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Monitoring the Philippine Economy First Quarter Report for 2015

Project of Angelo King Institute

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The Philippine economy's curtailed growth of 5.2 percent in the first quarter prompts government to speed up public spending.

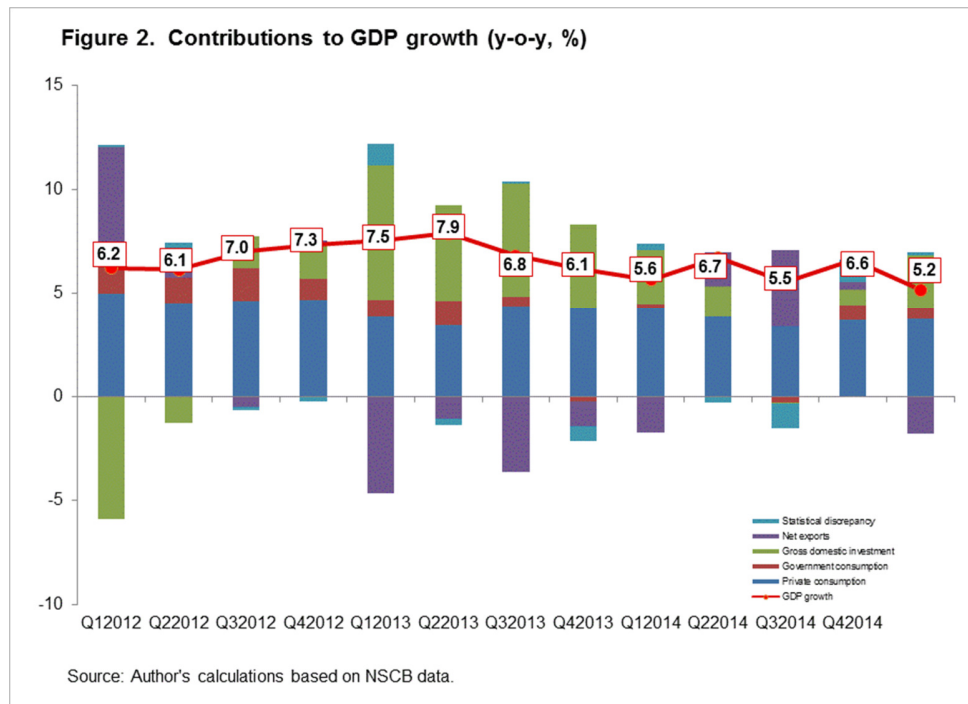
Economic performance: slower growth rate seen in the first quarter due to lower household spending and weaker exports.

- **Domestic economy's growth slows down Q1 2015.** Growth of the domestic economy was recorded at 5.2 percent from 5.6 percent the previous year. This was the lowest growth since the fourth quarter of 2011. Sluggish government spending coupled with weaker exports led to the slower growth of the economy.
- **Major components of aggregate demand**
 - **Household spending loses pace.** Private consumption in the fourth quarter decelerated to 5.4 percent year-on-year (y-o-y) from 6.1 percent the previous year. According to the National Statistical Coordination Board (NSCB), the slowdown in consumption was due to the decline of consumption of clothing and footwear (negative 11 percent y-o-y). On the other hand, consumption of alcoholic beverages and tobacco (26.8 percent) and transport (16.4 percent) had the highest growth.
 - **Domestic investment improves with a double-digit growth.** Capital formation jumped to 11.8 percent y-o-y from the previous quarter's 2.9 percent y-o-y growth. This was slightly lower though than last year's 12.8 percent y-o-y growth. The positive growth in capital formation was due to higher investments in durable equipment and intellectual property products. The NSCB reported that durable equipment increased 14.3 percent from 4.0 percent last year. Increase in investments were noted as follows: Water transport, recovered to 86.2 percent from negative 41.8 percent; Agricultural machineries, 62.1 percent from 3.3 percent; Mining and construction machineries, 53.1 percent from negative 25.2

¹ Report is based on latest available data as of June 15, 2015. For comments and questions, please email mitzie.conchada@dlsu.edu.ph

percent; Tractor other than steam, 48.4 percent from negative 21.4 percent; and Textile machineries, 32.9 percent from 99.6 percent.

- Government expenditure continues to increase in the fourth quarter.** Government expenditure rose to 4.8 percent from last year's 1.9 percent. Public spending on major government expenditures for personnel services and maintenance and other operating expenses increased due to high cash disbursement for major government expenditures for salaries and wages and other expenses.



- Philippine exports and imports weaken.** Growth of net exports slowed down to 78.7 percent y-o-y compared to last year's 244.2 percent y-o-y growth in the first quarter. Exports of goods and services grew by only 1.0 percent compared to 12.7 percent the previous year. Export of bananas, copra oil, sugar, electronic data processing, control instrumentation, and automotive electronics pulled down total export's growth. Total exports for the first quarter was recorded at Php815 billion. On the other hand, imports grew by only 4.6 percent compared to 16.3 percent last year. Imports of transport equipment and dairy products posted negative growth rates (negative 31 percent and negative 34.7 percent respectively). Total imports was Php884 billion bringing net exports to a negative Php69 billion.

- **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 also 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 this ratio makes “real price” synonymous with “relative price” or exchange value between the GDP of any two sectors where real price measures the value of a sector’s output in “GDP units” since real GDP is the numeraire. 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 2).²

- **Services sector remains as the main driver of supply-side growth.** The services sector itself posted a real growth rate of 5.6 percent, though lower than the previous year’s 6.8 percent, mostly due to the expansion of transport, storage and communication sub-sector (14.1 percent growth). Real estate, renting and business activity sub-sector also posted a positive growth with 6.4 percent. To the overall GDP growth of 5.2 percent in the first quarter, the services sector had the highest contribution of 4.10 percentage points of which 3.14 is due to quantity growth alone and the remaining 0.96 percentage point is due to an increase in the real price of services from an average of 1.01 GDP units in 2014Q1 to 1.02 in 2015Q1 combined with quantity-price growth interaction (based on the above GEN decomposition of GDP growth in Table 2).
- In contrast, without accounting for the growth effects of the above increase in real prices of services, the TRAD decomposition shows that the services sector contributed a smaller 3.13 percentage points to GDP growth compared to 4.10

² The results in Table 2 are DLSU-AKI 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), growth-price interaction effect (GPIE), and relative price effect (RPE) as an alternative to the “traditional” (TRAD) GDP growth decomposition. Analytically, PGE is the result of “quantity” growth holding real price constant; RPE is the result of “real price” growth holding quantity constant; and GPIE results from quantity-price growth interaction. The GEN formulas for PGE, GPIE, RPE, and the TRAD formula are given, respectively, by equations (15), (16), (17), and (23) in Dumagan, Jesus C. (2014), “An Alternative Framework for Sectoral Contributions to GDP Level and Growth: Application to the Philippines,” Working Paper Series 2014-009, 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 in the former paper which is implemented in Table 2.

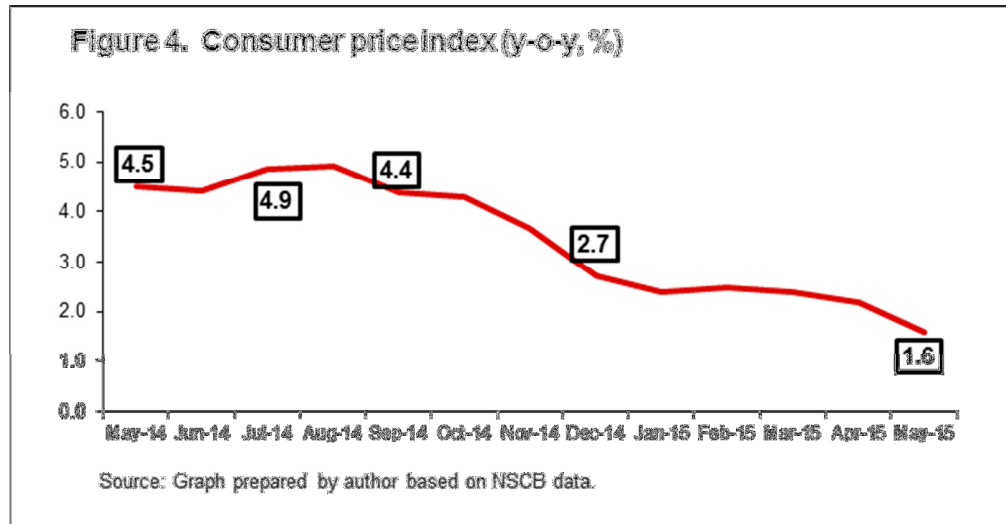
percentage points contribution from the GEN decomposition of GDP growth (Table 2). Thus, TRAD underestimates the growth contribution by ignoring the increase in real price.

- **Manufacturing leads the industry sector, displays solid performance.** By itself, industry grew 5.5 percent y-o-y in the first quarter with manufacturing making the largest contribution to industry growth. Within manufacturing, the top performers (based on individual growth) were basic metal industry (93.9 percent), publishing and printing (59.7 percent), and tobacco manufacturers (53.9 percent). The industry sector contributed 1.22 percentage points to GDP growth. This is lower than the 1.74 percentage points contributed by quantity growth alone after accounting for the effects of a decrease in the real price of industry sector output, from an average 0.95 GDP units in 2014Q1 to 0.94 in 2015Q1, together with quantity-price interaction effect.
- Without accounting for the growth effects of the above decrease in real prices of industry output, the TRAD decomposition shows that the industry sector contributed a larger 1.85 percentage points to GDP growth compared to 1.22 percentage points contribution from the GEN decomposition (Table 2). In this case, TRAD appears to overestimate the growth contribution by ignoring the decrease in real price.
- **Contribution of agriculture sector declines in first quarter.** The agriculture sector itself grew 1.6 percent y-o-y with agriculture and forestry growing 2.5 percent and fishing shrinking 2.6 percent. Compared to the services and industry sector, the agriculture sector had a negative 0.17 percentage point contribution to GDP growth. Quantity growth alone in the sector contributed 0.21 percentage points except that agriculture sector real prices fell resulting in the above negative contribution together with quantity-price interaction. On average, real prices in agriculture fell from 1.12 GDP units in 2014Q1 to 1.09 in 2015Q1.
- Similar to the case of the industry sector, agriculture real price also decreased. By ignoring this price decrease, the TRAD decomposition shows that the agriculture sector contributed a positive 0.17 percentage point to GDP growth compared to the exact opposite of a negative 0.17 percentage point contribution from the GEN decomposition (Table 2). Similarly, TRAD overestimates the growth contribution by ignoring the decrease in real price.

Other economic news

- **First quarter unemployment rate drops.** The recent Labor Force Survey (LFS) conducted in April revealed a drop in unemployment rate compared to the previous year. Unemployment rate was recorded at 6.4 percent, compared to last year's 7.5 percent. NCR has the highest unemployment rate in the Philippines at 9.3 percent. Most of the unemployed were males, belonged to the age group 15 to 24 years old, and had high school as their highest educational attainment. In addition,

employment for males is more frictional, wherein for all number of weeks of looking for work, males have a bigger distribution.



- **Inflation continues to move at a slower pace.** The month of May ended with a lower 1.6 percent inflation rate, compared to 4.5 percent last year. This was attributed to annual declines in prices of utilities, gas and other fuels, communication, food and non-alcoholic beverages, and alcoholic beverages and tobacco. Inflation in the NCR region was recorded at 0.7 percent while a 1.8 inflation rate was recorded in other areas outside NCR. Forecast for average inflation for this year is seen at 2.3 percent amid expected weakness of peso, uncertainty in oil prices and El Niño droughts.
- **Outlook on “Hot Money” inflow remains to be positive given strong stock market performance.** The bullish performance of the Philippine Stock market continues as it reached new time highs as the Philippine Stock Exchange index (PSEi) finished strong at 7,456.16 by June 13, 2015. The stock market has grown 3.12 percent since the start of the year. Overall the Philippine Stock market has experienced a relatively strong performance for the first quarter.
- **Bangko Sentral ng Pilipinas keeps key policy rates.** The Bangko Sentral ng Pilipinas (BSP) in its latest Monetary Policy Decision in March 26 decided to maintain key policy rates at 4.00 percent for the overnight borrowing or reserve repurchase facility due to the manageable inflation environment. BSP may decide in its next meeting in June to reduce key policy rate after inflation eased to 1.6 percent.



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Philippines Economic Data													
Monthly Leading Indicators	May-14	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15	Apr-15	May-15
Industrial Production (y-o-y, %)	12.7	12.6	7.6	5.7	4.8	8.7	9.1	6.4	4.4	-0.8	13.6
Consumer Price Index (y-o-y, %)	4.5	4.4	4.9	4.9	4.4	4.3	3.7	2.7	2.4	2.5	2.4	2.2	1.6
Retail Sales (y-o-y, %)	9.2	11.9	4.0	2.8	2.3	6.7	2.2	-0.1	8.1
Exports (y-o-y, %)	15.6	21.6	11.6	10.4	15.6	2.4	19.7	-3.2	0.0	-3.0	2.1
Imports (y-o-y, %)	-3.9	-1.2	1.3	5.1	1.1	15.4	-2.2	-10.6	-13.1	10.2	-6.8
Trade Balance, US\$ million	863	633	-139	-374	63	-441	-295	-67	-862	-838	264
Total Reserves (less gold), US\$ billion	72.45	72.45	72.63	72.82	71.99	72.10	71.45	72.06	72.67	73.20	73.02	73.45	...
Policy Rate	3.5	3.5	3.75	3.75	4	4	4	4	4	4	4
Fiscal Balance (million pesos)	11,782	-62,486	-1,762	29,865	-5,198	-2,530	6,824	-46,317
Quarterly/Annual Economic Indicators	2009	2010	2011	2012	1Q2013	2Q2013	3Q2013	4Q2013	1Q2014	2Q2014	3Q2014	4Q2014	1Q2015
Real GDP (y-o-y, %)	1.1	7.6	3.6	6.8	7.5	7.9	6.8	6.1	5.6	6.7	5.5	6.6	5.2
- Private Consumption	2.3	3.4	5.7	6.6	6.7	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
- Government Consumption	10.9	4.0	2.1	12.2	15.9	13.6	14.5	14.2	14.5	14.2	14.3	14.3	14.3
- Gross Capital Fixed Formation	-8.7	31.6	2.0	-3.2	-4.7	0.7	2.8	1.6	0.1	1.3	1.5	1.1	1.0
Current Account (% of GDP)	5.6	4.5	2.3	2.8	5	3.8	5	5	2.3	4.4	4.8	5.9	...
Financial Account (US\$ million)	-1731	7290	-5610	-6748	-655	835	1183	1585	4098	696	810	4480	...
- Net Direct Investments, US\$ million	1604	682	-1277	958	-1336	502	-589	168	-487	-543	842	977	...
- Net Portfolio Investments, US\$ million	-625	4365	-4390	-3205	-1697	-255	217	948	2811	-649	-903	1202	...
Overall BOP position (US\$, million)	6421	14308	11400	9236	1536	1041	1247	1260	-4475	330	712	574	...
Unemployment rate	7.7	7.3	7.4	7	7.1	7.5	7.3	6.5	7.5	7	6.7	6	6.4
Others	Mar-14	Apr-14	May-14	Jun-14	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15
Overseas Filipinos' Remittances (US\$, million)	1,888	1,918	1,984	2,054	2,068	2,057	2,110	2,228	2,122	2,317	1,814	1,876	2,101
... = not available													

Source: Bangko Sentral ng Pilipinas, National Statistics Office, *International Financial Statistics*, IMF, Asian Development Bank.

Table 1. Level of Philippine GDP, 2014Q1 - 2015Q1

	Nominal GDP		Real GDP	
	(million current pesos)		(million constant 2000 pesos)	
	2014Q1	2015Q1	2014Q1	2015Q1
Agriculture and Forestry	296,174	294,696	149,309	152,985
Fishing	47,956	45,538	29,833	29,066
Mining and Quarrying	33,150	28,532	20,117	21,554
Manufacturing	603,518	632,071	400,802	424,355
Construction	182,801	193,518	90,397	94,432
Electricity Gas and Water Supply	97,545	100,970	51,771	53,918
Transport Communication and Storage	186,112	205,815	129,949	141,104
Trade and Repair of Motor Vehicles Motorcycles Personal	468,343	496,922	254,757	268,528
Financial Intermediation	237,413	253,697	125,519	130,957
Real Estate Renting & Bus. Actvt	353,408	389,470	182,376	194,096
Public Administration & Defense: Compulsory Social Security	101,670	101,506	68,556	68,706
Other Services	271,391	294,260	178,120	188,487
Sum = GDP	2,879,481	3,036,995	1,681,506	1,768,188

Source: Philippine Statistical Authority.

Table 2. Industry Contributions to Philippine GDP Growth, 2014Q1 - 2015Q1

	TRAD	PGE	GPIE	RPE	GEN
	GDP Growth				GDP Growth
	(percent)	(percent)	(percent)	(percent)	(percent)
		(1)	(2)	(3)	(1)+(2)+(3)
GDP Growth	5.16	5.08	0.02	0.05	5.16
Industry Growth Contribution					
Agriculture	0.17	0.21	-0.01	-0.37	-0.17
Agriculture and Forestry	0.22	0.25	-0.01	-0.33	-0.08
Fishing	-0.05	-0.04	0.00	-0.05	-0.09
Industry	1.85	1.74	-0.03	-0.48	1.22
Mining and Quarrying	0.09	0.08	-0.02	-0.23	-0.16
Manufacturing	1.40	1.23	-0.02	-0.29	0.93
Construction	0.24	0.28	0.00	0.07	0.35
Electricity Gas and Water Supply	0.13	0.14	0.00	-0.03	0.11
Services	3.13	3.14	0.06	0.91	4.10
Transport Communication and Storage	0.66	0.55	0.01	0.10	0.66
Trade and Repair of Motor Vehicles Motorcycles Personal	0.82	0.88	0.00	0.06	0.94
Financial Intermediation	0.32	0.36	0.01	0.17	0.54
Real Estate Renting & Bus. Actvt	0.70	0.79	0.03	0.40	1.21
Public Administration & Defense: Compulsory Social Security	0.01	0.01	0.00	-0.02	-0.02
Other Services	0.62	0.55	0.01	0.20	0.76

Source: DLSU-AKI *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), *growth-price interaction effect* (GPIE), and *relative price effect* (RPE) as an alternative to the "traditional" (TRAD) GDP growth decomposition. The GEN formulas for PGE, GPIE, RPE, and the TRAD formula are given, respectively, by equations (15), (16), (17), and (23) in Dumagan, Jesus C. (2014), "An Alternative Framework for Sectoral Contributions to GDP Level and Growth: Application to the Philippines," Working Paper Series 2014-009, Angelo King Institute for Economic and Business Studies, De La Salle University, Manila. Analytically, PGE is the result of "quantity" growth holding real price constant; RPE is the result of "real price" growth holding quantity constant; and GPIE results from quantity-price growth interaction. 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