption	5.4	6.0	6.4	6.2	6.6	7.1	7.5	7.2	6.2	5.8	5.9
- Government Consumption	1.7	0.0	2.2	15.5	15.5	11.8	13.5	3.1	4.5	0.1	7.1
- Gross Capital Fixed Formation	5.4	15.7	28.6	15.3	16.2	31.5	30.3	21.7	14.7	10.6	8.7
Current Account (% of GDP)	4.4	3.2	3.1	0.1	4.8	0.9	0.1	1.3	1.2	-0.3 ...	
Financial Account ( US\$ million)	10,084	152	1,258	-291	1,404	995	-1,039	308	54	823	-688
- Net Direct Investments, US\$ million	789	358	-476	-11	7	-1,119	-1,030	-498	-1,829	-1,084	-2,110
- Net Portfolio Investments, US\$ million	2,460	-459	3,375	2,202	-361	1,573	787	-843	-309	3,275	-244
Overall BOP position (US\$, million)	-2,858	877	807	124	809	-210	843	1,014	-2,068	-994	289
Unemployment rate	6.8	6.4	6.5	5.6	5.8	5.8	5.4	4.7	4.7	6.6	5.6
<b>Others</b>	<b>Sep-16</b>	<b>Oct-16</b>	<b>Nov-16</b>	<b>Dec-16</b>	<b>Jan-17</b>	<b>Feb-17</b>	<b>Mar-17</b>	<b>Apr-17</b>	<b>May-17</b>	<b>Jun-17</b>	<b>Jul-17</b>
Overseas Filipinos' Remittances (US\$, million)	2,383	2,099	2,217	2,559	2,169	2,169	2,615	2,083	2,310	2,467	2,283
... = not available											

Source: Bangko Sentral ng Pilipinas, National Statistics Office, Asian Development Bank.

Table 2. Level of Philippine GDP, 2016Q2 – 2017Q2

	Nominal GDP		Real GDP	
	(million current pesos)		(million constant 2000 pesos)	
	2016Q2	2017Q2	2016Q2	2017Q2
Agriculture and Forestry	268,384	303,496	136,241	147,291
Fishing	42,822	44,705	27,383	26,580
Mining and Quarrying	27,753	34,854	26,597	30,228
Manufacturing	624,394	672,929	461,133	497,590
Construction	302,453	330,468	146,964	156,273
Electricity Gas and Water Supply	140,082	147,854	69,756	71,442
Transport Communication and Storage	247,379	261,695	164,419	170,209
Trade and Repair of Motor Vehicles Motorcycles Personal	650,338	712,592	334,929	355,907
Financial Intermediation	305,347	333,934	154,558	163,933
Real Estate Renting & Bus. Actvt	475,038	518,053	241,765	260,848
Public Administration & Defense: Compulsory Social Security	152,552	172,202	88,087	94,748
Other Services	380,961	411,510	231,359	243,035
<b>Sum = GDP</b>	<b>3,617,503</b>	<b>3,944,292</b>	<b>2,083,189</b>	<b>2,218,084</b>

Source: Philippine Statistics Authority.

Table 3. Industry Contributions to Philippine GDP Growth, 2016Q2 – 2017Q2

	TRAD	PGE	PCE	GEN
	GDP Growth			GDP Growth
	(percent)	(percent)	(percent)	(percent)
		(1)	(2)	(1)+(2)
<b>GDP Growth</b>	<b>6.48</b>	<b>6.43</b>	<b>0.05</b>	<b>6.48</b>
<b>Industry Growth Contribution</b>				
<b>Agriculture</b>	<b>0.49</b>	<b>0.57</b>	<b>0.23</b>	<b>0.80</b>
Agriculture and Forestry	0.53	0.60	0.17	0.77
Fishing	-0.04	-0.03	0.06	0.02
<b>Industry</b>	<b>2.45</b>	<b>2.09</b>	<b>-0.22</b>	<b>1.88</b>
Mining and Quarrying	0.17	0.10	-0.17	-0.06
Manufacturing	1.75	1.36	-0.62	0.75
Construction	0.45	0.53	0.54	1.07
Electricity Gas and Water Supply	0.08	0.09	0.03	0.12
<b>Services</b>	<b>3.53</b>	<b>3.77</b>	<b>1.52</b>	<b>5.28</b>
Transport Communication and Storage	0.28	0.24	0.15	0.39
Trade and Repair of Motor Vehicles Motorcycles Personal	1.01	1.13	0.53	1.65
Financial Intermediation	0.45	0.51	0.06	0.57
Real Estate Renting & Bus. Actvt	0.92	1.04	0.19	1.22
Public Administration & Defense: Compulsory Social Security	0.32	0.32	0.09	0.40
Other Services	0.56	0.53	0.51	1.05

Source: DLSU-AKI Philippine Economic Monitor calculations by applying the data in Table 2 to a "generalized" (GEN) exactly additive decomposition of GDP growth into pure growth effect (PGE) and price change effect (PCE) as an alternative to the "traditional" (TRAD) GDP growth decomposition. The GEN formulas for PGE and PCE and the TRAD formula are given, respectively, by equations (12), (13), and (17) in Dumagan, Jesus C. (2016), "Effects of Relative Prices on Contributions to the Level and Growth of Real GDP," Working Paper Series No. 2016-036, Angelo King Institute for Economic and Business Studies, De La Salle University, Manila. Analytically, PGE is the result of real GDP or "quantity" growth holding real price constant and PCE is the result of relative price or "real price" growth holding quantity constant. This alternative framework follows from the decomposition of "aggregate labor productivity" (ALP) growth in Dumagan, Jesus C. (2013), "A Generalized Exactly Additive Decomposition of Aggregate Labor Productivity Growth," Review of Income and Wealth, 59 (Issue 1): 157-168, where ALP is the ratio of GDP to total labor employment. Thus, by removing the labor variable, the decomposition of ALP growth in the latter paper yields the decomposition of GDP growth into PGE and PCE which is implemented in this Table 3.