Monitoring the Philippine Economy
Second Quarter Report for 2015

Project of Angelo King Institute

Mitzie Irene P. Conchada[1]
Assistant Professor
School of Economics

Edgardo Manuel Jopson
BS-MS Economics
School of Economics

The Philippine economy grows to a lower-than-forecast but modest 5.6 percent amidst regional slowdown.

Economic performance: slower economic growth experienced in the second quarter with a sluggish increase in consumption despite lower commodity prices and an increase in domestic investments.

- **Domestic economy recovers slowly in Q2 2015.** Growth of the domestic economy was recorded at 5.6 percent in the second quarter from 6.7 percent the previous year.   Though lower than forecasts and amidst regional slowdown, the economy posted a modest growth.   Government spending notably picked up due to higher public construction. The services sector had the highest contribution to the second quarter growth.

- **Major components of aggregate demand**

  - **Household spending slightly improves.** Private consumption in the second quarter registered a 6.2 percent year-on-year (y-o-y) growth, higher than last year's 5.7 percent growth. This is attributed to lower commodity prices which led to higher household spending. The National Statistical Coordination Board (NSCB) reported that the expenditure items posting higher growth were the following: miscellaneous goods and services at 10.5 percent, transportation at 9.5 percent, as well as recreation and culture at 9.0 percent. Food and non-alcoholic beverages (which account for 40.9 percent of total household spending) increased 5.6 percent this quarter.

  - **Domestic investment posts a high double-digit growth.**   Capital formation leaped to 17.4 percent y-o-y from last year's 8.3 percent growth due to higher investments in construction and durable equipment. Construction grew by 13.1 percent while durable equipment increased to 6.6 percent. Increase in investments was noted in machinery specialized for particular industries at 23.2 percent;

---

general industrial machinery and equipment at 7.4 percent and miscellaneous equipment at 2.5 percent. Notwithstanding the indicated growth of aggregate investments, declines were recorded for transport equipment at -6.8 percent and intellectual property products at -9.1 percent.

- **Government expenditure records accelerated growth.** Improvements in government expenditure were seen in the second quarter. Public expenditure increased to 3.9 percent compared to 0.02 percent last year. According to the NSCB, public spending on major government expenditures for personnel services and maintenance and other operating expenses increased due to sustained growth in these expenditures from the implementation of major government projects , specifically for social protection programs.

Figure 2. Contributions to GDP growth (y-o-y, %)

Source: Author's calculations based on NSCB data.
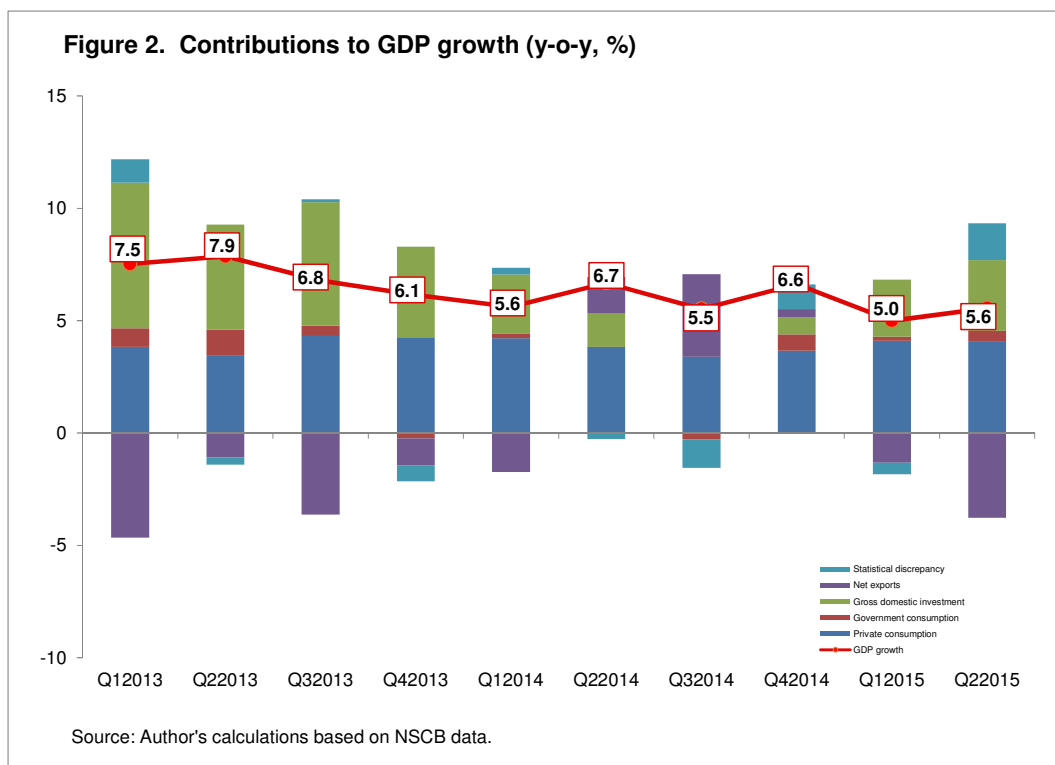
- **Philippine exports slowdown on sluggish global demand.** By the end of June, growth of exports declined 1.8 percent compared to 21.6 percent the previous year. Total exports amounted to only PhP 693 million in the second quarter. The decline in exports was affected by low global demand for agricultural products particularly bananas (-64 percent) and sugar (-71.9 percent), fishery products (-32.7 percent), and other commodities such as clothing, basketworks and copper. On the other hand, imports grew 22.9 percent in June, bringing overall growth for the second quarter to 9.5 percent. Imports rose higher compared to the previous year when its growth was only at 3.8 percent. The imports of goods that had the highest growth were electronics (53.6 percent), cereals (41.6 percent), and machinery and

mechanical appliances (24.9 percent). Net exports by the end of June reported a deficit of USD554 million.

- **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 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 2).[2]

- - **Services sector remains as the main driver of supply-side growth.** As usual, the services sector had the highest contribution to growth, with 4.72 percentage points from positive quantity and real price growth. The growth was driven by the real estate renting and business activities sector and the trade and repair of motor vehicles sector (with 1.24 percent for both).

- - **Construction leads the industry sector, displays strong performance.** The industry sector contributed 1.43 percentage points to GDP growth. This is lower than the 2.04 percentage points contributed by quantity growth alone after accounting for the effects of a decrease in the real price of industry sector output, from 1.03 last year to 0.98 in the second quarter together with quantity-price interaction effect. The laudable performance of the sector was attributed to the construction subsector, which grew 1.22 percent.

---

[2] The results in Table 2 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), 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.

- **Agriculture sector still experiences low growth.** Compared to the performance services and industry sector, the agriculture sector had a negative 0.59 percentage point contribution to GDP growth. Quantity growth alone contributed a negative 0.05 percentage points together with the fact 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 1.04 the previous year to 1.01 in the second quarter. The agriculture sector itself declined by 0.6 percent y-o-y with agriculture and forestry shrinking by 0.7 percent and fishing growing by 0.6 percent.

Challenges facing the economy

- **Weak global demand continues to affect Philippine exports.** The global economy finds it difficult to bounce back on the slowing down of global trade, sluggish momentum in industrial production in major economies, and downward price pressure on commodities including oil (National Economic Development Authority). China's transition from an export-based economy toward lower growth and more consumption driven has affected trends in the global economy. As of the end of the second quarter, Philippine trade balance was recorded at a deficit of USD 1.8 billion. The National Economic Development Authority reported that exports particularly for coconut products, fruits and vegetables, sugar products and other agro-based products declined.

- **El Nino continues to threaten Philippine agriculture.** Domestic shocks such as the prolonged El Nino continue to affect adversely Philippine agro-based products. The CNN Philippines reported that "dry farmlands, stunted growth of livestock, lower fishing output" are just some of the effects of the dry spell. Moreover, potential water shortage continues to prevail in the country. These events are endangering the production of basic commodities as well as the performance of various sectors such as the manufacturing sector, which can eventually put a toll on the country's gross domestic product. Safety nets for the looming negative effects of El Nino include an increase in food imports as well as an increase in overseas remittances.

Other economic news

- **Inflation plummets in August, lowest in years.** According to the National Economic and Development Authority (NEDA), sufficient supply of food and moderate price pressures in energy and oil rates have slowed the increase of commodity prices reaching its lowest rate in 20 years. Inflation rate was recorded at 0.6 percent in August, lower than last year's 4.1 percent. This was mainly due to the easing of prices of petroleum products, utilities, and transport sector. Inflation rate in the National Capital Region (NCR) was lower at 0.2 percent compared to the areas outside NCR with 0.8 percent. Inflation rate however is expected to rise by the end of the year due to the effect of El Nino on agro-based products.

Figure 4. Consumer price index (y-o-y, %)
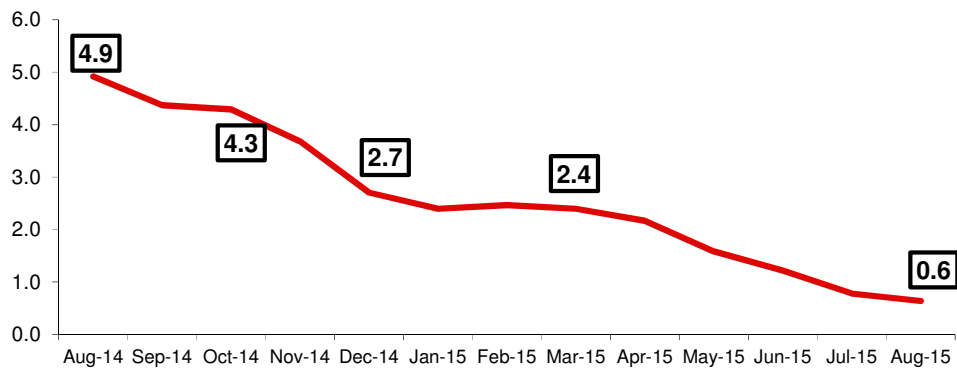
.Source: Graph prepared by author based on NSCB data

- **Market weakens on exposure to external shocks, signaling investors to sell stocks.** Amid the high market volatility from global investor concerns arising from the Greek Crisis, alongside China's economic slowdown , the PSEi decreased from the mid 8,000 mark in the first quarter to drop at a 7,106.79 index by the end of trading day on October 8, 2015. The Philippine stock market registered a 1.7 percent decline from the first trading day in January. Market volatility is expected to continue on slower-than-expected growth, the eventual US Federal rate hike, and the economic condition of China.

- **Domestic money supply expands in June.** The Bangko Sentral ng Pilipinas (BSP) declared that the growth of M3 has expanded to 9.3 percent in June. BSP Governor Amando Tentangco Jr. stated that money supply continued to expand due to sustained demand for credit; also stating that the continued expansion of liquidity will be sufficient to support economic growth for the following months.

Philippines Economic Data

Monthly Leading Indicators	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15	Apr-15	May-15	Jun-15	Jul-15	Aug-15
Industrial Production (y-o-y, %)	4.8	8.7	9.1	6.4	2.7	-2.0	14.8	1.8	-0.9	-1.6	-0.5	...
Consumer Price Index (y-o-y, %)	4.4	4.3	3.7	2.7	2.4	2.5	2.4	2.2	1.6	1.2	0.8	0.6
Retail Sales (y-o-y, %)	2.6	6.2	2.2	-2.6	-5.3	-6.5	3.3	-3.4	-7.6	...	...	...
Exports (y-o-y, %)	15.6	2.4	19.7	-3.2	0.0	-3.0	2.1	-4.1	-17.4	...	...	...
Imports (y-o-y, %)	1.1	15.4	-2.2	-10.6	-13.1	10.2	-6.8	-12.2	-13.4	...	...	...
Trade Balance, US$ million	63	-441	-295	-67	-862	-838	264	-337	508	...	...	...
Total Reserves (less gold), US$ billion	71.99	72.10	71.45	72.06	72.67	73.20	73.02	73.45	72.92	73.27	73.47	73.11
Policy Rate	4	4	4	4	4	4	4	4	4	4	4	4
Fiscal Balance (million pesos)	-5,198	-2,530	6,824	-46,317	13,424	-21,490	-18,131	26,258	-9,601	-7,691	-26,482	9,220

Quarterly/Annual Economic Indicators	2011	2012	1Q2013	2Q2013	3Q2013	4Q2013	1Q2014	2Q2014	3Q2014	4Q2014	1Q2015	2Q2015
Real GDP (y-o-y, %)	3.6	6.8	7.5	7.9	6.8	6.1	5.6	6.7	5.5	6.6	5.0	5.6
- Private Consumption	5.7	6.6	6.7	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
- Government Consumption	2.1	12.2	15.9	13.6	14.5	14.2	14.5	14.2	14.3	14.3	14.3	14.3
- Gross Capital Fixed Formation	2.0	-3.2	-4.7	0.7	2.8	1.6	0.1	1.3	1.5	1.1	1.0	1.2
Current Account (% of GDP)	2.3	0.7	5	3.8	5	5	2.3	4.4	4.8	5.9	4.8	...
Financial Account (US$ million)	-5,610	-4,821	-655	835	1,183	1,585	4,098	696	810	4,480	606	...
- Net Direct Investments, US$ million	-1,277	-898	-1,336	502	-589	168	-487	-543	842	977	395	...
- Net Portfolio Investments, US$ million	-4,390	-1,248	-1,697	-255	217	948	2,811	-649	-903	1,202	227	...
Overall BOP position (US$, million)	11,400	1,243	1,536	1,041	1,247	1,260	-4,475	330	712	574	877	...
Unemployment rate	7.4	6.975	7.1	7.5	7.3	6.5	7.5	7	6.7	6	6.4	6.5

Others	Jul-14	Aug-14	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15	Apr-15	May-15	Jun-15
Overseas Filipinos' Remittances (US$, million)	2,068	2,057	2,110	2,228	2,122	2,317	1,814	1,876	2,101	2,015	2,099	2,179

... = not available

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

Table 1. Level of Philippine GDP, 2014Q2 - 2015Q2				
	Nominal GDP		Real GDP	
	(million current pesos)		(million constant 2000 pesos)	
	2014Q2	**2015Q2**	**2014Q2**	**2015Q2**
Agriculture and Forestry	280,649	260,821	138,137	137,665
Fishing	44,847	45,099	28,910	28,468
Mining and Quarrying	37,105	29,775	27,935	28,601
Manufacturing	579,148	587,185	414,742	433,733
Construction	225,128	262,738	112,245	128,588
Electricity Gas and Water Supply	127,822	131,421	59,876	61,672
Transport Communication and Storage	211,841	228,540	144,074	152,640
Trade and Repair of Motor Vehicles Motorcycles Personal	544,100	581,435	287,956	305,416
Financial Intermediation	261,644	281,385	136,690	144,619
Real Estate Renting & Bus. Actvt	392,642	430,397	209,839	224,034
Public Administration & Defense: Compulsory Social Security	137,095	136,410	82,918	82,685
Other Services	299,835	331,307	188,872	205,841
Sum = GDP	**3,141,856**	**3,306,513**	**1,832,194**	**1,933,962**

Source: Philippine Statistical Authority.

Table 2. Industry Contributions to Philippine GDP Growth, 2014Q2 - 2015Q2					
	TRAD	PGE	GPIE	RPE	GEN
	GDP Growth				GDP Growth
	(percent)	(percent)	(percent)	(percent)	(percent)
		(1)	(2)	(3)	(1)+(2)+(3)
GDP Growth	**5.55**	**5.61**	**0.06**	**-0.12**	**5.55**
Industry Growth Contribution					
Agriculture	**-0.05**	**-0.05**	**0.00**	**-0.54**	**-0.59**
Agriculture and Forestry	-0.03	-0.03	0.00	-0.58	-0.61
Fishing	-0.02	-0.02	0.00	0.03	0.01
Industry	**2.06**	**2.04**	**-0.01**	**-0.60**	**1.43**
Mining and Quarrying	0.04	0.03	-0.01	-0.25	-0.23
Manufacturing	1.04	0.84	-0.02	-0.51	0.31
Construction	0.89	1.04	0.02	0.16	1.22
Electricity Gas and Water Supply	0.10	0.12	0.00	0.00	0.13
Services	**3.54**	**3.62**	**0.07**	**1.03**	**4.72**
Transport Communication and Storage	0.47	0.40	0.01	0.14	0.55
Trade and Repair of Motor Vehicles Motorcycles Personal	0.95	1.05	0.01	0.18	1.24
Financial Intermediation	0.43	0.48	0.01	0.16	0.66
Real Estate Renting & Bus. Actvt	0.77	0.85	0.03	0.37	1.24
Public Administration & Defense: Compulsory Social Security	-0.01	-0.01	0.00	0.00	-0.01
Other Services	0.93	0.86	0.01	0.16	1.03

Source: DLSU-AKI *Philippine Economic Monitor* calculations by applying the data in Table 1 to a "generalized" (GEN) exactly addtive 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