



Monitoring the Philippine Economy

Third Quarter Report for 2017

Project of Angelo King Institute

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Third quarter economic performance: GDP growth exceeds expectations but lower than previous year.

Philippine economy experiences slower growth. Third quarter growth in 2017 declined to 6.9 percent from 7.1 percent the previous year. Viewed from the demand side, overall growth slowed due to growth deceleration in private consumption and gross fixed capital formation although there was a significant growth acceleration in government consumption. Trade deficit narrowed due to faster growth in exports compared to imports. On the supply side, all sectors were able to register positive growth rates. However, only the service sector exceeded last year's growth. Industry and agriculture sector experienced slight slowdown in growth compared to the previous year.

- **Major components of aggregate demand**
 - **Household spending remains stagnant.** Overall private consumption in the third quarter grew slower at 4.5 percent year-on-year (y-o-y) compared to its 7.2 percent growth the previous year. The Philippine Statistics Authority (PSA)² reported growth increases in some components of Household Final Consumption Expenditure such as furnishings, household equipment and routine household maintenance (1.1 percent to 10.7 percent y-o-y), communication (1.0 percent to 6.3 percent y-o-y), and clothing and footwear (-4.5 percent to -0.4 percent y-o-y). However, these were counterbalanced by growth declines in alcoholic beverages and tobacco (6.9 percent to -7.7 percent y-o-y), transport (12.7 percent to 0.7 percent y-o-y), and food and non-alcoholic beverages (8.4 percent to 3.4 percent y-o-y).
 - **Slowing domestic investment growth relative to previous year.** Gross fixed capital formation growth slowed to 6.6 percent from the 21.7 percent growth the previous year. According to PSA³, investments in Intellectual Property Products maintained its growth at 29.2 percent from a 28.7 percent growth the previous year. Durable equipment, breeding stock & orchard development, and construction exhibited a y-o-y growth of 8.3 percent, 3.5 percent, and 2.8 percent, respectively.

¹ Report is based on latest available data as of December 1, 2017. For comments and questions, please email mitzie.conchada@dlsu.edu.ph

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

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

- **Rising government expenditures over last year.** Government consumption increased to 8.3 percent from 3.1 percent the previous year. PSA stated that the acceleration was a result of disbursements for social protection programs, speedier filling-in of government positions, and execution of the salary adjustment based on Executive Order No. 201, series of 2016, which increases the base pay of civilian, military, and uniformed personnel.⁴
- **Trade deficit narrows down.** At the end of September, the Philippines recorded a smaller trade deficit of 1.91 billion USD than the 2.02 billion USD deficit the previous year. Exports and imports were recorded at 5.6 billion USD (4.3 percent growth y-o-y) and 7.5 billion USD (1.7 percent growth y-o-y), respectively. Major contributors in the expansion of export sales were gold (171.3 percent y-o-y), coconut oil (63.8 percent y-o-y), and machinery and transport equipment (34.9 percent growth y-o-y). On the other hand, growth in imports were caused by mineral fuels, lubricants and related materials (40.4 percent y-o-y), iron and steel (25.8 percent y-o-y), and telecommunication equipment and electrical machinery (7.8 percent y-o-y).⁵
- **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).⁶

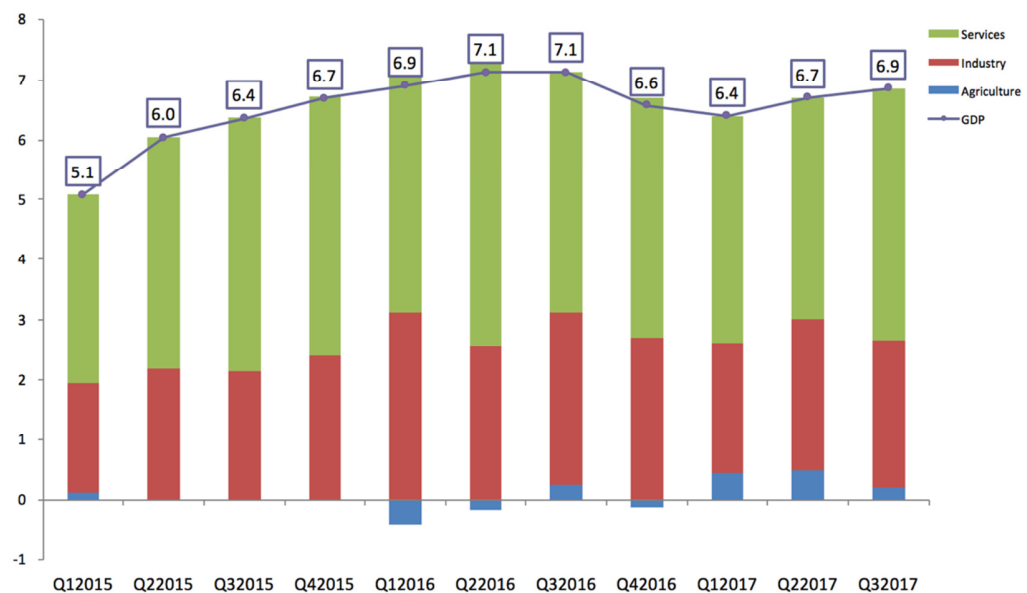
⁴ <http://psa.gov.ph/nap-press-release/sector/Government%20Final%20Consumption>

⁵ <https://psa.gov.ph/content/highlights-philippine-export-and-import-statistics-september-2017>

⁶ 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.

- Services sector remains the highest contributor to supply-side growth.** Services sector registered highest contribution to growth, with 4.38 percentage points from positive quantity and real price growth (see Table 3). The sector grew 7.1 percent, which was higher than the 6.8 percent growth the previous year. Its share of GDP remains robust at 58.8 percent from last year's 58.7 percent. Top contributors in the service sector for Q3 2017 remained the same as in 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 31.3 percent, 21.1 percent, and 17.1 percent, respectively.
- Manufacturing continues to drive industry sector growth.** The industry sector grew by 7.5 percent, lower than the 8.8 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 67.4 percent share in the sector while construction is the largest contributor in the group with 1.13 percentage points to total GDP growth (Table 3).
- Agriculture sector growth remains low.** In Q3 2017, the agriculture sector realized a low but positive growth of 2.5 percent, slightly lower than the registered sector growth of 3.0 percent the previous year. Furthermore, the share of the sector contracted to 7.8 percent from last year's 8.2 percent. Agriculture sector contributed a low 0.37 percentage points to GDP growth 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**⁷. The peso depreciated by 1.93 percent to average ₱50.84/US\$1, on a quarter-on-quarter basis, from the previous average of ₱49.86/US\$1. Furthermore, on a year-on-year basis, the peso depreciated by 7.44 percent, from the previous year's ₱47.06/US\$1 average. Peso depreciation or dollar appreciation was partially caused by aggressive remarks from various US Federal Reserve officials that strengthened the case for another interest rate hike before the year ends, and the increasing optimism towards US President Trump's tax reform program.
- **Unfavorable economic factors may threaten the economy**⁸. Depreciation of the peso, possibility of further monetary tightening by the US Federal Reserve, and geopolitical tensions on the international front remain as challenges the Philippine economy has to face.
- **Weather disturbances serve as an adversity to the economy**. Unexpected inclement weather conditions, natural disasters, and the like disturb agricultural activities in the country. These harsh conditions may worsen poverty level, unemployment rate, and threaten food security, especially for the poor Filipinos. Infrastructure improvements are deemed vital to augment agriculture sector's resiliency.

Other economic news

- **Stock market reports increase PSEi**⁹. For the third quarter, PSEi recorded an increase quarter-on-quarter of 3.2 percent to average 8,015.7 index points. This growth of the benchmark index in some way reflects the country's ability to withstand internal conflicts and external volatilities, the economy's rosy growth prospects, and optimism with the passage of the government's first tax reform package before end of 2017.
- **Inflation level remains within target range**¹⁰. With the consumer price index growing at an average of 3.1 percent in 3Q 2017, BSP reports that this growth is within the national government's foreseen target range of 3.0 percent \pm 1.0 percentage point (Figure 3). Food inflation decreased as prices of major items eased. On the other hand, non-food inflation increased due to upticks in domestic fuel prices.

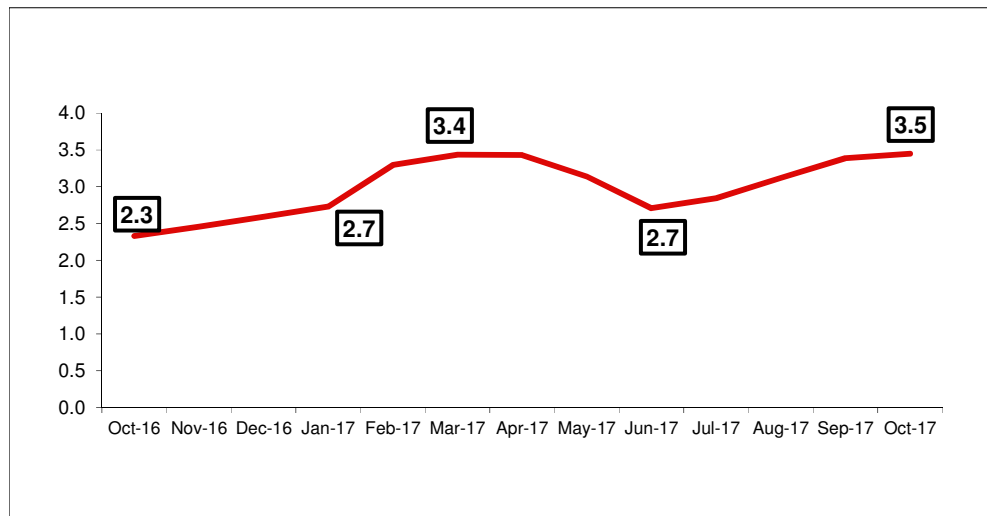
⁷ http://www.bsp.gov.ph/downloads/Publications/2017/IR3qtr_2017.pdf

⁸ http://www.bsp.gov.ph/downloads/Publications/2017/IR3qtr_2017.pdf

⁹ http://www.bsp.gov.ph/downloads/Publications/2017/IR3qtr_2017.pdf

¹⁰ http://www.bsp.gov.ph/downloads/Publications/2017/IR3qtr_2017.pdf

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



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

- Consumer sentiment declines¹¹.** Consumer confidence diminished but remained positive for Q3 2017. Consumer confidence index (CI) decreased to 10.2 percent from 13.1 percent the previous quarter. The weakening in CI was caused by (a) anticipated higher prices of commodities which would lead to increased household expenditures, (b) peace and order problems, especially the ongoing crisis in Marawi City, (c) low or no increase in income, and (d) expected increase in unemployment. However, upbeat CI is expected for the next quarter due to positive expectations such as additional income and salary increase, improvement in peace and order, and increased job opportunities. In addition, the percentage of households with savings increased to 36.8 percent from 35.8 percent the previous quarter.
- 31st ASEAN Summit in the Philippines¹².** Last November 12-14, 2017, world leaders gathered to attend the 31st ASEAN Summit, with the theme “Partnering for Change, Engaging the World.” This event was hosted by the Philippines, wherein related summits were held in the Philippine International Convention Center (PICC), Manila. At the main meeting, leaders of the ten ASEAN countries discussed and gave guidance to the various ASEAN sectoral bodies on the way forward in building a region of peace and progress for the mutual benefit of ASEAN citizens. The Philippines, as the host and chair of ASEAN, was able to push for its own initiatives and play a vital role in finalizing the ASEAN Consensus on the Protection and Promotion of the Rights of Migrant Workers. Moreover, it showed leadership in various aspects of regional cooperation, increased connectivity,

¹¹ <http://www.bsp.gov.ph/publications/media.asp?id=4462>

¹² <https://www.dfa.gov.ph/newsroom/dfa-releasesupdate/14628-significance-of-the-philippines-hosting-of-the-31st-asean-summit-and-related-summits>

enhanced trade, while boosting local tourism and talents. Some of the significant accomplishments by the ASEAN leaders at the summit include: (1) Signing the ASEAN Consensus on the Protection and Promotion of the Rights of Migrant Workers—ten years after the ASEAN leaders signed the Cebu Declaration on the Protection and Promotion of the Rights of Migrant Workers in January 2007—to solidify social protection and access to justice and health services of the region's migrant workers, and ensure fair treatment. (2) Discussing ways to combat peace and order issues prevailing in the region. (3) Meeting US President Donald Trump, Chinese Premier Li Keqiang, UN Secretary-General Antonio Guterres, and the leaders of five other dialogue partners of ASEAN. An agreement between ASEAN member-countries and China on the drafting of a South China Sea code was also signed.

Table 1. Philippine Economic Indicators

Monthly Leading Indicators	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17
Industrial Production (y-o-y, %)	15.1	21.8	14.9	9.8	12.3	3.0	5.3	2.9	-3.5	1.6	-3.7	...
Consumer Price Index (y-o-y, %)	2.5	2.6	2.7	3.3	3.4	3.4	3.1	2.7	2.8	3.1	3.4	3.5
Retail Sales (y-o-y, %)	15.6	21.8	20.7	18.6	19.7	0.6	3.2	-0.9	-6.8	-4.9
Exports (y-o-y, %)	-7.5	6.3	22.0	8.7	18.1	19.1	14.0	5.8	10.4	11.0	7.4	...
Imports (y-o-y, %)	19.7	13.8	12.2	15.2	18.0	-0.1	16.6	-1.3	-3.2	14.2	5.8	...
Trade Balance, US\$ million	-2,566	-2,158	-2,469	-1,768	-2,297	-1,754	-2,737	-1,992	-1,646	-2,393	-1,915	...
Total Reserves (less gold), US\$ billion	74	73	74	74	73	74	74	73	73	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	3.0
Fiscal Balance (million pesos)	-19,145	-118,229	2,222	-23,724	-61,471	52,797	-33,421	-90,873	-50,512	28,808	-36,892	...
Quarterly/Annual Economic Indicators	2014	1Q2015	2Q2015	3Q2015	4Q2015	1Q2016	2Q2016	3Q2016	4Q2016	1Q2017	2Q2017	3Q2017
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	6.7	6.9
- Private Consumption	5.4	6.0	6.4	6.2	6.6	7.1	7.5	7.2	6.2	5.8	5.9	4.5
- Government Consumption	1.7	0.0	2.2	15.5	15.5	11.8	13.5	3.1	4.5	0.1	7.1	6.6
- Gross Capital Fixed Formation	5.4	15.7	28.6	15.3	16.2	31.5	30.3	21.7	14.7	10.6	8.5	6.6
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	...
Others	Oct-16	Nov-16	Dec-16	Jan-17	Feb-17	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17
Overseas Filipinos' Remittances (US\$, million)	2,099	2,217	2,559	2,169	2,169	2,615	2,083	2,310	2,467	2,283	2,499	2,186
... = not available												

Source: Bangko Sentral ng Pilipinas, Philippine Statistics Authority, Asian Development Bank.

Table 2. Level of Philippine GDP, 2016Q3 – 2017Q3

	Nominal GDP		Real GDP	
	(million current pesos)		(million constant 2000 pesos)	
	2016Q3	2017Q3	2016Q3	2017Q3
Agriculture and Forestry	275,300	293,697	130,055	134,824
Fishing	51,423	53,026	30,182	29,389
Mining and Quarrying	29,778	35,825	16,120	16,868
Manufacturing	617,912	671,631	427,977	468,185
Construction	253,158	269,507	126,560	131,355
Electricity Gas and Water Supply	101,241	107,794	76,246	78,792
Transport Communication and Storage	209,255	221,294	134,551	139,820
Trade and Repair of Motor Vehicles Motorcycles Personal	708,149	774,496	359,656	384,069
Financial Intermediation	281,349	315,047	141,816	153,995
Real Estate Renting & Bus. Actvt	490,274	540,713	240,150	258,678
Public Administration & Defense: Compulsory Social Security	133,941	152,050	75,731	81,979
Other Services	334,160	368,026	195,437	210,476
Sum = GDP	3,485,941	3,803,106	1,954,481	2,088,429
Source: Philippine Statistics Authority.				

Table 3. Industry Contributions to Philippine GDP Growth, 2016Q3 – 2017Q3

	TRAD	PGE	PCE	GEN
	GDP Growth			GDP Growth
	(percent)	(percent)	(percent)	(percent)
		(1)	(2)	(1)+(2)
GDP Growth	6.85	6.77	0.08	6.85
Industry Growth Contribution				
Agriculture	0.20	0.25	0.12	0.37
Agriculture and Forestry	0.24	0.29	0.06	0.35
Fishing	-0.04	-0.04	0.05	0.01
Industry	2.47	2.08	0.11	2.19
Mining and Quarrying	0.04	0.04	0.10	0.14
Manufacturing	2.06	1.67	-0.85	0.81
Construction	0.25	0.28	0.86	1.13
Electricity Gas and Water Supply	0.13	0.10	0.01	0.11
Services	4.18	4.45	-0.06	4.38
Transport Communication and Storage	0.27	0.24	-0.01	0.23
Trade and Repair of Motor Vehicles Motorcycles Personal	1.25	1.38	0.02	1.40
Financial Intermediation	0.62	0.69	-0.02	0.67
Real Estate Renting & Bus. Actvt	0.95	1.09	0.22	1.30
Public Administration & Defense: Compulsory Social Security	0.32	0.32	-0.17	0.15
Other Services	0.77	0.74	-0.11	0.63

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.