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Angelo King Institute
for Economic and Business Studies

Monitoring the Philippine Economy Third Quarter Report for 2015

Project of Angelo King Institute

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Third quarter growth, led mainly by the services sector, inches to 6.0 percent despite lackluster global market performance and sluggish exports.

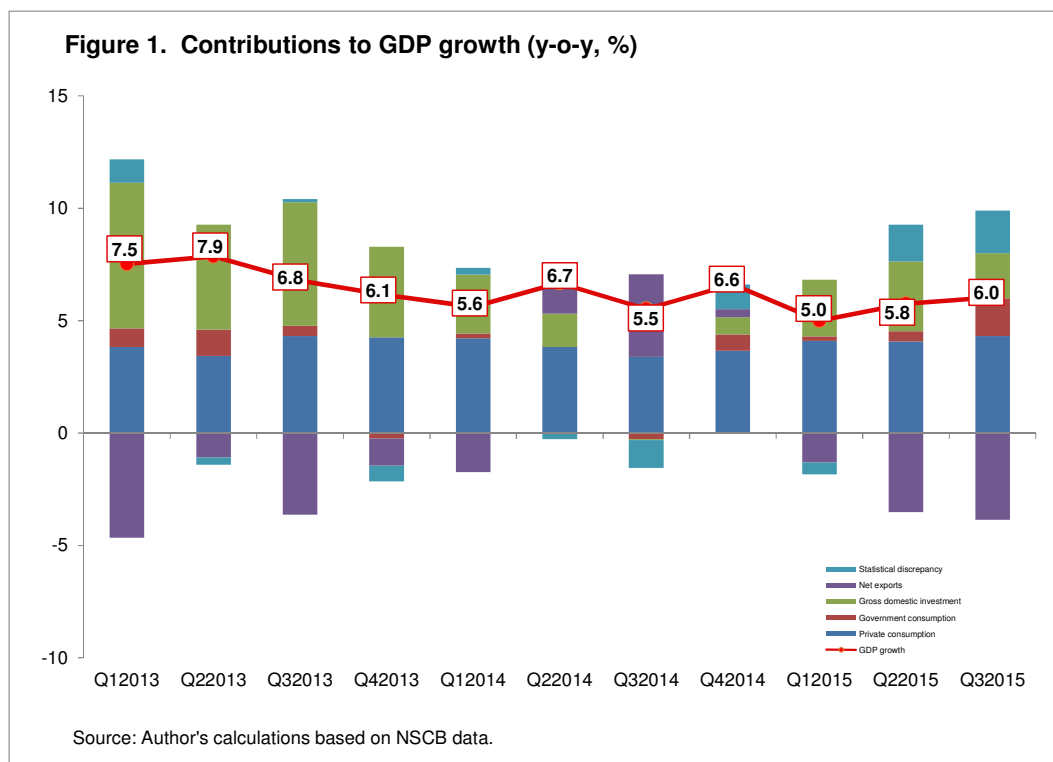
Economic performance: sustained economic growth in the third quarter amidst stable prices and increased government expenditure.

- **Domestic economy posts slightly higher growth in the third quarter.** The expansion of the domestic economy was recorded at 6.0 percent, higher than last year's 5.5 percent growth. Though the highest in the region, the economy may not reach its target of 7 percent growth by the end of the year. The slower than expected performance of the domestic economy was mainly due to weak exports despite the solid performance of government spending and investment.
- **Major components of aggregate demand**
 - **Lower prices boost household spending.** Private consumption in the second quarter registered a 6.3 percent year-on-year (y-o-y) growth, higher than last year's 4.9 percent growth. The continuous decline in commodity prices is seen as one of the main factors that led to higher household spending. The National Statistical Coordination Board (NSCB) reported that the expenditure items posting higher growth were restaurants and hotels at 13.9 percent, miscellaneous goods and services at 13.8 percent, and transport at 9.8 percent. Food and non-alcoholic beverages (which account for 41.3 percent of total household spending) increased 5.5 percent this quarter.
 - **Domestic investment displays modest growth.** Gross domestic capital formation grew 8.9 percent y-o-y, higher than last year's negative 0.2 percent. However, investments in capital formation and construction slowed to 9.3 percent and 5.3 percent respectively from 10.7 percent and 13.9 percent the previous year. This was attributed to lower investments in private construction (negative 0.4 percent growth) despite the strong performance of public construction. On the

¹ Report is based on latest available data as of November 30, 2015. For comments and questions, please email mitzie.conchada@dlsu.edu.ph

other hand, durable equipment displayed a notable growth of 12.1 percent compared to 7.7 percent the previous year. Investment in transport equipment particularly road vehicles exhibited the highest growth with 42 percent.

- Government expenditure mainly on projects continues to surge.** From a negative growth of 2.5 percent last year, government spending accelerated to an impressive 17.4 percent in the third quarter. The Philippine Statistics Authority (PSA) reported that this was due to higher disbursements for salaries and wages of government employees coupled with higher maintenance and other operating expenses.



- Philippine exports report biggest decline since 2011.** Weaker global demand lowered exports further by end of the third quarter. Exports of goods and services reached a 6.4 percent growth, much lower than last year's 12.1 percent growth. Total exports of goods amounted to PhP 838 million while total exports of services amounted to PhP 329 million. Lower global demand continued to depress exports of agricultural products particularly sugar (-89.2 percent) and bananas (-58.9 percent) as well as apparel and clothing (-37.9 percent). On the other hand, imports grew 13.4 percent in the third quarter, higher than last year's 4.7 percent. Imports of goods that reported the highest growth were telecommunication related electronics (85.7 percent), medical and pharmaceutical products (81.2 percent), and office equipment related electronics (75.3 percent). Net exports reported a deficit of USD 587 million in the third quarter.

- **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 the main driver of supply-side growth.** During the third quarter, the services sector contributed the highest to the 6.0 percent y-o-y GDP growth, with 5.71 percentage points. This contribution by the services sector was driven mainly by trade and repair of motor vehicles subsector (1.82 percentage points) and real estate renting and business activities subsector (1.57 percentage points).
- **Construction continues to lead the industry sector, though at a slower rate.** The industry sector contributed 1.43 percentage points to y-o-y GDP growth the previous quarter but only 0.49 percentage points this quarter. Quantity growth alone in the industry sector contributed 1.60 percentage points, but the decrease in the real price of industry output lowered this sector’s contribution to 0.49 percentage points. After accounting for the combined effects of positive quantity

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.

and real price growth in the construction subsector, this subsector contributed the most to industry growth this quarter.

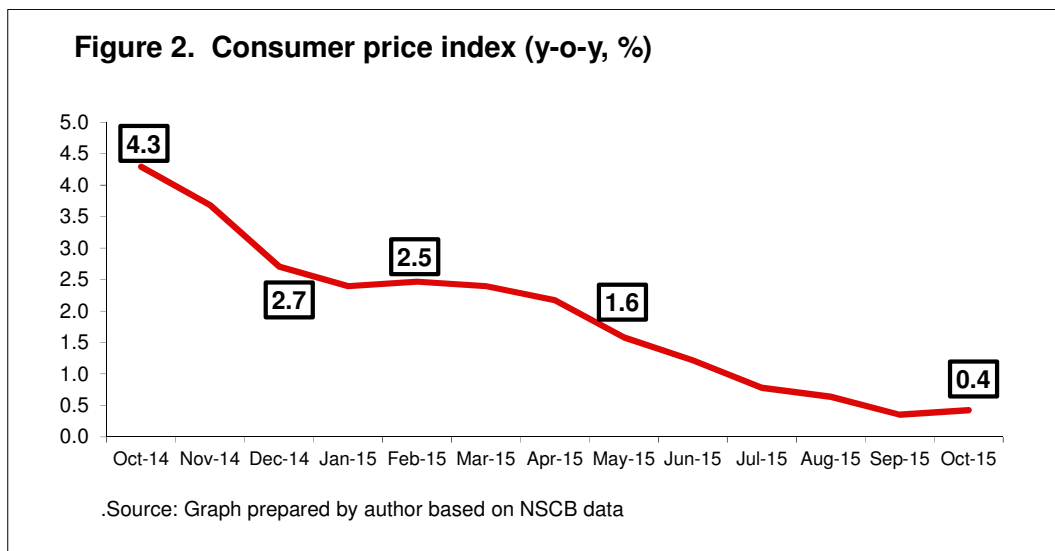
- **Slow growth still persists in the agriculture sector.** The third quarter's performance of the agriculture sector remained dismal. Agriculture sector quantity growth alone contributed 0.03 percentage points to y-o-y GDP growth but this sector's real prices fell resulting in a negative 0.15 percentage point contribution to GDP growth. Almost all of the positive quantity growth came from the fishing subsector while the fall in real prices came from the agriculture and forestry subsector that more than offset the above quantity growth.

Challenges facing the economy

- **Remittances unexpectedly slackened in the third quarter.** What used to prop up the domestic economy, cash remittances slowed down to an average of 1.4 percent y-o-y growth in the third quarter. Cumulative remittances by the end of the third quarter reached USD 18.4 billion. Cash remittances fell 0.6 percent in August, lower than the previous year's 6.14 percent growth, mainly on the depreciation of the peso. As of December 1, the peso depreciated 5.10 percent against the US dollar since January 2, 2015 (www.aric.adb.org). The depreciation of the peso prompted some to hold on longer to their dollars, expecting the dollar to appreciate more. Furthermore, remittances from the Middle East also slowed down due to the prolonged drop in oil prices. Despite these factors, the drop may only be seasonal and may start to pick up in the fourth quarter, meeting the projected 5 percent growth by end of the year.
- **Looming US FED rate hike and China's manufacturing recession pose risk to the domestic economy.** As exports from the domestic economy and region continue to struggle, higher interest rates might add to the region's challenges. The US Federal Reserve could increase its rates before the end of December, creating uncertainty in the global market. This could cause higher interest rates in the domestic economy which could dampen consumers' and investors' confidence. On the other hand, the slow pace of economic expansion in China continues to dampen prospects for Philippine exports. Latest statistics reveal that the Chinese manufacturing sector is experiencing a recession, falling to 49.6 percent in November from 49.8 percent the previous month.

Other economic news

- **Inflation steadies in October but is expected to pick up in November.** Prices of basic commodities bottomed out in October, displaying a record low growth of 0.4 percent, thus, improving the purchasing power of Filipinos. Low inflation was mainly due to the sharp drop in oil prices placing a downward pressure on transport and utility prices. November inflation, however, could pick up from expected higher food and energy prices.



- **Philippine stock market starts December on a high note.** The PSEi recorded an above 7,000 mark in the first trading day of December despite weak Chinese manufacturing sector. The domestic property sector led the market gain and ended the day with a 1.93 percent increase from the previous trading day. This may be short-lived though as the prospect of higher interest rate in the US could spur foreign outflows.
- **Domestic money supply sustains its growth in September.** The Bangko Sentral ng Pilipinas (BSP) declared that the growth of M3 has expanded to 8.5 percent in September. 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.
- **APEC advocates inclusive growth and the youth rises to the occasion.** According to the Philippine Star (2015), the Asia-Pacific Economic Cooperation (APEC) summit from Nov. 17 to 20 was attended by 9,000 participants, including 21 heads of state. Throughout the APEC events, inclusive growth was emphasized through a collaborative and multilateral

approach, focused particularly on the members of the grassroots level: the youth and the poor.

Through the Asian Development Bank (ADB) forums, the APEC Business Advisory Council (ABAC) dialogues, the Gawad Kalinga (GK) Enchanted Farm immersion, the SME and CEO Summits participation, and the APEC Economic Leaders' Meeting youth declaration, a select group of 100 youth representatives from 17 APEC economies embraced inclusive growth in their diverse advocacies. In particular, the Youth Declaration to the APEC Economic Leaders' Meeting underscored the importance of inclusive growth through "proactive [participation of the youth] in the creation of resilient, sustainable, and inclusive communities in the Asia-Pacific"; innovative entrepreneurship in the making and furthering of SMEs; collaborative partnership between the public and private sectors; quality education and developed human capital; and environmental sustainability and stewardship.

Through bilateral agreements among the economic leaders, Filipinos from all walks of life can expect greater education and health services, and more employment and business opportunities in the services, manufacturing, and technology sectors of society and the APEC region.



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Philippines Economic Data													
Monthly Leading Indicators	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15	Apr-15	May-15	Jun-15	Jul-15	Aug-15	Sep-15	Oct-15
Industrial Production (y-o-y, %)	8.7	9.1	6.4	2.7	-2.1	14.9	1.8	-1.1	-1.9	-0.2	2.0	3.6	...
Consumer Price Index (y-o-y, %)	4.3	3.7	2.7	2.4	2.5	2.4	2.2	1.6	1.2	0.8	0.6	0.4	0.4
Retail Sales (y-o-y, %)	6.2	2.2	-2.6	-5.3	-6.5	3.3	-3.4	-7.6
Exports (y-o-y, %)	2.4	19.7	-3.2	0.0	-3.0	2.1	-4.1	-17.4	-1.8	-1.8	-6.3	-15.5	...
Imports (y-o-y, %)	15.4	-2.2	-10.6	-13.1	10.2	-6.5	-12.2	-13.4	22.6	23.0	5.7	6.7	...
Trade Balance, US\$ million	-441.00	-295.00	-67.00	-862.00	-838.00	246.00	-337.00	507.00	-554.00	-1,519.00	-1,048.00	-1,231.00	...
Total Reserves (less gold), US\$ billion	72.10	71.45	72.06	72.67	73.20	73.02	73.45	72.92	73.27	73.47	73.10	73.54	73.92
Policy Rate	4	4	4	4	4	4	4	4	4	4	4	4	...
Fiscal Balance (million pesos)	-2,530	6,824	-46,317	-6,472	-9,673	-17,372	52,599	67,337	-72,673	-32,198	15,040	-22,140	...
Quarterly/Annual Economic Indicators	2011	2012	1Q2013	2Q2013	3Q2013	4Q2013	1Q2014	2Q2014	3Q2014	4Q2014	1Q2015	2Q2015	3Q2015
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	5.8	6.0
- Private Consumption	5.7	6.6	5.5	5.0	6.3	5.8	6.1	5.7	4.9	5.0	6.0	6.2	6.3
- Government Consumption	2.1	12.2	7.3	9.4	4.3	-2.8	1.9	0.0	-2.5	9.4	1.7	3.9	17.4
- Gross Capital Fixed Formation	2.0	-3.2	41.7	32.3	27.5	17.2	12.8	8.3	-0.2	3.0	11.6	17.2	8.9
Current Account (% of GDP)	2.3	0.7	5	3.8	5	5	2.3	4.4	4.8	5.9	2.8	3.8	...
Financial Account (US\$ million)	-5610	-4821	-655	835	1183	1585	4098	696	810	4480	1100	51	...
- Net Direct Investments, US\$ million	-1277	-898	-1336	502	-589	168	-487	-543	842	977	404	-424	...
- Net Portfolio Investments, US\$ million	-4390	-1248	-1697	-255	217	948	2811	-649	-903	1202	396	2145	...
Overall BOP position (US\$, million)	11400	1243	1536	1041	1247	1260	-4475	330	712	574	877	807	...
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	Sep-14	Oct-14	Nov-14	Dec-14	Jan-15	Feb-15	Mar-15	Apr-15	May-15	Jun-15	Jul-15	Aug-15	Sep-15
Overseas Filipinos' Remittances (US\$, million)	2,110	2,228	2,122	2,317	1,814	1,876	2,101	2,015	2,099	2,179	2,078	2,044	2,201
... = not available													

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

Table 1. Level of Philippine GDP, 2014Q3 - 2015Q3				
	Nominal GDP		Real GDP	
	(million current pesos)		(million constant 2000 pesos)	
	2014Q3	2015Q3	2014Q3	2015Q3
Agriculture and Forestry	262,566	251,513	124,601	124,634
Fishing	51,881	53,999	30,667	31,201
Mining and Quarrying	28,841	23,313	15,127	15,258
Manufacturing	584,913	579,444	378,608	399,721
Construction	196,842	210,892	101,681	106,592
Electricity Gas and Water Supply	94,834	93,335	63,766	68,067
Transport Communication and Storage	182,296	196,767	118,974	127,992
Trade and Repair of Motor Vehicles Motorcycles Personal	599,733	645,866	312,034	336,620
Financial Intermediation	239,792	255,737	124,033	131,495
Real Estate Renting & Bus. Actvt	399,964	441,403	206,038	221,876
Public Administration & Defense: Compulsory Social Security	122,821	126,210	70,795	72,967
Other Services	282,066	305,778	168,832	182,395
Sum = GDP	3,046,549	3,184,257	1,715,156	1,818,818

Source: Philippine Statistical Authority.

Table 2. Industry Contributions to Philippine GDP Growth, 2014Q3 - 2015Q3

	TRAD	PGE	GPIE	RPE	GEN
	GDP Growth				GDP Growth
	(percent)	(percent)	(percent)	(percent)	(percent)
		(1)	(2)	(3)	(1)+(2)+(3)
GDP Growth	6.04	5.99	0.04	0.02	6.04
Industry Growth Contribution					
Agriculture	0.03	0.03	0.00	-0.18	-0.15
Agriculture and Forestry	0.00	0.00	0.00	-0.24	-0.24
Fishing	0.03	0.03	0.00	0.06	0.10
Industry	1.78	1.60	-0.05	-1.06	0.49
Mining and Quarrying	0.01	0.01	0.00	-0.18	-0.17
Manufacturing	1.23	1.07	-0.05	-0.92	0.10
Construction	0.29	0.31	0.01	0.24	0.56
Electricity Gas and Water Supply	0.25	0.21	-0.01	-0.20	0.00
Services	4.24	4.35	0.09	1.26	5.71
Transport Communication and Storage	0.53	0.45	0.01	0.11	0.57
Trade and Repair of Motor Vehicles Motorcycles Personal	1.43	1.55	0.02	0.25	1.82
Financial Intermediation	0.44	0.47	0.01	0.16	0.65
Real Estate Renting & Bus. Actvt	0.92	1.01	0.04	0.52	1.57
Public Administration & Defense: Compulsory Social Security	0.13	0.12	0.00	0.05	0.17
Other Services	0.79	0.74	0.01	0.17	0.92

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

