Q2 | INFLATION REPORT

2020
SECOND QUARTER

Foreword

The primary objective of monetary policy is to promote a low and stable rate of inflation conducive to a balanced and sustainable economic growth. The adoption in January 2002 of the inflation targeting framework for monetary policy was aimed at helping to fulfill this objective.

One of the key features of inflation targeting is greater transparency, which means greater disclosure and communication by the BSP of its policy actions and decisions. This Inflation Report is published by the BSP as part of its transparency mechanisms under inflation targeting. The objectives of this Inflation Report are: (i) to identify the risks to price stability and discuss their implications for monetary policy; and (ii) to document the economic analysis behind the formulation of monetary policy and convey to the public the overall thinking behind the BSP's decisions on monetary policy. The broad aim is to make monetary policy easier for the public to understand and enable them to better monitor the BSP's commitment to the inflation target, thereby helping both in anchoring inflation expectations and encouraging informed debate on monetary policy issues.

The government's target for annual headline inflation under the inflation targeting framework has been set at 3.0 percent ± 1.0 percentage point (ppt) for 2020-2022 by the Development Budget Coordination Committee. This is consistent with the desired disinflation path over the medium term, favorable trends in inflation dynamics, and expected higher capacity of the economy for growth under a low inflation environment.

The report is published on a quarterly basis, presenting an analysis of the various factors affecting inflation. These include recent price and cost developments, inflation expectations, prospects for aggregate demand and output, labor market conditions, monetary and financial market conditions, fiscal developments, and the international environment. An entire section is devoted to a discussion of monetary policy developments in the most recent quarter, while a separate section provides a comprehensive analysis of the BSP's view of the inflation outlook for the policy horizon.

The Monetary Board approved this Inflation Report at its meeting on 16 July 2020.

BENJAMIN E. DIOKNO
Governor

The Monetary Policy of the Bangko Sentral ng Pilipinas

The BSP Mandate

The BSP's main responsibility is to formulate and implement policy in the areas of money, banking and credit, with the primary objective of maintaining stable prices conducive to a balanced and sustainable economic growth in the Philippines. The BSP also aims to promote and preserve monetary stability and the convertibility of the national currency.

Monetary Policy Instruments

The BSP's primary monetary policy instrument is its overnight reverse repurchase (RRP) or borrowing rate. Other instruments to implement the desired monetary policy stance to achieve the inflation target include (a) increasing/decreasing the reserve requirement (RR); (b) conducting auctions for the term deposit facility (TDF);[1] (c) adjusting the rediscount rate on loans extended to banking institutions on a short-term basis against eligible collateral of banks' borrowers; and (d) outright sales/purchases of the BSP's holdings of government securities.

Policy Target

The BSP's target for monetary policy uses the Consumer Price Index (CPI) or headline inflation rate, which is compiled and released to the public by the Philippine Statistics Authority (PSA). The policy target is set by the Development Budget Coordination Committee (DBCC)[2] in consultation with the BSP. The inflation target for 2020-2022 is 3.0 percent ± 1.0 ppt.[3]

BSP's Explanation Clauses

These are the predefined set of acceptable circumstances under which an inflation-targeting central bank may fail to achieve its inflation target. These clauses reflect the fact that there are limits to the effectiveness of monetary policy and that deviations from the inflation target may sometimes occur because of factors beyond the control of the central bank. Under the inflation targeting framework of the BSP, these exemptions include inflation pressures arising from: (a) volatility in the prices of agricultural products; (b) natural calamities or events that affect a major part of the economy; (c) volatility in the prices of oil products; and (d) significant government policy changes that directly affect prices such as changes in the tax structure, incentives, and subsidies.

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[1] The TDF was introduced under the interest rate corridor system which was implemented on 3 June 2016.

[2] The DBCC, created under Executive Order No. 232 dated 14 May 1970, is an inter-agency committee tasked primarily to formulate the National Government's fiscal program. It is composed of the Office of the President (OP), Department of Budget and Management (DBM), National Economic and Development Authority (NEDA), and the Department of Finance (DOF). The BSP attends the Committee meetings as a resource agency.

[3] In a joint statement with the DBM on 11 December 2019, the DBCC decided to keep the inflation target at 3.0 percent ± 1.0 percentage point for 2020 – 2022.

The Monetary Board

The powers and functions of the BSP, such as the conduct of monetary policy and the supervision over the banking system, are exercised by its Monetary Board (MB), which has seven members appointed by the President of the Philippines. The Monetary Board holds eight (8) monetary policy meetings in a year to review and decide on the stance of monetary policy.

Chairman & Governor
Benjamin E. Diokno

Members
Carlos G. Dominguez III
Felipe M. Medalla
Juan D. De Zuñiga, Jr.
Peter B. Favila
Antonio S. Abacan, Jr.
V. Bruce J. Tolentino

The Advisory Committee

The Advisory Committee was established as an integral part of the institutional setting for inflation targeting. It is tasked to deliberate, discuss, and make recommendations on monetary policy to the Monetary Board. Like the Monetary Board, the Committee meets eight times a year but may also meet between regular meetings, whenever deemed necessary.

Chairman
Benjamin E. Diokno
Governor

Members
Francisco G. Dakila, Jr.
Deputy Governor
Monetary and Economics Sector

Ma. Cyd Tuaño-Amador
Deputy Governor
Corporate Services Sector

Chuchi G. Fonacier
Deputy Governor
Financial Supervision Sector

Ma. Ramona GDT Santiago
Senior Assistant Governor
Financial Market Operations Sub-Sector

Johnny Noe E. Ravalo
Assistant Governor
Office of Systemic Risk Management

Iluminada T. Sicat
Assistant Governor
Monetary Policy Sub-sector

2020 SCHEDULE OF MONETARY POLICY MEETINGS, INFLATION REPORT PRESS CONFERENCE AND PUBLICATION OF MB HIGHLIGHTS

2020	Advisory Committee (AC) Meeting	Monetary Board (MB) Meeting	MB Highlights Publication	Inflation Report (IR) Press Conference
Jan	31 (Fri) (AC Meeting No. 1)		9 (Thu) (12 Dec 2019 MB meeting)	24 (Fri) (Q4 2019 IR)
Feb		6 (Thu) (MB Meeting No. 1)		
Mar	13 (Fri) (AC Meeting No. 2)	19 (Thu) (MB Meeting No. 2)	5 (Thu) (6 Feb 2020 MB meeting)	
Apr			16 (Thu) (19 Mar 2020 MB meeting)	24 (Fri) (Q1 2020 IR)
May	15 (Fri) (AC Meeting No. 3)	21 (Thu) (MB Meeting No. 3)		
Jun	19 (Fri) (AC Meeting No. 4)	25 (Thu) (MB Meeting No. 4)	18 (Thu) (21 May 2020 MB meeting)	
Jul			23 (Thu) (25 Jun 2020 MB meeting)	27 (Mon) (Q2 2020 IR)
Aug	14 (Fri) (AC Meeting No. 5)	20 (Thu) (MB Meeting No. 5)		
Sep	25 (Fri) (AC Meeting No. 6)		17 (Thu) (20 Aug 2020 MB meeting)	
Oct		1 (Thu) (MB Meeting No. 6)	29 (Thu) (1 Oct 2020 MB meeting)	30 (Fri) (Q3 2020 IR)
Nov	13 (Fri) (AC Meeting No. 7)	19 (Thu) (MB Meeting No. 7)		
Dec	11 (Fri) (AC Meeting No. 8)	17 (Thu) (MB Meeting No. 8)	17 (Thu) (19 Nov 2020 MB meeting)	

List of Acronyms, Abbreviations, and Symbols

ASF	African Swine Fever
AHFF	Agriculture, Hunting, Forestry and Fishing
AONCR	Areas Outside the National Capital Region
ASEAN	Association of Southeast Asian Nations
BAP	Bankers Association of the Philippines
BES	Business Expectations Survey
BI	Bank Indonesia
BIR	Bureau of Internal Revenue
BIS	Bank for International Settlements
BNM	Bank Negara Malaysia
BOC	Bureau of Customs
BOT	Bank of Thailand
bp	Basis Point
BPO	Business Process Outsourcing
BTr	Bureau of the Treasury
CALABARZON	Cavite, Laguna, Batangas, Rizal and Quezon
CAMPI	Chamber of Automotive Manufacturers of the Philippines, Inc.
CAR	Capital Adequacy Ratio
CBD	Central Business District
CDS	Credit Default Swap
CES	Consumer Expectations Survey
CI	Confidence Index
CPI	Consumer Price Index
DA	Department of Agriculture
DBCC	Development Budget Coordination Committee
DBM	Department of Budget and Management
DI	Diffusion Index
DOE	Department of Energy
DOF	Department of Finance
DPWH	Department of Public Works and Highways
EIA	Energy Information Administration
EMBIG	Emerging Market Bond Index Global
ERC	Energy Regulatory Commission
FCD	Foreign Currency Deposit
FDI	Foreign Direct Investment
FOMC	Federal Open Market Committee
GDP	Gross Domestic Product
GIR	Gross International Reserve
GNI	Gross National Income
GNPL	Gross Non-Performing Loan
GOUR	Generation Over/Under Recovery
GS	Government Securities
IMF	International Monetary Fund
IMTS	International Merchandise Trade Statistics
IPP	Independent Power Producers
kWh	Kilowatt Hour
LEM	Loans Especially Mentioned
LFS	Labor Force Survey
LGU	Local Government Unit
LRT	Light Railway Transit
LSOUR	Lifeline Subsidy Over/Under Recovery
MB	Monetary Board
mb/d	Million Barrels per Day
MERALCO	Manila Electric Company
MISSI	Monthly Integrated Survey of Selected Industries
MTP	Major Trading Partner
MUP	Military and Uniformed Personnel

NBQBs	Non-Banks with Quasi-Banking Function
NCR	National Capital Region
NEDA	National Economic and Development Authority
NEER	Nominal Effective Exchange Rate
NFA	Net Foreign Asset
NG	National Government
NGCP	National Grid Corporation of the Philippines
NIA	National Income Accounts
NNPL	Net Non-Performing Loans
NPC	National Power Corporation
NSFR	Net Stable Funding Ratio
NSS	Net Settlement Surplus
ODF	Overnight Deposit Facility
OFW	Overseas Filipino Worker
OP	Office of the President
OPEC	Organization of the Petroleum Exporting Countries
OPR	Overnight Policy Rate
PBOC	People's Bank of China
PISM	Philippine Institute for Supply Management
PMI	Purchasing Managers' Index
ppt	Percentage Point
PSA	Philippine Statistics Authority; Power Supply Agreement
PSALM	Power Sector Assets and Liabilities Management
PSEi	Philippine Stock Exchange Index
QBs	Quasi-Banks
q-o-q	Quarter-on-Quarter
RBs	Rural Banks
REER	Real Effective Exchange Rate
RP	Repurchase
RR	Reserve Requirement
RREL	Residential Real Estate Loan
RREPI	Residential Real Estate Price Index
RRP	Reverse Repurchase
RRR	Reserve Requirement Ratio
SBL	Substandard or Below Loan
SDA	Special Deposit Account
SEC	Securities and Exchange Commission
SLOS	Senior Bank Loan Officers' Survey
SLOUR	System Loss Over/Under Recovery
SME	Small and Medium Enterprise
SRR	Statutory Reserve Requirement
TAFPPC	True-up Adjustments of Fuel and Purchased Power Cost
TAFxA	True-up Adjustments of Foreign Exchange Related Costs
TBs	Thrift Banks
TDF	Term Deposit Facility
TLP	Total Loan Portfolio
TOUR	Transmission Over/Under Recovery
TPI	Trading Partner Index
TPI-A	Trading Partner Index in Advanced Countries
TPI-D	Trading Partner Index in Developing Countries
U/KBs	Universal and Commercial Banks
VaPI	Value of Production Index
VoPI	Volume of Production Index
WEO	World Economic Outlook
WESM	Wholesale Electricity Spot Market
WTO	World Trade Organization
y-o-y	Year-on-Year
y-t-d	Year-to-Date

Contents

Overview

Headline inflation eases further but remains within target range. The Q2 2020 inflation settled at 2.3 percent year-on-year (y-o-y), lower than the quarter- and year-ago rates of 2.7 percent and 3.0 percent, respectively. The slowdown was driven mainly by the significant fall in global oil prices. The year-to-date inflation of 2.5 percent in the first half of 2020 remains within the National Government's (NG) inflation target of 3.0 percent ± 1.0 percentage point.

Q2 2020 inflation eases but remains within 2-4 percent target range

Core inflation was also lower at 2.9 percent y-o-y in Q2 2020 from 3.2 percent in the previous quarter. Similarly, all three BSP-computed alternative core inflation measures eased during the review quarter. Consistent with the downtrend in overall inflation, the number of CPI items with inflation rates higher than the threshold of 4.0 percent decreased to 55 items from 61 items in the previous quarter. These items accounted for about 18.3 percent of the total weight in the CPI basket for Q2 2020.

Inflation expectations are lower but remain manageable. The results of the BSP's survey on private sector economists for June 2020 indicate lower mean inflation forecasts over the policy horizon relative to the March 2020 survey. Private sector forecasts decreased to 2.3 percent from 2.9 percent for 2020, and 2.9 percent from 3.0 percent for 2021 and 2022. Analysts expect 2020 inflation to be at the lower end of the target range, with risks to the inflation outlook leaning to the upside with the anticipated recovery following the relaxation of quarantine measures. Nevertheless, a key downside risk to the analysts' inflation outlook is the subdued domestic demand given high unemployment resulting from closure of businesses.

Domestic economy slows down. The Q1 2020 real gross domestic product (GDP) contracted to 0.2 percent from 6.7 percent and 5.7 percent in the previous quarter and year. Domestic activity declined significantly as demand fell and production was constrained following the implementation of community quarantines to contain the COVID-19 pandemic. On the demand side, household spending was almost nil at 0.2 percent while investments declined by 18.3 percent. On the supply side, the services sector slowed to 1.4 percent while the other production sectors of the economy contracted.

Domestic growth slows down in Q1 2020

Forward-looking and high frequency indicators also suggest a weakening in domestic demand. Preliminary composite Purchasing Managers' Index (PMI) for June 2020 was below the expansion threshold at 43.8 index points as all surveyed industries continued to report contractions. However, results of the June survey also suggest some degree of improvement as more businesses re-opened following the gradual easing of lockdown and quarantine measures in most parts of the country. On the other hand, the average capacity utilization in the manufacturing sector remained below the optimal level in May 2020 as production orders deteriorated. Other demand barometers such as new vehicles sales and energy usage in residential, commercial, and industrial areas declined notably. Meanwhile, real estate prices show modest increases although a slowdown in leasing activities for office spaces has been noted.

Global economic activity further contracts. The JP Morgan Global All-Industry Output Index remained in contraction territory at 47.7 in June 2020 as new business volumes fell for the fifth successive month. This follows contractions in key economies in Q1 2020 such as in the US, euro area, China and Japan as the global health crisis necessitated the imposition of economic lockdowns. Moreover, while manufacturing PMIs in US and China point to gradual expansions, that of other economies including the ASEAN region are still in contraction territory. The uncertain and uneven pace of recovery, even as economies begin to reopen gradually, prompted several central banks, mostly within the region and including the BSP, to continue with their accommodative monetary policy stance to provide support to their respective economies.

The domestic financial system remains stable amid high uncertainty. Market volatility due to expectations of the negative impact of the COVID-19 pandemic on the economy led to the

15.2-percent decline in the Philippine Stock Exchange index (PSEi), quarter-on-quarter, to average at 5,832.17 index points. Nevertheless, the decisive policy actions of the BSP in Q2 2020 to ease monetary conditions and enhance financial liquidity restored investor sentiment. Following the BSP actions, issuance of government securities by the Bureau of the Treasury were consistently oversubscribed, with yields declining due in part to strong market interest. The optimism on the country's response to the pandemic was likewise seen in the performance of the peso which averaged ₱50.45/US$1 in Q2 2020, appreciating by 0.75 percent from the previous quarter. The country's macroeconomic fundamentals, which include the manageable inflation environment, a strong and resilient banking system, prudent fiscal position, and a high level of international reserve buffer provided support to the peso. Moreover, the country's banking system remained sound and stable. Asset and deposits continued to grow and capital adequacy ratios remain above the BSP's and Bank for International Settlements' prescribed levels.

The BSP reduced the key policy rate twice by a total of 100 bps in Q2 2020. The BSP decided to lower the key policy interest rate by 50 basis points (bps) in an off-cycle policy meeting in April. A follow-through interest rate cut by another 50 bps was decided in the scheduled June policy meeting. This brings the RRP rate to a record low of 2.25 percent. In deciding to reduce the key policy interest rate twice during the review quarter, the BSP considered the impact of the COVID-19 pandemic on the Philippine economy.

Key policy rate reduced by 100 bps in Q2 2020 in response to the COVID-19 pandemic

Moreover, latest baseline forecasts during the review period indicate that inflation could settle near the low end of the target range of 3.0 percent ± 1 percentage point for 2020 up to 2022, with inflation expectations remaining firmly anchored over the policy horizon. Meanwhile, the balance of risks to the inflation outlook leans toward the downside from 2020 up to 2022 owing largely to the potential impact of a deeper and more disruptive pandemic on domestic and global demand conditions.

Given these considerations, the BSP believes that there remains a critical need for continuing measures to bolster economic activity and support financial conditions. Keeping the monetary stance sufficiently accommodative amid a benign inflation environment will help mitigate the strong downside risks to growth and boost market confidence. Even with the improvement in domestic liquidity conditions and market function owing to prior liquidity-enhancing measures, the policy rate cuts during the quarter will also help ease the cost of borrowing further and ensure ample credit and liquidity in the financial system as the economy transitions toward recovery in the coming months.

Going forward, the BSP reiterates its support for the health and fiscal programs already being rolled out by the NG in responding to the needs of Filipino households and businesses. The BSP remains committed to deploying its full range of monetary instruments and regulatory relief measures as needed in the fulfillment of its mandate to promote non-inflationary and sustainable growth.

I. Inflation and Real Sector Developments

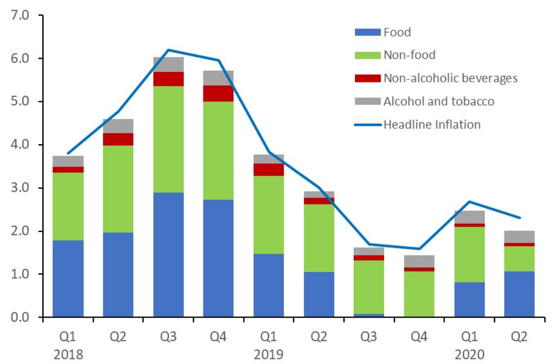
Prices

Headline inflation. Headline inflation in Q2 2020 settled at 2.3 percent year-on-year (y-o-y), lower than quarter- and year-ago rates of 2.7 percent and 3.0 percent, respectively. The slowdown was driven mainly by lower non-food inflation stemming from the significant decline in global oil prices that, in turn, offset higher food inflation.

Inflation eases further in Q2 2020 but remains within the target range

The year-to-date inflation of 2.5 percent in the first half of 2020 remains within the National Government's (NG) inflation target of 3.0 percent ± 1.0 percentage point for the year.

Chart 1. Quarterly Headline Inflation (2012=100)
In percent



Source: PSA and BSP estimates

Core Inflation. Core inflation—which excludes selected volatile food and energy items to measure underlying price pressures—also eased to 2.9 percent y-o-y in Q2 2020 from 3.2 percent in the previous quarter.

Official core inflation eases

Likewise, preliminary estimates showed that all three BSP-computed alternative core inflation measures, also eased in Q2 2020 from their previous quarter's levels.

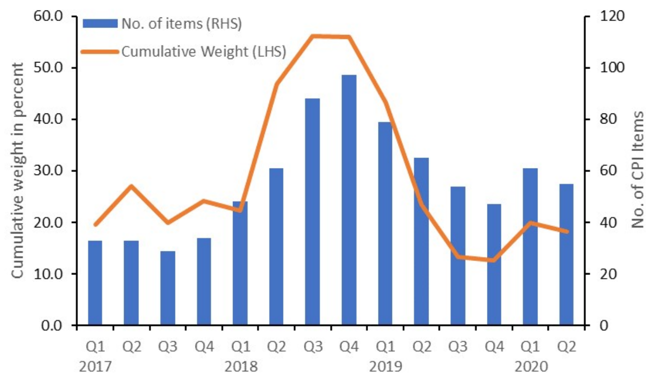
Table 1. Alternative Core Inflation Measures
Quarterly averages of year-on-year change

Quarter	Official Headline Inflation	Official Core Inflation	Trimmed Mean[1]	Weighted Median[2]	Net of Volatile Items[3]
2019					
Q1	3.8	3.9	3.8	3.4	3.7
Q2	3.0	3.4	2.9	3.0	3.0
Q3	1.7	2.9	1.9	2.8	3.3
Q4	1.6	2.7	1.7	2.6	3.3
2020					
Q1	2.7	3.2	2.2	2.6	3.8
Q2	2.3	2.9	2.1	2.3	3.5

[1] The trimmed mean represents the average inflation rate of the (weighted) middle 70 percent in a lowest-to-highest ranking of year-on-year inflation rates for all CPI components.
[2] The weighted median represents the middle inflation rate (corresponding to a cumulative CPI weight of 50 percent) in a lowest-to-highest ranking of year-on-year inflation rates.
[3] The net of volatile items method excludes the following items: bread and cereals, vegetables, sugar, jam, honey, chocolate, and confectionery, electricity, gas, fuel and lubricants for personal transport equipment, and passenger transport by road, which represents 29.5 percent of all items.
Source: PSA and BSP estimates

The number of CPI items (at the sub-classes level) with inflation rates higher than the threshold of 4.0 percent[4] dropped to 55 items in Q2 2020 from 61 items in the previous quarter.

Chart 2. CPI Items with Inflation Rates Above Threshold (2012=100)



Source: BSP

These items accounted for around 18.3 percent (from 20 percent in the previous quarter) of the total weight in the CPI basket.

[4] Based on the upper end of the NG's 2-4 percent target range for 2020.

Food Inflation. Food inflation accelerated in Q2 2020 compared to the previous quarter's level. Rice inflation, on a y-o-y basis, has turned less negative in Q2 2020 amid an increase in rice prices due to supply bottlenecks as quarantine measures impeded farming and trading activities in the provinces. At the same time, strong local demand from national agencies, local government units, and non-government organizations to shore up relief efforts also contributed to the increase in rice prices in Q2 2020.

Food inflation accelerates in Q2 2020

Meanwhile, hurdles in the transport of food items amid the Luzon-wide quarantine has also exerted upward pressure on food prices during the quarter, prompting the government to implement various measures (i.e., food pass system) to address logistical issues and ease supply-side pressures. The y-o-y inflation for fruits, oils and fats, as well as milk, cheese, and eggs accelerated in Q2 2020 compared to the previous quarter.

Table 2. Inflation Rates for Selected Food Items (2012=100)
Year-on-year, in percent

Commodity	2019	2020	
	Q2	Q1	Q2
Food and Non-Alcoholic Beverages	**3.0**	**2.3**	**3.0**
Food	3.0	2.3	3.0
Bread and Cereals	0.2	-4.0	-1.4
Rice	-0.8	-6.1	-2.8
Corn	-3.3	-2.2	-0.2
Meat	3.6	3.0	2.7
Fish	3.8	9.3	8.0
Milk, Cheese and Eggs	2.5	3.3	3.6
Oils and Fats	3.1	1.0	2.0
Fruit	4.1	8.7	11.1
Vegetables	9.9	8.1	7.4
Sugar, Jam, Honey, Chocolate and Confectionery	4.6	-1.7	-0.8
Food Products N.E.C.	6.5	6.8	6.6
Non-Alcoholic Beverages	5.1	2.8	2.6
Alcoholic Beverages and Tobacco	9.5	18.4	18.1

Source: PSA and BSP estimates

Non-food Inflation. By contrast, non-food inflation eased as most sub-components posted lower y-o-y inflation in Q2 2020 relative to Q1 2020. In particular, inflation for housing, water, electricity, gas, and other fuels slowed down in Q2 2020 due to lower electricity rates as generation charges declined while lower LPG and kerosene prices also contributed to the slowdown.

Non-food inflation fell as global oil prices decline

At the same time, transport inflation also declined owing to the significant drop in global oil prices as reflected in the negative inflation for operation of personal transport equipment. This was tempered slightly by the higher inflation for transport services from the tricycle fare hike during the quarter.

Table 3. Inflation Rates for Selected Non-Food Items (2012=100)
Year-on-year, in percent

Commodity	2019	2020	
	Q2	Q1	Q2
Non-Food	**2.6**	**2.1**	**1.0**
Clothing and Footwear	2.4	2.7	2.5
Housing, Water, Electricity, Gas, and Other Fuels	3.2	1.9	0.3
Furnishings, Household Equipment, and Routine Maintenance of the House	3.2	3.6	4.1
Health	3.6	2.9	2.8
Transport	3.0	1.0	-3.2
Communication	0.4	0.4	0.3
Recreation and Culture	3.1	1.5	1.4
Education	-4.0	4.7	3.6
Restaurants and Miscellaneous Goods and Services	3.3	2.6	2.4

Source of basic data: PSA and BSP

Private Sector Economists' Inflation Forecasts.[5] The results of the BSP's survey of private sector economists for June 2020 showed lower mean inflation forecasts for 2020 to 2022 relative to the March 2020 survey.[6]

Inflation expectations are lower but remain within NG's target range

Based on the June 2020 survey, the mean inflation forecast for 2020 decreased to 2.3 percent from 2.9 percent. Similarly, mean inflation forecasts for 2021 and 2022 both declined to 2.9 percent from 3.0 percent.

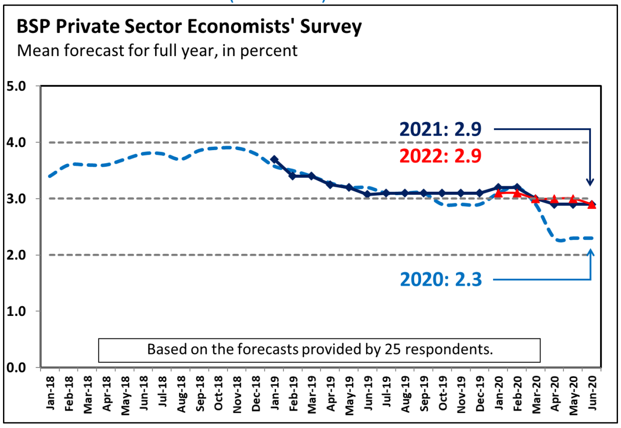
[5] No update on inflation expectations based on the Business Expectations Survey and Consumer Expectations Survey. There were no surveys conducted for Q2 2020.
[6] There were 25 respondents in the BSP's survey of private sector economists in June 2020. The survey was conducted from 8 to 12 June 2020.

Chart 3. BSP Private Sector Economists' Survey*

Mean forecast for full year; in percent

January 2016 to February 2018 (2006=100)

March 2018 to June 2020 (2012=100)



Analysts expect inflation to hover near the lower end of the target range in 2020, with risks to the inflation outlook generally leaning towards the upside given the anticipated recovery in domestic demand following the recent relaxation of lockdown and quarantine measures.

The key upside risks to inflation include
(a) possible strong rebound in global oil prices;
(b) increase in private consumption following the recent easing of quarantine measures;
(c) challenging supply chain and logistics for basic and essential commodities; (d) higher prices of food, including rice; and (e) adverse weather conditions such as typhoons, which could affect food supply.

Meanwhile, downside risks to inflation are seen to emanate from (a) subdued domestic demand due to high unemployment resulting from the closure of businesses; (b) persistent downside pressures on global crude oil prices; and (c) price ceilings imposed by the government on selected commodities.

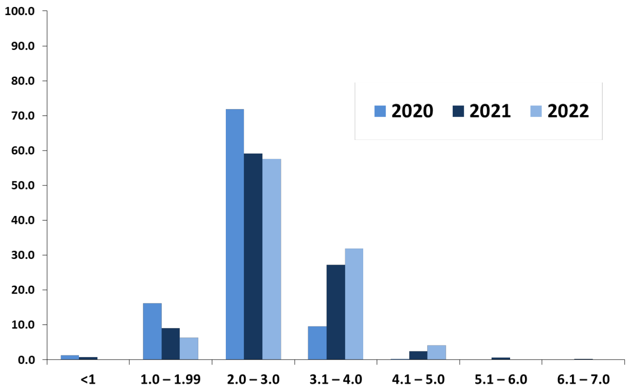
Table 4. Private Sector Forecasts for Inflation

Annual percentage change; June 2020 (2012=100)

	2020			2021	2022
	Q3	Q4	FY	FY	FY
1) Al-Amanah Islamic Bank	2.50	3.00	3.00	3.00	3.00
2) Banco De Oro	2.26	2.35	2.36	2.70	3.00
3) Bangkok Bank	2.20	2.30	2.30	3.00	3.00
4) Bank of Commerce	2.02	2.28	2.27	-	-
5) Bank of China Ltd.	2.30	2.20	2.20	2.50	2.50
6) Barclays	2.30	2.40	2.40	3.00	-
7) Citibank	2.20	1.60	2.20	2.40	-
8) Chinabank	2.00	2.00	2.30	2.40	2.40
9) CTBC Bank	2.00 - 2.50	2.00 - 2.50	1.50 - 2.50	2.50 - 3.50	3.00 - 4.00
10) Deutsche Bank	-	-	2.70	3.70	-
11) Eastwest Bank	2.50	2.40	2.40	2.40	3.10
12) Global Source	2.60	2.50	2.50	2.90	3.00
13) Korea Exchange Bank	2.50	2.25	2.50	2.50	2.75
14) Land Bank of the Phils	2.10	2.40	2.30	2.30	2.10
15) Maybank	2.10	2.40	2.32	3.50	3.20
16) Maybank-ATR KimEng	1.80	1.50	2.00	2.00	2.50
17) Metrobank	-	-	2.00 - 3.00	-	-
18) Nomura	1.80	1.60	2.10	2.60	-
19) RCBC	2.20	2.00	2.20	2.70 - 3.20	2.90 - 3.40
20) Robinsons Bank	2.20	2.40	2.40	3.00	3.00
21) Philippine Equity Partners	2.30	2.40	2.40	3.10	-
22) Security Bank	2.10	2.20	2.10	3.00	3.10
23) Standard Chartered	1.10	0.80	1.60	4.00	2.50
24) Union Bank of the Phils.	3.00	3.30	2.80	3.90	3.40
25) UBS	2.30	2.20	2.30	2.50	-
Median Forecast	2.2	2.3	2.3	3.0	3.0
Mean Forecast	**2.2**	**2.2**	**2.3**	**2.9**	**2.9**
High	3.0	3.3	3.0	4.0	3.5
Low	1.1	0.8	1.6	2.0	2.1
Number of observations	23	23	25	23	17
Government Target	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**	**3.0±1.0**

Based on the probability distribution of the forecasts provided by 20 out of 25 respondents, there is an 81.6-percent probability that average inflation for 2020 will settle between the 2-4 percent range, while there is a 17.6-percent chance that inflation will fall below 2.0 percent. Meanwhile, the probabilities that inflation will fall within the target band in 2021 and 2022 are seen at 86.5 percent and 89.4 percent.

Chart 4. Probability Distribution for Analysts' Inflation Forecasts* (2020-2022)



*Probability distributions were averages of those provided by 20 of 25 respondents.
(Source: June 2020 BSP Survey)

Energy prices. Dubai crude oil prices remained subdued in Q2 2020, declining by 39.8 percent on a quarter-on-quarter (q-o-q) basis. Despite rising in May and June, prices remained significantly lower compared to Q1 2020.

Lower global oil prices can be traced to expectations of weaker oil demand amid reduced economic activity following mitigating measures imposed by governments to limit the spread of COVID-19. Based on the International Energy Agency (IEA) estimates, global oil demand is expected to decline by 8.1 million barrels per day (mb/d) in 2020.[7]

Nevertheless, production cuts from the Organization of the Petroleum Exporting Countries and its allies (OPEC+), declining US tight oil production, and reopening efforts have pushed prices higher in May and June 2020.

Expectations of weaker oil demand continue to weigh down on global oil prices

The estimated futures prices of Dubai crude oil as of end-June 2020,[8] which are based on movements of Brent crude futures price, showed a higher path for 2020 – 2022 compared to the previous quarter's level (as of 31 March 2020).

On a year-to-date basis, there was a net price decrease of domestic petroleum products as of 30 June 2020.[9] A net price decrease was recorded for gasoline, diesel, and kerosene at ₱4.97 per liter, ₱8.84 per liter, and ₱12.99 per liter, respectively, compared to end-2019 level.

Power. The overall electricity rate in the Meralco-serviced area declined by around ₱0.25 per kilowatt hour (kWh) to ₱8.82 per kWh (from ₱9.07 per kWh in Q1 2020) on the back of lower generation charge. According to Meralco, the downward adjustment in the generation cost was due primarily to the reduction in fixed costs for generation capacity as a result of Meralco's Force Majeure claim. Meralco invoked the Force Majeure provision in its Power Supply Agreements (PSAs) from April to June 2020, owing to the significant reduction in power demand in its service area during the implementation of community quarantine. At the same time, contributing to the decline in generation charges during the review period was the reduction in the cost of power from the Independent Power Producers (IPPs) as a result of higher average plant dispatch, lower fuel prices, and the appreciation of the peso against the US dollar. Likewise, charges from the Wholesale Electricity Spot Market (WESM) declined in April driven by improved supply conditions in the Luzon grid.

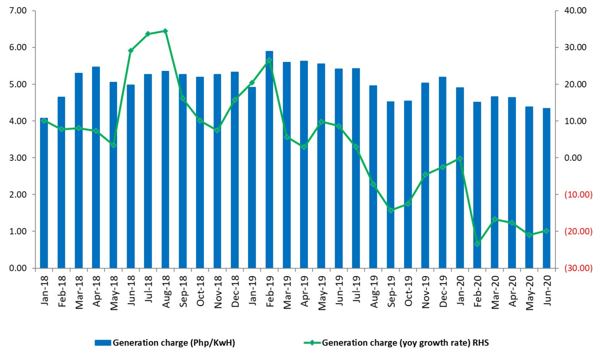
Retail electricity prices are lower

There are potential sources of upside pressures on electricity charges. Meralco has existing petitions for rate increases with ERC which include the petition to implement the Maximum Average Price for 2012, 2013, 2014, and 2015, amended application for a rate increase in the January 2014 billing (consisting of incremental fuel costs and deferred generation cost to be collected monthly for six months); and petitions for the refund of generation over/under recovery (GOUR), transmission over/under recovery (TOUR), system loss over/under recovery (SLOUR), and lifeline subsidy over/under recovery (LSOUR) for the period January-December 2011.

In addition, the Power Sector Assets and Liabilities Management (PSALM) has several pending petitions with ERC for the recovery of True-Up Adjustments of Fuel and Purchased Power Costs (TAFPPC), Foreign Exchange Related Costs (TAFxA) and Purchased Power Costs and Foreign Exchange Related Costs by the National Power Corporation (NPC), and NPC's Stranded Debt portion of the universal charge. Likewise, the National Grid Corporation of the Philippines (NGCP) also filed several petitions to recover connection charges and residual sub-transmission charges for 2011-2013 and the costs of repair on damages caused by force majeure events such as earthquake, flooding, landslides, and lightning incidents in 2011-2012.

[7] Source: IEA Oil Market Report (June 2020), https://www.iea.org/reports/oil-market-report-june-2020
[8] Future prices using Brent crude futures data. Taken as of 30 June 2020. Sources: Bloomberg L.P. and BSP-staff calculations.
[9] Based on the Department of Energy (DOE) prevailing retail prices of petroleum products in NCR/Metro Manila: https://www.doe.gov.ph/oil-monitor?q=oil-monitor

Chart 5. Meralco's Generation Charge
PhP/kWh; year-on-year growth rates in percent



Source: Meralco

Aggregate Demand and Supply[10]

The Q1 2020 real gross domestic product (GDP) contracted to 0.2 percent, y-o-y, from 6.7 percent in Q4 2019 and 5.7 percent in Q1 2019. This was the first recorded contraction since Q4 1998. The decline in economic activity was due to lower domestic demand as well as production constraints following the implementation of the Enhanced Community Quarantine (ECQ) beginning in mid-March 2020 to contain the COVID-19 pandemic and, to some extent, the impact of the Taal Volcano eruption in January 2020.

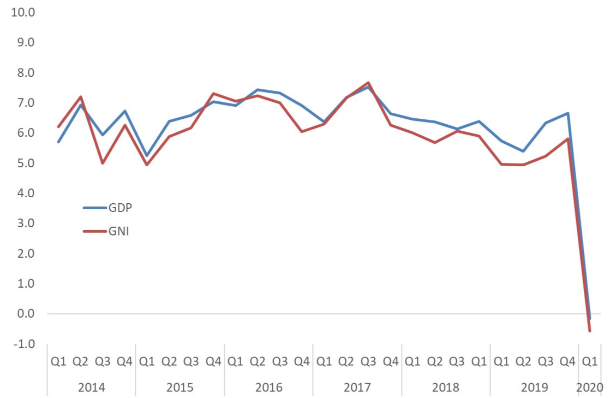
Real GDP slows down significantly in Q1 2020

On the demand side, household consumption weakened significantly to 0.2 percent in Q1 2020 from 5.7 percent in Q4 2019 and 6.2 percent in Q1 2019. Government spending grew by 7.1 percent, slower compared to 17.0 percent in Q4 2019 but slightly higher than 6.4 percent in Q1 2019. Meanwhile, investments declined by 18.3 percent, a reversal from the 2.5-percent and 9.8-percent growth rates in Q4 2019 and Q1 2019, respectively.

On the supply side, growth in the services sector moderated substantially by 1.4 percent in Q1 2020 from 8.1 percent in Q4 2019 and 7.1 percent in Q1 2019. Both the industry and agriculture, forestry and fishing (AFF) sectors declined by 3.0 percent (from expansions of 6.0 percent and 4.9 percent in the previous quarter and year) and by 0.4 percent (from growth of 0.8 percent and 0.5 percent in the previous quarter and year), respectively.

Gross national income (GNI) posted a 0.6-percent decline in Q1 2020, from the 5.8-percent and 5.0-percent expansions in Q4 2019 and Q1 2019, respectively. Likewise, net primary income declined further by 4.4 percent from the recorded contractions by 2.8 percent and 1.6 percent in the previous quarter and year, respectively.

Chart 6. Gross Domestic Product (GDP) and Gross National Income (GNI)
At constant 2018 prices



Source: PSA

Aggregate Demand. Under the expenditure approach, household spending, government spending, net exports, and investments (or capital formation) contributed 0.1 ppt, 0.8 ppt, 2.9 ppts, and -4.7 ppts, respectively, to total GDP growth in Q1 2020.

Decline in investments weighs down aggregate demand

Household expenditures, which accounted for 74.5 percent of GDP in Q1 2020, grew marginally by 0.2 percent in Q1 2020 from 5.7 percent in Q4 2019. The subdued growth can be attributed to the decline in expenditures for restaurants and hotels (-15.4 percent from 8.1 percent in Q4 2019) and transport (-8.9 percent from 5.0 in Q4 2019) amid the closure of tourism-related establishments in CALABARZON and cancellation of nearly 400 domestic flights due to the Taal volcano eruption in January 2020. Moreover, the decisions of the national and local governments to impose an ECQ in most regions banned non-essential activities and suspended the operations of public land, water, and air transportation. The

[10] Estimates on the first quarter 2020 National Accounts of the Philippines (NAP) are based on the 2018 base year following the recent revision and rebasing of the NAP series.

ECQ restrictions also resulted in the decline in purchases of furnishings, household equipment, and routine household maintenance (-7.4 percent from 5.0 in Q4 2019), and recreation and culture (-1.9 percent from 6.6 in Q4 2019). Receipts for alcoholic beverages and tobacco also dropped further by 16.4 percent in Q1 2020. Other household commodities that posted slower growth in Q1 2020 include miscellaneous goods and services, food and non-alcoholic beverages, housing, water, electricity, gas, and other fuels, education, clothing and footwear, and communication

Government expenditures increased by 7.1 percent in Q1 2020 from 17.0 percent in Q4 2019. Based on the actual disbursements data (net of accounts payable) from the Department of Budget and Management (DBM), government spending for personnel services increased on account of higher pension requirements and filling of positions for military and uniformed personnel. Likewise, the government's maintenance and other operating expenses increased in Q1 2020.

Investments declined by 18.3 percent in Q1 2020, a reversal of the 2.5-percent expansion in Q4 2019. The contraction in total investments was due mainly to the sustained drawdown in inventories as well as the slump in construction activities particularly by the general government and financial and non-financial corporations. Additionally, all construction activities were halted temporarily due to the implementation of the ECQ in Luzon and other areas in the country. Other sub-sectors that posted weaker growth include durable equipment, breeding stock and orchard development, and intellectual property products, and valuables.

Table 5. Gross Domestic Product by Expenditure
At constant 2018 prices; growth rate in percent

BY EXPENDITURE ITEM	2019				2020
	Q1	Q2	Q3	Q4	Q1
Household Consumption	6.2	5.6	6.0	5.7	0.2
Government Expenditure	6.4	6.8	8.8	17.0	7.1
Capital Formation	9.8	-0.8	-0.1	2.5	-18.3
Fixed Capital	7.8	-2.9	5.9	5.8	-4.3
Exports	4.2	3.1	1.8	0.3	-3.0
Imports	8.9	0.1	-0.1	-0.7	-9.0

Source: PSA

Overall exports decreased by 3.0 percent in Q1 2020 from 0.3 percent in Q4 2019 due mainly to the contraction in exports of services (-4.3 percent from 3.2 percent in Q4 2019) particularly, travel services and transport services. The Department of Tourism estimated foreign tourist arrivals from January to March 2020 to have decreased by 40.2 percent y-o-y on travel restrictions and quarantine measures imposed worldwide amid the COVID-19 pandemic. Merchandise exports also sustained its downtrend due largely to the contraction in export sales of chemicals to major markets such as Japan, China, and the US as the health crisis dampened global economic activity.

Overall imports declined further by 9.0 percent in Q1 2020 from 0.7 percent in Q4 2019. The continued downtrend in imports of goods, particularly electronic products, was attributed to disruptions in the global supply chain brought by the COVID-19 pandemic. Likewise, imports of services weakened during Q1 2020, particularly travel, as many countries imposed travel restrictions to avoid the spread of the disease, while non-essential outbound travel of Filipinos were suspended.

Other Demand Indicators.[11] High-frequency demand indicators suggest a weakening in the domestic economy in the near term. Preliminary composite PMI as of June 2020 was below the 50-index point expansion territory while production orders in the manufacturing sector deteriorated sharply. Other demand barometers point to sales decline as well, such as new vehicles and energy. Meanwhile, real estate prices show modest increases although a slowdown in leasing activities for office spaces has been noted.

Property Prices

Capital Values. Average capital values[12] for office buildings in Metro Manila[13] in Q1 2020 rose by 15.6 percent y-o-y to ₱212,077/sq.m., almost unchanged from the previous quarter's increase but slightly lower than a year ago.

Capital values for office and residential buildings increase

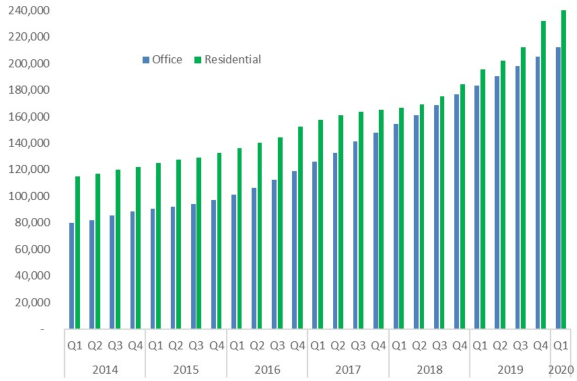
In terms of location, capital values for office buildings in Manila Bay area recorded the highest

[11] There were no surveys conducted for Q2 2020 Business Expectations Survey and Consumer Expectations Survey.
[12] Probable price that the property would have fetched if sold on the date of the valuation. The valuation includes imputed land and building value.
[13] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, Alabang, and Manila Bay Area.

y-o-y growth at 32.1 percent in Q1 2020, albeit slower from the 43.4 percent in the same period in 2019.

Likewise, average capital values for luxury residential buildings[14] in Metro Manila[15] in Q1 2020 increased to ₱245,811/sq.m., higher by 25.7 percent y-o-y. In terms of location, capital values for three-bedroom luxury residential condominium units in Fort Bonifacio area recorded the highest y-o-y growth at 35.6 percent in Q1 2020, a further increase from the 22.0-percent expansion in the same period in 2019.

Chart 7. Capital Values
Price per square meter



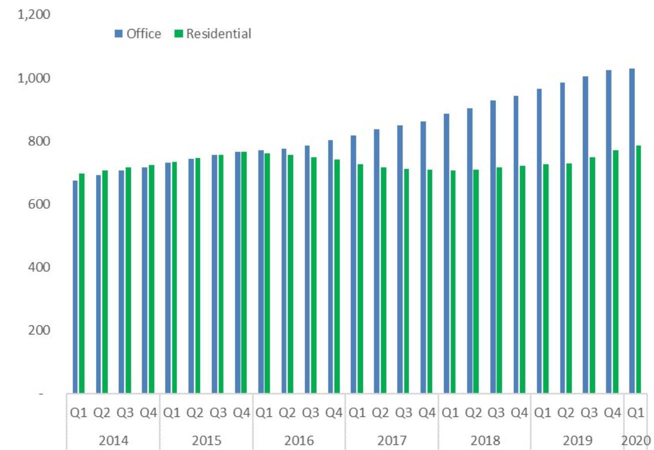
Source: Colliers International Philippines

Rental Values[16] Average monthly office rents in Metro Manila reached ₱1,029/sq.m. in Q1 2020, an increase by 6.6 percent y-o-y, which is slightly lower than the 8.6-percent and 8.8-percent increases in the previous quarter and year. The slight appreciation in office rental rates was due to the sustained demand from offshore gaming and traditional firms. In terms of location, rental values for office buildings in Manila Bay area recorded the highest growth at 13.2 percent y-o-y in Q1 2020, albeit slower than the 19.4-percent expansion in the same period in 2019.

Rental values for office and residential spaces increase

Average monthly rents for luxury three-bedroom condominium units in the Metro Manila was recorded at ₱786/sq.m. in Q1 2020, higher by 8.2 percent y-o-y. The increase in rents in Metro Manila in Q1 2020 could be attributed to the continued demand from foreign and local employees, especially in business districts. In terms of location, capital values for three-bedroom luxury residential condo units in Makati CBD recorded the highest y-o-y growth at 12.0 percent in Q1 2020. This was faster than the 3.1-percent growth in the same period in 2019.

Chart 8. Rental Values
Price per square meter



Source: Colliers International Philippines

Vacancy Rates. The overall office vacancy rate in Metro Manila was lower at 4.1 percent in Q1 2020 from 4.3 percent in the Q4 2019 and 5.4 percent in Q1 2019 due mainly to the sustained take up from outsourcing and traditional firms.

Vacancy rates for offices decline while that for residences increase

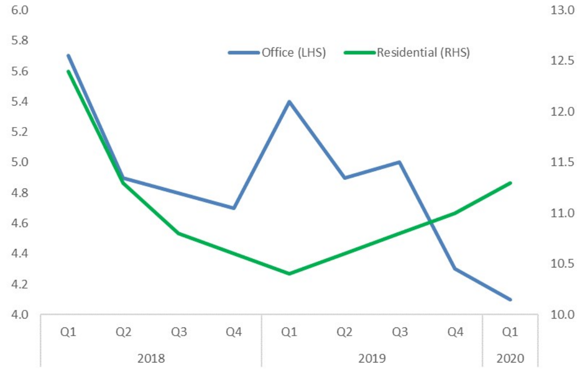
In terms of location, the office vacancy rates in Fort Bonifacio (3.4 percent from 3.7 percent), and Ortigas Center (4.1 percent from 5.0 percent) declined in Q1 2020 compared to Q4 2019. By contrast, office vacancy rates in Manila Bay Area (4.9 percent from 0.5 percent) and Makati CBD

[14] In terms of location, luxury residential units are located within the CBD core and have quality access to/from and have superior visibility from the main avenue. Meanwhile, in terms of general finish, luxury residential units have premium presentation and maintenance.
[15] This includes Makati CBD, Fort Bonifacion, Ortigas, Eastwood, and Rockwell.
[16] Actual rentals for housing account for 12.9 percent of the 2012-based CPI basket. The NSO presently surveys rentals only ranging from around ₱300-₱10,000/month to compute rent inflation. However, the rental values discussed in this section pertain to high-end rented properties, which may be considered as indicators of wealth and demand.

(1.7 percent from 1.6 percent) increased in Q1 2020 compared to the previous quarter.

Following the adverse impacts of the pandemic and the ECQ in Luzon, higher office vacancy rate is expected in 2020 due to slowdown in leasing activities. With the rise in vacancy and a greater leeway for rent negotiations and concessions, rent will decline in 2020 before recovering in 2021.

Chart 9. Vacancy Rates
In percent



Source: Colliers International Philippines

Meanwhile, the overall residential vacancy rate in Metro Manila rose to 11.3 percent in Q1 2020 from the quarter- and year-ago rates of 11.0 percent and 10.4 percent, respectively. The increase in vacancy rates is due to the completion of additional units across Metro Manila. In particular, residential vacancy rates were higher in areas such as Makati CBD (11.1 percent from 10.9 percent), Fort Bonifacio (15.2 percent from 15.0 percent), Rockwell Center (10.2 percent from 10.0 percent), Ortigas Center (4.6 percent from 4.4 percent), Eastwood City (4.4 percent from 4.3 percent), and Manila Bay area (13.2 percent from 12.8 percent).

A softening of demand, particularly in business districts dependent on Philippine Offshore Gaming Operators (POGOs), is anticipated for 2020. Nevertheless, market analysts see a rebound in 2021, especially if the virus is contained and market sentiment improves before the end of 2020.

BSP Residential Real Estate Price Index (RREPI).[17] Based on the RREPI measure, residential real estate prices of various types of housing units nationwide rose by 12.4 percent y-o-y in Q1 2020, higher than the 10.2-percent growth in the previous quarter and 3.3 percent a year ago. This is the third consecutive quarter that the index has registered a double-digit growth.

Residential real estate prices continue to rise

By area, residential property prices increased y-o-y in both the National Capital Region (NCR) and in Areas Outside NCR (AONCR). Residential property prices grew at a faster pace in NCR (18.3 percent) compared with those in AONCR (8.5 percent). The brisker growth of property prices in NCR can be attributed to the higher increase in the prices of condominium units which outweighed the decline in prices of single detached/attached houses, duplexes, and townhouses. Meanwhile, growth in prices were recorded in all types of housing units in AONCR albeit at a slower pace in townhouses and condominium units.

[17] The RREPI measures the average changes in prices of different types of housing units over a period of time across different geographical regions where the growth rate of the index measures house inflation. It is computed as a weighted chain-linked index based on the average appraised value per square meter weighted by the share of floor area of new housing units. The RREPI was computed based on data from housing loans granted by universal, commercial, and thrift banks.

Table 6. Residential Real Estate Price Index[1] by Housing Type

Q1 2014=100; growth rate in percent

	Overall[2]	Single Detached/ Attached House	Duplex[3]	Townhouse	Condominium Unit
2017 Q1	**113.9**	108.0	91.2	107.6	128.3
Q2	**111.8**	103.6	103.6	112.7	129.3
Q3	**111.6**	103.4	88.4	107.7	131.0
Q4	**117.4**	104.6	102.6	116.3	143.3
2018 Q1	**116.2**	107.3	131.5	122.4	130.9
Q2	**117.0**	105.1	99.0	128.4	138.5
Q3	**116.6**	103.6	115.5	127.7	138.6
Q4	**118.1**	102.6	98.8	129.9	144.2
2019 Q1	**120.0**	105.7	121.0	134.4	145.2
Q2	**117.5**	100.7	111.4	133.9	151.8
Q3	**128.7**	106.1	144.2	135.4	178.9
Q4	**130.2**	108.5	148.6	143.0	171.5
2020 Q1	**134.9**	113.1	167.3	141.8	179.5
		Year-on Year Growth Rates			
2017 Q1	**6.5**	9.2	-20.5	0.3	4.1
Q2	**0.1**	-2.1	5.1	3.2	4.4
Q3	**1.8**	0.8	-8.6	7.2	3.6
Q4	**5.7**	-0.3	17.3	8.0	14.2
2018 Q1	**2.0**	-0.6	44.2	13.8	2.0
Q2	**4.7**	1.4	-4.4	13.9	7.1
Q3	**4.5**	0.2	30.7	18.6	5.8
Q4	**0.6**	-1.9	-3.7	11.7	0.6
2019 Q1	**3.3**	-1.5	-8.0	9.8	10.9
Q2	**0.4**	-4.2	12.5	4.3	9.6
Q3	**10.4**	2.4	24.8	6.0	29.1
Q4	**10.2**	5.8	50.4	10.1	18.9
2020 Q1	**12.4**	7.0	38.3	5.5	23.6
		Quarter-on-Quarter Growth Rates			
2017 Q1	**2.5**	3.0	4.2	-0.1	2.2
Q2	**-1.8**	-4.1	13.6	4.7	0.8
Q3	**-0.2**	-0.2	-14.7	-4.4	1.3
Q4	**5.2**	1.2	16.1	8.0	9.4
2018 Q1	**-1.0**	2.6	28.2	5.2	-8.7
Q2	**0.7**	-2.1	-24.7	4.9	5.8
Q3	**-0.3**	-1.4	16.7	-0.5	0.1
Q4	**1.3**	-1.0	-14.5	1.7	4.0
2019 Q1	**1.6**	3.0	22.5	3.5	0.7
Q2	**-2.1**	-4.7	-7.9	-0.4	4.5
Q3	**9.5**	5.4	29.4	1.1	17.9
Q4	**1.2**	2.3	3.1	5.6	-4.1
2020 Q1	**3.6**	4.2	12.6	-0.8	4.7

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015
[2] No index generated for apartments due to very few observations
[3] Indices for duplex exhibit more volatility due to relatively small number of reported real estate loans
Source: Bangko Sentral ng Pilipinas (BSP)

In Q1 2020, the purchase of new housing units accounted for 74.4 percent of residential real estate loans (RRELs). More than half of residential property loans were used for the acquisition of condo units (53.8 percent), followed by single detached/attached houses (38.2 percent), and townhouses (7.6 percent).

By area, most of the RRELs granted in NCR were for the purchase of condominium units, while RRELs granted in AONCR were for the purchase of single detached houses. By region, NCR accounted for almost half (49.4 percent) of the total number of RRELs granted in Q1 2020, followed by CALABARZON (24.7 percent), Central Luzon (7.7 percent), Central Visayas (6.1 percent), Western Visayas (3.3 percent), Davao Region (2.9 percent) and Northern Mindanao (2.2 percent). NCR and these six other regions combined accounted for 96.3 percent of total housing loans granted by banks.

Table 7. Residential Real Estate Price Index[1] by Area

Q1 2014=100; growth rate in percent

	Overall[2]	NCR	AONCR
2017 Q1	**113.9**	118.4	111.6
Q2	**111.8**	120.4	107.5
Q3	**111.6**	118.2	108.1
Q4	**117.4**	127.6	111.1
2018 Q1	**116.2**	121.6	112.5
Q2	**117.0**	125.7	112.0
Q3	**116.6**	126.4	110.5
Q4	**118.1**	129.8	110.2
2019 Q1	**120.0**	132.5	113.1
Q2	**117.5**	132.2	110.8
Q3	**128.7**	154.4	115.9
Q4	**130.2**	149.3	119.2
2020 Q1	**134.9**	156.7	122.7
		Year-on-Year Growth Rates	
2017 Q1	**6.5**	4.4	8.0
Q2	**0.1**	3.7	-1.6
Q3	**1.8**	2.2	1.8
Q4	**5.7**	8.8	3.0
2018 Q1	**2.0**	2.7	0.8
Q2	**4.7**	4.4	4.2
Q3	**4.5**	6.9	2.2
Q4	**0.6**	1.7	-0.8
2019 Q1	**3.3**	9.0	0.5
Q2	**0.4**	5.2	-1.1
Q3	**10.4**	22.2	4.9
Q4	**10.2**	15.0	8.2
2020 Q1	**12.4**	18.3	8.5
		Quarter-on-Quarter Growth Rates	
2017 Q1	**2.5**	0.9	3.4
Q2	**-1.8**	1.7	-3.7
Q3	**-0.2**	-1.8	0.6
Q4	**5.2**	8.0	2.8
2018 Q1	**-1.0**	-4.7	1.3
Q2	**0.7**	3.4	-0.4
Q3	**-0.3**	0.6	-1.3
Q4	**1.3**	2.7	-0.3
2019 Q1	**1.6**	2.1	2.6
Q2	**-2.1**	-0.2	-2.0
Q3	**9.5**	16.8	4.6
Q4	**1.2**	-3.3	2.8
2020 Q1	**3.6**	5.0	2.9

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015
[2] No index generated for apartments due to very few observations
[3] Indices for duplex exhibit more volatility due to relatively small number of reported real estate loans
Source: Bangko Sentral ng Pilipinas (BSP)

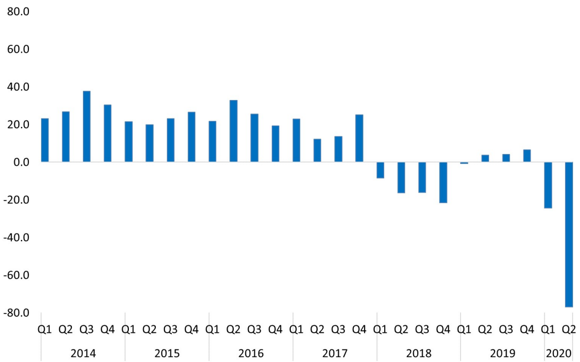
Vehicle Sales. Sales of new vehicles from CAMPI-TMA[18] members declined by 76.9 percent y-o-y in Q2 2020, a turnaround from the 3.7-percent expansion recorded in the same period in 2019. The decline in sales of passenger and commercial vehicles during the period could be attributed to closures of car dealerships, limited marketing strategies, and shift in consumer demand to essential goods following the implementation of ECQ.

[18] Vehicle sales data is gathered on a monthly basis by the Chamber of Automotive Manufacturers of the Philippines (CAMPI) and the Truck Manufacturers Association (TMA). CAMPI represents the local assemblers and manufacturers of vehicle units in the Philippine automotive industry. The following are the active members of CAMPI: (1) Asian Carmakers Corp., (2) CATS Motors, Inc., (3) Columbian Autocar Corp., (4) Honda Cars Philippines, Inc., (5) Isuzu Philippines Corp., (6) Mitsubishi Motors Philippines Corp., (7) Nissan Motor Philippines Corp., (8) Suzuki Philippines Inc., (9) Toyota Motor Philippines Corp. and (10) Universal Motors Corp.

New vehicle sales fall sharply

Commercial vehicle sales, which account for about 70.1 percent of total vehicle sales, went down by 77.0 percent y-o-y in Q2 2020 from the 6.9-percent increase in the same period in 2019. Commercial vehicles sold during the period reached 14,373 units from 62,501 units in the same period a year ago.

Chart 10. Vehicle Sales
Growth rate in percent



Source: CAMPI

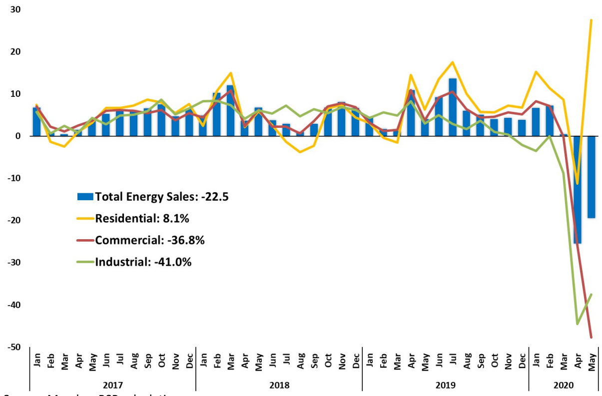
Similarly, passenger car sales decreased by 76.7 percent y-o-y in Q2 2020, a further decline from the 3.1-percent contraction in the same period in 2019. New passenger car sales accrued to a total of 6,126 units in Q2 2020 from 26,246 units in the same period a year ago.

Energy Sales. Energy sales of Meralco contracted by 22.5 percent y-o-y in Q2 2020, a reversal from the 7.5-percent growth in the same period a year ago. The contraction in Q2 2020 reflects the impact of the implementation of the ECQ/modified ECQ in its service area. Energy sales from the commercial sector and industrial sectors contracted by 36.8 percent and 41.0 percent, respectively. Meanwhile, albeit slower, energy sales in the residential sector expanded by 8.1 percent from 10.4 percent in Q2 2019.

Energy sales contract in Q2 2020

According to Meralco, energy consumption for the month of April were based on estimated consumption due to meter reading limitations during the implementation of the community quarantine in its service area.[19] Consumption based on actual meter reading will be reflected in succeeding data provisions once completed.

Chart 11. Energy Sales
Year-on-year growth in percent



Source: Meralco, BSP calculations

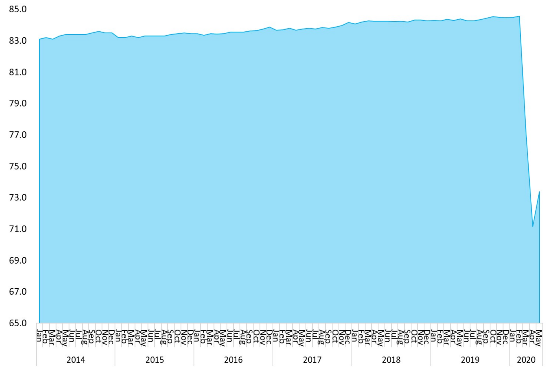
Capacity Utilization. The average capacity utilization rate of the manufacturing sector stood at 73.4 percent in May 2020, higher than the month-ago level at 71.2 percent (revised) based on the Philippine Statistics Authority's (PSA) Monthly Integrated Survey of Selected Industries (MISSI).

Utilization rate in May 2020 remain below optimal capacity

Of the 506 respondent-establishments, only 43.3 percent operated at a capacity of at least 80.0 percent in May 2020. The 506 respondents are significantly lower than the April level at 608 firms (revised), and only takes account for about 56.7 percent of the 893 sample establishments.

[19] Meralco stated that the estimation consumption is in line with the Energy Regulatory Commission's (ERC) Distribution Service Open Access Rules (DSOAR), which states that the estimated consumption is based on the average past three-months' consumption with available meter reading (e.g. December 2019 to February 2020 – which are considered "low consumption" months because of the cooler climate compared to March, April and May summer months).

Chart 12. Monthly Average of Capacity Utilization for Manufacturing
In percent



Source: PSA

With the extension of the ECQ in May, only five (out of the 20) major industries in the sector operated at least at the 80.0-percent capacity level that include: wood and wood products (91.7 percent), textiles (90.6 percent), footwear and wearing apparel (85.8 percent), rubber and plastic products (82.2 percent), and electrical machinery (81.4 percent). Meanwhile, eight major industries operated at the 70 to 79 percent capacity range namely, furniture and fixtures (78.7 percent), food manufacturing (76.6 percent), paper and paper products (76.4 percent), leather products (75 percent), transport equipment (74.4 percent), basic metals (73.6 percent), non-metallic mineral products (73.5 percent), and chemical products (72.8 percent).

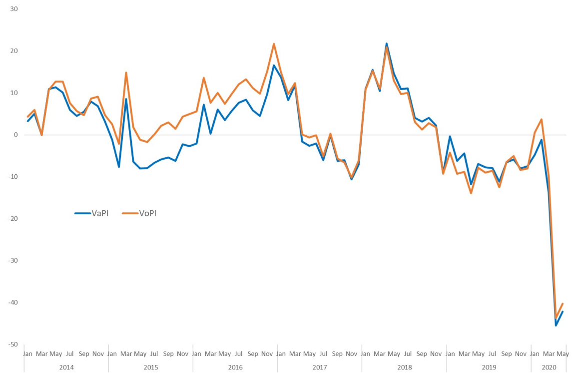
The enforcement of the ECQ from March to May resulted in business closures, logistical bottlenecks, subdued domestic demand, as well as supply disruptions. Nonetheless, the May 2020 survey suggests an improvement from month-ago levels which, according to NEDA, could be indicative that the sector is showing signs of recovery. A rebound is expected in the coming months as the Philippine economy gradually reopens following the easing of lockdown and quarantine measures beginning in the second half of May. Moreover, the government is set to provide particular support to firms in the areas of health, digital economy, digital education, and power.

Volume and Value of Production. Preliminary results of the MISSI showed that volume of production index (VoPI) declined by 40.3 percent y-o-y in May 2020, albeit an improvement from the 43.6-percent (revised) contraction in the previous month.

Manufacturing output continues to deteriorate

All 20 major industries posted negative growth rates: petroleum products (-91.4 percent), electrical machinery (-33.7 percent), machinery except electrical (-61.5 percent), food manufacturing (-29.1 percent), transport equipment (-79.3 percent), beverages (-56.2 percent), footwear and wearing apparel (-76.6 percent), basic metals (-43.6 percent), rubber and plastic products (-57.4 percent), tobacco products (-73.1 percent), miscellaneous manufactures (-52.3 percent), fabricated metal products (-61.4 percent), textiles (-43.7 percent), non-metallic mineral products (-27.2 percent), printing (-62.1 percent), paper and paper products (-32.4 percent), chemical products (-4.2 percent), furniture and fixtures (-26.7 percent), leather products (-32.6 percent), and wood and wood products (-8 percent).

Chart 13. Volume and Value Indices of Manufacturing Production
Year-on-year in percent



Source: PSA

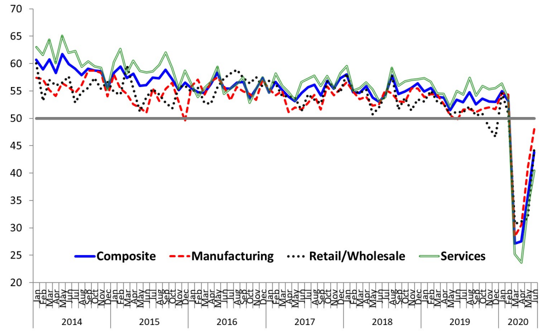
Similarly, the value of production index (VaPI) posted a 42.1-percent plunge in May 2020 from a 45.5-percent slump a month-ago. This was attributed to the deceleration of all 20 sub-sectors: petroleum products (-92.1 percent), electrical machinery (-37.8 percent), machinery except electrical (-62.3 percent), food manufacturing (-28.6 percent), transport equipment (-80.3 percent), beverages (-54.6 percent), footwear and wearing apparel (-78.7 percent), basic metals (-46.2 percent), rubber and plastic products (-58.4 percent), tobacco products (-71.9 percent), miscellaneous manufactures (-53 percent), fabricated metal products (-59.7 percent), non-metallic mineral products (-28.4 percent), textiles (-43.9 percent), printing (-61.4 percent), chemical products (-9.4 percent), paper and paper products (-34.7 percent), wood and wood products (-17.6 percent), leather products (-40.8 percent), and furniture and fixtures (-11 percent).

Purchasing Managers' Index.[20] The preliminary composite PMI in June 2020 remained below the 50-point expansion threshold[21] at 43.8 as all the industries in review continued to report contractions. However, the June PMI is a significant improvement from the May PMI at 35.6 as more businesses re-opened and operated at least at 50 percent capacity following the gradual easing of lockdown and quarantine measures in most parts of the country.

Composite PMI in June 2020 improves but still below expansion territory

The manufacturing PMI jumped by 7.0 index points to 48.1 in June 2020 from 41.1 in May, but still falls short of business managers' expectations that the sector will switch to expansion mode. Nonetheless, this is a huge improvement as it hovers near the 50-point threshold. The sector's better performance was a result of a more relaxed quarantine measures in June that enabled more firms to conduct business activities. This is evident in the faster expansion of the Production Index (at a PMI of 50.2) and Inventory Index (51.4), despite still subdued demand (New Orders Index at 46.8) and given limited manpower (Employment Index at 37.2). Delivery lead time continued to move at a slow pace – as seen in the expansion of the Supplier Deliveries Index – as travel restrictions remained in place. Meanwhile, respondent-firms expect the manufacturing sector to shift to expansion mode in July 2020.

Chart 14. Purchasing Managers' Index



Similarly, the services PMI increased by 6.7 index points to 40.5 in June from 33.7 in the previous month, which is consistent with respondents' expectations of a higher PMI. All the indices in review recorded slower contraction during the month, indicative that the services sector started to show recovery after being hard hit by the lockdown measures. In particular, Business Activity Index and New Orders Index – which are both measures of demand – rose by 7.6 index points and 9.0 index points, respectively. Survey respondents anticipate less favorable outcome for the sector in the month ahead.

The retail and wholesale PMI surged by 12.6 index points to 44.3 in June from 31.7 a month ago, consistent with managers' expectations of an uptick. All the indices posted higher PMIs, except for the Supplier Deliveries Index. In particular, the Purchases Index and Sales Revenues Index – which are both demand indicators – recorded the biggest increments of 29.2 index points and 17.9 index points, respectively. Inventory and Employment also improved with PMIs going beyond the 40-point mark. Meanwhile, the respondents anticipate an acceleration for the retail and wholesale sector in July.

[20] Data based on the monthly purchasing managers' index report of the Philippine Institute for Supply Management (PISM).

[21] The actual formula used to calculate the PMI assigns weights to each common element and then multiplies them by 1.0 for improvement, 0.5 for no change, and 0 for deterioration. As a result, an index above 50 indicates economic expansion, and an index below 50 implies a contraction. PMI surveys are conducted on the last week of the month.

External Demand[22]

Exports. Exports of goods decreased by 5.1 percent y-o-y in Q1 2020, a reversal from the 6.2-percent expansion in Q4 2019 and notably lower than the 2.0-percent contraction in Q1 2019.

Goods exports contract in Q1 2020

The lower outbound shipments of forest products, manufactures, and other agro-based products outstripped the growth in exports of coconut products, sugar products, fruits and vegetables, mineral products, and petroleum products.

Table 8. Exports of Goods
Growth rate in percent, year-on-year

By Commodity	2019		2020
Group	Q1	Q4	Q1
Coconut Products	-27.5	-21.2	1.5
Sugar Products	-54.2	78.3	10.3
Fruits and Vegetables	50.4	36.1	20.4
Other Agro-Based Products	0.4	-5.5	-7.9
Forest Products	51.5	21.6	-16.2
Mineral Products	12.1	26.7	5.6
Petroleum Products	-26.7	-26.6	13.6
Manufactures	-4.2	5.9	-6.7
Special Transactions	14.0	-17.3	-30.4
Total Exports	-2.0	6.2	-5.1

Source: BSP staff computations based on the Foreign Trade Statistics data of PSA

Imports. Imports of goods contracted further by 13.6 percent y-o-y in Q1 2020 from the 4.9-percent decline in Q4 2019 and a turnaround from the 7.6-percent growth in Q1 2019.

Merchandise imports records double-digit decline in Q1 2020

The contraction in inward shipments during the period was due largely to lower imports of capital goods, raw materials and intermediate goods, minerals and lubricant, and consumer goods.

Table 9. Imports of Goods
Growth rate in percent, year-on-year

By Commodity	2019		2020
Group	Q1	Q4	Q1
Capital Goods	14.2	2.6	-14.7
Raw Materials and Intermediate Goods	1.6	-13.5	-13.6
Mineral Fuels and Lubricant	-0.9	-11.7	-12.4
Consumer Goods	15.3	5.6	-12.1
Special Transactions	39.6	11.3	-12.5
Total Imports	7.6	-4.9	-13.6

Source: BSP staff computations based on the Foreign Trade Statistics data of PSA

Aggregate Supply

The services sector contributed 0.8 percentage point to total GDP growth. However, this was offset by the industry sector which reduced total GDP growth by almost a percentage point.

Contraction in the industry sector dampens supply-side activity

Growth in the services sector slowed down to 1.4 percent in Q1 2020 from 8.1 percent in Q4 2019. This was due primarily to the decline in transportation and storage, accommodation and food service activities, and other services as well as the deceleration in public administration and defense, compulsory social activities. Moreover, there was a slower growth in education, real estate and ownership of dwellings, professional and business services, and financial and insurance activities. Wholesale and retail trade slowed down, owing largely to the closure of shopping malls and non-essential establishments following the guidelines of the ECQ. Accommodation and food service activities declined as travel restrictions that started as early as 31 January 2020 and the ECQ effective mid-March halted tourism-related activities and services and forced hotel operators to shut down. Growth in other services also fell which could be attributed to the decline in arts, entertainment, and recreation and other service activities.

[22] International Merchandise Trade Statistics (IMTS) concept

Table 8. Gross Domestic Product by Industrial Origin

At constant 2018 prices; growth rate in percent

BY INDUSTRIAL ORIGIN	2019				2020
	Q1	Q2	Q3	Q4	Q1
Agriculture, forestry, and fishing	0.5	0.7	3.0	0.8	-0.4
Industry	4.9	2.5	5.4	6.0	-3.0
Mining & Quarrying	3.4	14.2	-3.5	-4.0	-22.3
Manufacturing	5.2	2.0	0.9	4.3	-3.6
Construction	5.0	-0.1	15.3	10.7	-1.8
Electricity, steam, water and waste managemen	3.4	8.1	7.3	7.3	5.3
Service	7.1	7.5	7.3	8.1	1.4
Wholesale and retail trade; repair of motor vehicles and motorcycles	7.0	8.6	8.3	8.5	1.1
Transportation and storage	6.8	6.1	7.9	4.7	-10.7
Accommodation and food service activities	6.0	4.9	6.0	7.8	-15.3
Information and communication	9.9	5.6	5.5	5.3	5.7
Financial and insurance activities	12.1	10.7	12.8	12.1	9.6
Real estate and ownership of dwellings	5.1	4.9	6.2	4.5	2.2
Professional and business services	1.1	3.0	2.7	2.2	0.7
Public administration and defense; compulsory social activities	11.7	11.4	8.7	21.3	5.2
Education	5.1	12.0	2.1	4.5	0.9
Human health and social work activities	3.0	-0.6	5.8	9.2	9.2
Other Services	6.7	6.6	5.2	7.3	-7.6

Source: PSA

The industry sector fell by 3.0 percent in Q1 2020, significantly lower than the 6.0-percent growth in Q4 2019. Nearly all manufacturing sub-sectors posted either lower or negative growth, including food products, coke and refined petroleum products, and beverages. Export-oriented manufactures also declined, such as electrical equipment, transport equipment, and machinery and equipment except electrical. Similarly, growth in the mining and quarrying sector fell further due to declines in stone quarrying and other mining quarrying and extraction of crude petroleum and natural gas. Meanwhile, construction slowed down from its double-digit growth in the previous quarter as government and private projects were temporarily halted by the ECQ.

The agriculture sector contracted by 0.4 percent in Q1 2020 from the 0.8-percent growth in Q4 2019. The decline in agricultural output was primarily on account of lower production of palay (-1.9 percent from -0.6 percent in Q4 2019) and fishing and aquaculture (-5.2 percent from 4.0 percent in Q4 2019). Poultry and egg and support activities to agriculture, forestry and fishing also recorded slower growth.

Labor Market Conditions

Major indicators for both quantity and quality of employment deteriorated in Q2 2020 from the year-ago conditions due to the impact of the COVID-19 pandemic. Results of the April 2020 Labor Force Survey showed that the country's employment rate dropped to 82.3 percent (from 94.9 percent a year ago), unemployment rate rose to 17.7 percent (from 5.1 percent), underemployment rate increased to 18.9 percent (from 13.4 percent), and youth unemployment rate rose sharply to 31.6 percent (from 12.9 percent).

Employment conditions deteriorate in Q2 2020

On a year-to-date basis, unemployment rate is at 11.5 percent while youth unemployment rate averaged at 22.6 percent. Prior to COVID-19, unemployment rate for 2020 was assessed to range between 3.8 and 5.2 percent and youth unemployment rate was seen at 9.2 percent.[23]

The employment rate in April 2020 was equivalent to 33.8 million employed individuals, 19.1 percent lower compared to 41.8 million employed persons in the same period a year ago. Employment losses were recorded in all sectors, particularly in services and industry. Employment in the services sector declined by 21.7 percent to 19.3 million, mainly due to wholesale and retail trade, transportation and storage, and accommodation and food service activities. Employment in the industry sector contracted by 28.9 percent, largely on account of construction and manufacturing subsectors. The latter is consistent with the latest result of the MISSI, which posted a 59.8-percent drop in the VOPI in April 2020. Employment in agriculture sector declined by 3.5 percent growth, which halted the improvement in agriculture employment starting Q3 2019.

[23] NEDA (2019), "Socio Economic Report 2018." There were no targets for overall employment rate and underemployment rate.

Unemployment registers double-digit rate

The double-digit unemployment rate of 17.7 percent translated to 7.3 million unemployed individuals, a 220.0-percent increase in from the previous year. In terms of highest grade completed, majority of the unemployed were junior high school graduates (30.3 percent) and college graduates (18.7 percent share). In terms of age, majority of unemployed were in the 25-34 year-old age group (31.6 percent), followed by the 15-24 year-old age group or the youth (28.2 percent). The number of unemployed youth increased by 105.0 percent during the period.
As some employers have reduced the number of work hours due to lower domestic demand, underemployment rate increased during the period. This overturned the declining trend in underemployment since October 2018. Other aspects of quality of employment also worsened during the period as evidenced by lower share of remunerative work or wage and salary workers (63.2 percent in April 2020 from 63.8 percent a year ago) and the substantial decline in overall mean hours of work (hours per week) from 41.8 in April 2019 to 35.0 in April 2020.

II. Monetary and Financial Market Conditions

Domestic Liquidity

Domestic liquidity (M3) grew by 16.6 percent y-o-y in May 2020 to ₱13.7 trillion, faster than the 13.3-percent expansion as of end-Q1 2020.

Domestic liquidity expands further

Money supply continued to increase due mainly to sustained demand for credit. Domestic claims rose by 16.2 percent in May from 11.9 percent as of end-Q1 2020 due to the sustained growth in credit to the private sector. Meanwhile, net claims on the central government increased by 59.6 percent in May, faster than the 21.6-percent growth as of end-Q1 2020, owing to the increase in domestic borrowings by the NG.

Chart 15. Domestic Liquidity
Year-on-year growth rates in percent

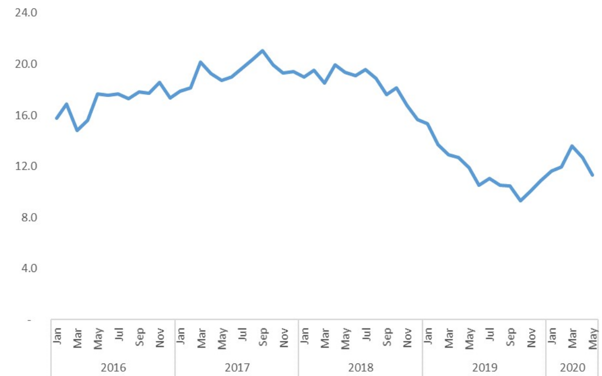
Net foreign assets (NFA) in peso terms grew by 12.1 percent y-o-y in May from a growth of 9.1 percent in end-Q1 2020. The BSP's NFA position improved in May, reflecting the increase in gross international reserves after the NG deposited with the BSP the proceeds of its foreign exchange borrowings. Meanwhile, the growth in the NFA of banks eased, as banks' foreign assets declined mainly on account of lower investments in marketable securities.

Outstanding loans of commercial banks, net of reverse repurchase (RRP) placements with the BSP, increased by 11.3 percent y-o-y in May 2020, slower than the 13.6-percent growth rate posted at end-Q1 2020. However, this was faster than the 10.5-percent growth recorded in end-Q2 2019.

Bank lending growth decelerates slightly

Loans for production activities increased by 9.8 percent y-o-y in May 2020 from 11.6 percent in end-Q1 2020 and 9.8 percent in end-Q2 2019. The expansion in production loans was driven primarily by increased lending to the following sectors: real estate activities; financial and insurance activities; electricity, gas, steam and air conditioning supply; information and communication; and transportation and storage.

Chart 16. Loans Outstanding of Commercial Banks
Year-on-year growth rates in percent



Meanwhile, loans for household consumption grew by 30.2 percent in May 2020, lower than the 36.5-percent growth in end-Q1 2020 but higher than the 15.3-percent expansion in end-Q2 2019.

Monetary Operations

As of end-Q2 2020, total outstanding amount absorbed in the BSP liquidity facilities stood at ₱1.5 trillion. Bulk of the BSP's liquidity-absorbing monetary operations had been through the overnight deposit facility (ODF), comprising about 73.3 percent of the total outstanding amount. Meanwhile, placements in the term deposit facility (TDF) and reverse repurchase agreement or RRP facility each made up 13.4 percent.

The BSP calibrated its monetary operations to ensure adequate short-term peso liquidity in the financial system and support the smooth flow of funding to businesses and households amid the implementation of quarantine protocols in response to the COVID-19 pandemic. There were no offerings in the TDF for 1 and 8 April 2020. In addition, beginning 8 April, the daily RRP volume offering was reduced to ₽100 billion (from ₽305 billion). The BSP gradually reopened the TDF by offering the 7-day and 14-day tenors on 15 April and 10 June, respectively, while the daily RRP offer volume was increased to ₽200 billion on 10 June.

The reduced TDF operations in Q2 2020 resulted in lower average weekly offer volume at about ₽131.5 billion for the period 15 April – 24 June relative to the previous quarter's ₽151.8 billion. Meanwhile, average bid-to-cover ratios for the 7-day and 14-day tenors were higher at 2.4 and 3.1 compared to 1.4 and 1.5, respectively, in the previous quarter. Similarly, the average bid-to-cover ratio for the daily RRP auction increased significantly to around 5.2 during the quarter from 1.7 in Q1 2020.

For the standing facilities, there were a few availments in the overnight lending facility (OLF) in the first half of April but at minimal amounts only. Meanwhile average daily placements in the ODF in Q2 2020 was at about ₽560.25 billion, higher than ₽226.56 billion in the previous quarter.

Credit Conditions

Credit Standards. Results of the Q2 2020 Senior Bank Loan Officers' Survey (SLOS)[24] showed that most of the respondent banks tightened their overall credit standards for loans to both enterprises and households during the quarter based on the modal approach.[25] This is the first time that the majority of respondent banks reported tighter credit standards following 44 consecutive quarters of broadly unchanged credit standards.

Consequently, the diffusion index (DI) approach,[26,27] likewise indicated a net tightening of overall credit standards for both loans to enterprises and households in Q2 2020. In the previous quarter, credit standards for business and consumer loans also showed a net tightening based on the DI approach.

Majority of respondent banks tighten overall credit standards

It should be noted that the Q2 2020 survey was conducted during the period when strict lockdown measures implemented in response to the COVID-19 pandemic were still in effect. This covers the ECQ period beginning 17 May - 30 April 2020, prior to the start of the gradual easing of quarantine measures in some areas by May 2020

Lending to Enterprises. Results based on both the modal and DI approaches pointed to tightening of credit standards for business loans, as most banks (69.4 percent of banks that responded to the question) reported tighter overall credit standards for loans to enterprises during the quarter. The overall tightening of credit standards was also noted across all borrower firm sizes, namely, top corporations, large middle-market enterprises, small and medium enterprises (SMEs), and micro-enterprises, as indicated by both modal- and DI-based results. Respondent banks attributed the tightening of credit standards largely to less favorable economic outlook, deterioration in the profiles of borrowers, and banks' reduced tolerance for risk, among other factors.

[24] The survey consists of questions on loan officers' perceptions relating to the overall credit standards of universal/commercial banks (U/KBs) and selected large thrift banks (TBs) in the Philippines, as well as to factors affecting the supply of and demand for loans by both enterprises and households. Survey questionnaires were sent to 64 U/KBs and TBs, of which, 40 banks responded to the current survey representing a response rate of 62.5 percent. The response rate for Q2 2020 SLOS is slightly higher compared to the previous survey round following the easing of lockdown measures and the transition to a general community quarantine in Metro Manila for the period 1 June to 15 July 2020 which is within the survey data collection period (1 June - 7 July 2020).
[25] In the modal approach, the results of the survey are analyzed by looking at the option with the highest share of responses.

[26] In the DI approach, a positive DI for credit standards indicates that the proportion of respondent banks that have tightened their credit standards exceeds those that eased ("net tightening"), whereas a negative DI for credit standards indicates that more respondent banks have eased their credit standards compared to those that tightened ("net easing").
[27] During the Q1 2010 to Q4 2012 survey rounds, the BSP used the diffusion index (DI) approach in the analysis of survey results. Beginning in Q1 2013, the BSP used both the modal and diffusion index (DI) approaches in assessing the results of the survey.

Table 9. General Credit Standards for Loans to Enterprises (Overall)

	2018		2019				2020	
	Q1	Q2	Q1	Q2	Q3	Q4	Q1	Q2
Tightened considerably	0.0	3.6	2.1	4.8	4.1	0.0	2.8	20.4
Tightened somewhat	3.7	10.7	22.9	11.9	12.2	15.2	30.6	**49.0**
Remained basically unchanged	**92.6**	**82.1**	**72.9**	**81.0**	**81.6**	**84.8**	**66.7**	24.5
Eased somewhat	3.7	3.6	0.0	0.0	0.0	0.0	0.0	6.1
Eased considerably	0.0	0.0	2.1	2.4	2.0	0.0	0.0	0.0
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Diffusion Index for Credit Standards	***0.0***	***10.7***	***22.9***	***14.3***	***14.3***	***15.2***	***33.3***	***63.3***
Weighted Diffusion Index for Credit Standards	***0.0***	***7.1***	***11.5***	***8.3***	***8.2***	***7.6***	***18.1***	***41.8***
Mean	*3.0*	*2.9*	*2.8*	*2.8*	*2.8*	*2.8*	*2.6*	*2.2*
Number of banks responding	***27.0***	***28.0***	***48.0***	***42.0***	***49.0***	***46.0***	***36.0***	***49.0***

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").

Looking at specific credit standards, the net tightening of overall credit standards was reflected in the reduced credit line sizes; stricter collateral requirements and loan covenants; and increased use of interest rate floors. Nonetheless, results also showed some net easing in terms of narrower loan margins (across all firm sizes) and longer loan maturities (particularly for loans to large-middle market enterprises, SMEs, and micro-enterprises).

Over the next quarter, the majority of the respondent banks expect to tighten overall credit standards on the back of more uncertain economic outlook, expected deterioration in borrowers' profiles as well as in the profitability and liquidity of banks' portfolios, and banks' lower tolerance for risk.

Lending to Households. Most of the respondent banks (60.6 percent) also reported a tightening of overall credit standards for loans extended to households during the quarter. Consequently, results based on the DI approach showed net tightening of credit standards for household loans. The net tightening of credit standards was also observed across all types of consumer loans, including housing, credit card, auto, and personal/salary loans.

Table 10. General Credit Standards for Loans to Households (Overall)

	2018		2019				2020	
	Q1	Q2	Q1	Q2	Q3	Q4	Q1	Q2
Tightened considerably	0.0	0.0	3.3	4.0	3.1	0.0	0.0	**39.4**
Tightened somewhat	15.8	5.9	16.7	8.0	6.3	6.9	21.7	21.2
Remained basically unchanged	**78.9**	**94.1**	**73.3**	**88.0**	**81.3**	**89.7**	**69.6**	33.3
Eased somewhat	5.3	0.0	3.3	0.0	9.4	3.4	8.7	6.1
Eased considerably	0.0	0.0	3.3	0.0	0.0	0.0	0.0	0.0
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Diffusion Index for Credit Standards	***10.5***	***5.9***	***13.3***	***12.0***	***0.0***	***3.4***	***13.0***	***54.5***
Weighted Diffusion Index for Credit Standard	***5.3***	***2.9***	***6.7***	***8.0***	***1.6***	***1.7***	***6.5***	***47.0***
Mean	*2.9*	*2.9*	*2.9*	*2.8*	*3.0*	*3.0*	*2.9*	*2.1*
Number of banks responding	***19.0***	***17.0***	***30.0***	***25.0***	***32.0***	***29.0***	***23.0***	***33.0***

Note: A positive diffusion index for credit standards indicates that more banks have tightened their credit standards compared to those that eased ("net tightening"), whereas a negative diffusion index for credit standards indicates that more banks have eased their credit standards compared to those that tightened ("net easing").

Respondent banks cited less favorable economic outlook, a reduced tolerance for risk, and the deterioration in borrowers' profile and profitability of banks' portfolios as major factors that contributed to the tightening of credit standards for loans to households. In terms of specific credit standards, the overall net tightening of credit standards for loans to households was manifested in reduced credit line sizes; stricter collateral requirements and loan covenants; and increased use of interest rate floors by respondent banks. However, some form of easing of credit standards was also noted in terms of narrower loan margins (across all types of loans to households) and longer loan maturities (specifically for housing, auto, and personal/salary loans).

In terms of respondent banks' outlook for the next quarter, results based on both the modal and DI approaches reflected expectations of net tighter overall credit standards for household loans, which respondent banks attributed to more uncertain prospects on the economy, banks' lower tolerance for risk, and anticipated deterioration in borrowers' profile and in the profitability of banks' portfolios.

Loan demand. Responses to the survey question on loan demand indicated that most respondent banks saw a decrease in overall demand for loans from both enterprises and households in Q2 2020. Accordingly, results based on the DI approach also showed a net decrease in overall demand[28] for both business and household loans. The overall net decrease in loan demand from firms was associated by respondent banks mainly to the deterioration in clients' business prospects amid the lockdown, decline in customer inventory financing needs and working capital requirements, attributed in turn to delay in investment plans in plant or equipment. Meanwhile, respondent banks cited lower household consumption and housing investment as major reasons for the overall net decrease in household loan demand for the quarter.

Over the next quarter, most of respondent banks expect an increase in demand for business loans (across all firm sizes) as well as for credit card and personal/salary loans, reflecting in part

[28] The "DI for loan demand" refers to the percentage difference between banks reporting an increase in loan demand and banks reporting a decrease. A positive DI for loan demand indicates that more banks reported an increase in loan demand compared to those stating the opposite, whereas a negative DI for loan demand implies that more banks reported a decrease in loan demand compared to those reporting an increase.

expectation for pick up in domestic economic activity following the partial re-opening of the economy. DI-based results likewise suggested expectations of a net increase in overall demand for business loans, associated largely with corporate clients' higher working capital requirements, lack of other sources of funds, decline in clients' internally-generated funds, and a rise in customer inventory financing needs.

Loan demand from firms and households declines

For loans extended to households, DI-based results indicated expectations of a net decline in demand for housing and auto loans while demand for credit card and personal/salary loans pointed to a net increase. Respondent banks cited lower housing investment and household consumption as major reasons for the anticipated net decrease in demand for housing and auto loans for the next quarter. Meanwhile, the expected net increase in demand for credit card and personal/salary loans was attributed by respondent banks largely to lack of other sources of funds and lower income prospects among other factors.

Real Estate Loans. Most of the respondent banks (55.6 percent) reported that overall credit standards for commercial real estate loans (CRELs) tightened in Q2 2020. Meanwhile, the DI approach continued to point to a net tightening of overall credit standards for CRELs for the 18th consecutive quarter. Respondent banks cited a less favorable economic prospects and a deterioration of borrowers' profiles as major factors for the tightening of overall credit standards for the said type of loan. In terms of specific credit standards, the net tightening of overall credit standards for commercial real estate loans reflected wider loan margins, reduced credit line sizes, stricter collateral requirements and loan covenants, increased use of interest rate floors, and shortened loan maturities. Over the next quarter, respondent banks anticipate tightening their credit standards for commercial real estate loans based on both the modal approach and DI-based results.

Majority of banks tighten credit standards for real estate loans

Most of the respondent banks reported unchanged demand for commercial real estate loans in Q2 2020, while DI-based results indicated a net decrease in loan demand. Over the next quarter, a higher number of respondent banks anticipated a generally steady loan demand in real estate loans. DI-based results, meanwhile, pointed to expectations of a net decrease in demand for CRELs due largely to anticipated deterioration in customers' economic outlook.

For housing loans extended to households, most of the respondent banks (60.0 percent) reported tightening their credit standards in Q2 2020. At the same time, the majority of the respondent banks expect overall credit standards for housing loans to tighten over the next quarter amid more uncertain economic prospects, deterioration in borrowers' profile, and lower risk tolerance of banks.

Results based on both the modal and DI approaches pointed to a decrease in demand for housing loans in Q2 2020, which was attributed by respondent banks largely to reduced housing investment and household consumption, restrained by the implementation of the community quarantine. Over the next quarter, more respondent banks continue to see lower demand for housing loans compared to those that anticipate a rise in loan demand for the said type of loan amid expectations of a decrease in housing investment as expenditure plans will be weighed down by repayment of postponed bills payable during the lockdown, as well as consumers' concerns over employment and income level.

Interest Rates

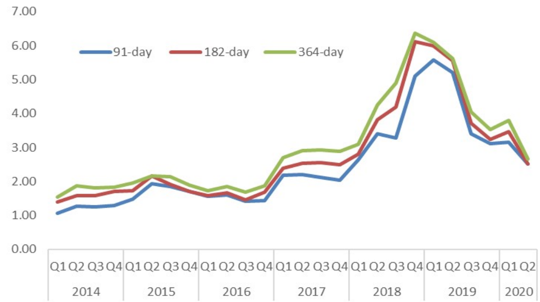
Primary Interest Rates. The average interest rates for the 91-, 182- and 364-day T-bills in the primary market in Q2 2020 went down to 2.516 percent, 2.523 percent, and 2.664 percent from 3.161 percent, 3.459 percent, and 3.793 percent, respectively, in the previous quarter. Similarly, the average interest rate for the issued 35-day T-bills showed a declining trend, which ranges from 1.684 percent to 2.714 percent.

Treasury bill rates are lower

The results of the auctions reflected ample liquidity in the financial system owing to BSP liquidity enhancing measures, as well as market players' strong demand for safe-haven government notes, especially for longer-tenored note (e.g., 1-year) amid cautious market sentiment towards the Philippine economic growth in 2020 brought about by the impact of the implementation of community quarantine in response to COVID-19 pandemic. At the same time, the decline in yields resulted from the cumulative 100-basis point reduction in policy rate of the BSP in April and June 2020.

Chart 17. Treasury Bill Rates

In percent



Source : Bureau of the Treasury

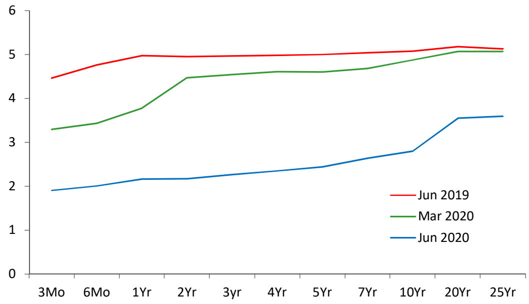
Yield Curve.[29] As of end-June 2020, the secondary market yield for government securities (GS) for all maturities declined relative to the end-March 2020 levels, as market players invested their excess liquidity and serviced their clients' requirements in anticipation of the additional liquidity from the BSP's liquidity enhancing measures.

GS yields decline in Q2 2020

Debt paper yields were lower by a range of 138.7 bps for the 3-month GS to 230.0 bps for the 2-year GS compared to end-March 2020 levels.

Chart 18. Yields of Government Securities in the Secondary Market

In percent



Source: Bloomberg

Relative to year-ago levels, the secondary market yields for GS for all maturities likewise decreased by a range of 153.6 bps (for the 25-year GS) to 280.8 bps (for the 1-year GS).

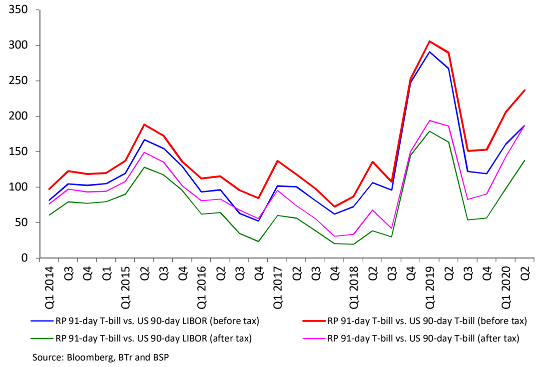
Interest Rate Differentials. The average differentials between domestic and US interest rates, gross and net of tax, widened further in Q2 2020 relative to the previous quarter.

Interest rate differentials widen further in Q2 2020

The average 91-day RP T-bill rate declined q-o-q by 66.5 bps to 2.427 percent in Q2 2020 from 3.137 percent in Q1 2020. Likewise, the average US 90-day LIBOR and the US 90-day T-bill rate declined by 93.2 bps and 97.7 bps, respectively, to 0.602 percent and 0.107 percent in Q2 2020. These developments led generally to wider positive gross and net of tax differentials between the 91-day RP T-bill rate and US interest rates. Domestic and foreign interest rates fell following market uncertainties from the COVID-19 pandemic outbreak and the reduction in the BSP's policy rate during the quarter.

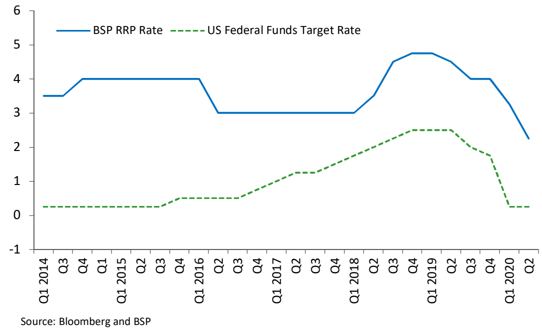
[29] On 29 October 2018, the Bankers Association of the Philippines (BAP) replaced the PDST Reference Rates and launched the PHP BVAL Reference Rates which will be used as the Philippine Peso GS benchmark. The PHP BVAL Reference Rates are calculated by Bloomberg Finance Singapore L.P. and/or its affiliates in an agreement with the BAP.

Chart 19. Interest Rate Differentials
Quarterly averages; in basis points



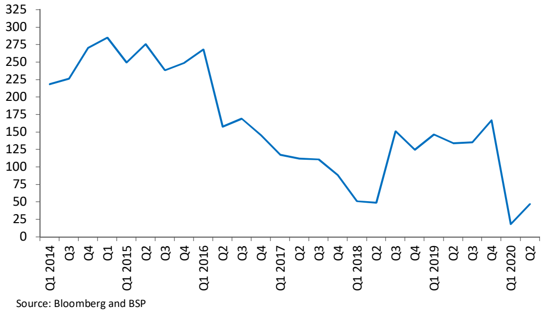
The positive differential between the BSP's overnight borrowing or RRP rate and the US Fed funds target rate narrowed to a range of 200-225 bps in Q2 2020 from 300-325 bps in Q1 2020, reflecting the impact of the 100-bp cumulative decrease in the BSP's overnight RRP rate to 2.75 percent on 17 April 2020 and 2.25 percent on 26 June 2020.

Chart 20. BSP RRP Rate and US Federal Funds Target Rate
In percent



Meanwhile, the interest rate differential between the BSP's overnight RRP rate and the US Fed funds target rate adjusted for risk[30] widened to 47 bps as of end-June 2020 from 18 bps in end-March 2020.

Chart 21. Risk-Adjusted Differentials
In basis points



This development could be traced to the 129-bp decrease in the country risk premium following the 131-bp and 3-bp decreases in the 10-year ROP note and 10-year US note, respectively, and 100-bp decrease in the interest rate differential between the BSP's overnight RRP rate and the US federal funds rate.

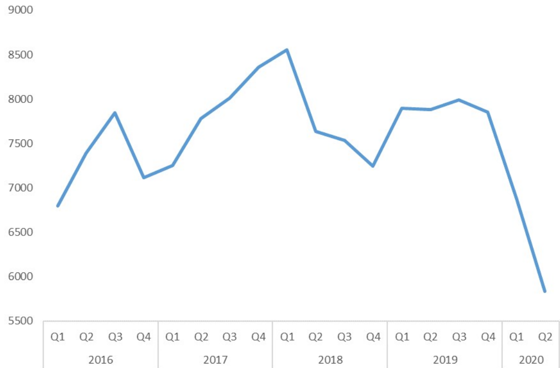
Financial Market Conditions

The decisive policy actions of the BSP during the review quarter to ease monetary conditions and enhance financial liquidity restored the calm and confidence of investors in the domestic market. Demand for government securities rose while the peso generally appreciated. Moreover, the banking system remained stable and continued to provide intermediation services during the ECQ period.

Stock Market. In Q2 2020, the Philippine Stock Exchange index (PSEi) declined by 15.2 percent q-o-q to average 5,832.17 index points. Trading in the equities market remained relatively volatile due to expectations of the negative impact of the COVID-19 pandemic on the economy. The BSP's decision to provide liquidity to stimulate economic activity and the gradual easing of the government's quarantine measures in some parts of the country improved investor sentiment. Subsequently, the main index closed at 6,207.72 index points in end-June, about 16.7 percent higher relative to the closing index in end-March of 5,321.23 index points.

[30] The difference between the 10-year ROP note and the 10-year US Treasury note is used as proxy for the risk premium.

Chart 22. Quarterly Average PSEi
In index points



Source: Bloomberg

During the review period, the following factors negatively affected trading in the Philippine stock market: expectations of economic losses following the extension of the ECQ in most parts of Luzon; contraction in manufacturing PMI data (in April and May); decline in Q1 2020 GDP growth; the IMF's negative outlook for the Philippine economy;[31] and the BSP's announcement that remittances from overseas Filipino workers may drop 5 percent in 2020. Moreover, external developments such as the sharp drop in oil prices;[32] lingering trade tensions between the US and China; renewed conflict between China and India;[33] the US Fed's negative assessment of US economic prospects;[34] and concerns over a 'second wave' of COVID-19 infections across the globe[35] also weighed on the main index.

The negative performance of the PSE was tempered by the following: the BSP's decision to inject liquidity into the economy through cuts in policy rates and reduction in banks' reserve requirement ratio (RRR) to spur economic activity; the easing of domestic inflation; the Philippine government's openness to public-private partnerships (PPP) in infrastructure projects and it's implementation of fiscal stimulus packages; the easing of quarantine measures starting June that allowed some businesses to reopen;[36] news of potential COVID-19 vaccines; and Merry Mart Consumer Corporation's successful initial public offering (IPO). In addition, relaxing lockdown measures abroad (e.g., US, France, Germany, Italy, Spain, Austria, Denmark) and the US Fed's announcement of plans to begin its corporate bond-buying program[37] lifted trading in the local stock market.

Mirroring the gradual uptick in the benchmark index, total capitalization in the Philippine stock market went up from ₱4 trillion in end-March 2020 to reach ₱13.16 trillion on 26 June. The price-earnings (P/E) ratio of listed firms similarly improved from 12.6x in end-March to reach 14.7x in end-June. In contrast, foreign investors continued to withdraw from the domestic stock market as they posted net sales of ₱36.6 billion in Q2 2020 from a ₱32.3-billion net sales in the preceding quarter.

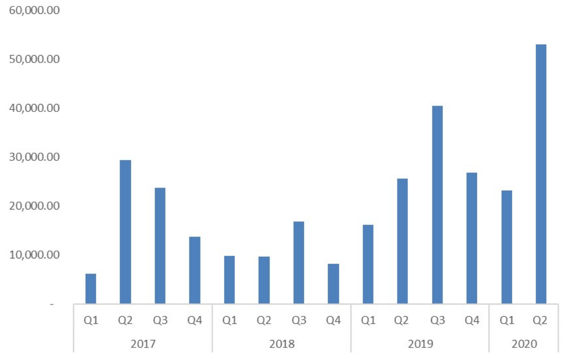
Government Securities. Results of the T-bill auctions conducted in April – June 2020 show increased market players' preference for government securities with total subscription for the quarter amounting to around ₱1.4 trillion or about 3.9 times the ₱350.0-billion aggregate offered amount. The oversubscription for Q2 2020, at ₱1.0 trillion, was significantly higher than the ₱324.8-billion oversubscription in the previous quarter.

Demand for Treasury bills surges

[31] The IMF projected that the Philippine economy will contract by 3.6 percent from April's forecast of a 0.6-percent growth. The figure is lower than the World Bank's 1.9-percent contraction estimate and the government's estimate of 2-3.4 percent decline.
[32] Global crude oil prices were dragged down by a supply glut and sagging demand for crude due to the coronavirus pandemic.
[33] On 15 June, tension between India and China escalated following the violent clash between Indian and Chinese troops in a border where India claims about 15,000 square miles of Chinese-controlled territory.
[34] The US Federal Reserve projected a 6.5 percent decline in the GDP of the US this year.
[35] On 29 June, data from the Johns Hopkins Coronavirus Resource Center showed that about 10.15 million COVID-19 cases have been recorded across the world. The United States and Brazil are leading other nations in the number of cases with 2.55 million and 1.34 million cases, respectively.
[36] On 28 May, President Duterte announced that Metro Manila and nearby cities would be placed under a general community quarantine (GCQ) starting June 1, to gradually reopen the economy after more than two months of strict quarantine measures that halted economic activity. Meanwhile, the rest of the country was placed under modified general quarantine at the same time.
[37] The Federal Reserve announced on 15 June that it will start buying up to $250 billion corporate bonds through the secondary market corporate credit facility to assist small and medium-sized businesses survive the COVID-19 pandemic.

The Bureau of the Treasury (BTr) awarded in full the ₱5.0-billion, ₱5.0-billion and ₱10.0-billion offered amounts for the 91-, 182- and 364-day T-bills, respectively, in all auctions.[38] Moreover, during all T-bill auctions (excluding on 6, 13 April and 15, 22 June) in Q2 2020, the BTr increased the total volume of T-bills it awarded on the back of lower rates and strong market demand for government securities. Likewise, for the 35-day T-bills, the BTr awarded in full the ₱15.0-offered amount in all auctions. Results of the T-bond auctions during the quarter showed strong demand for T-bonds.

Chart 23. Total Oversubscription of T-bill Auctions
In billion pesos



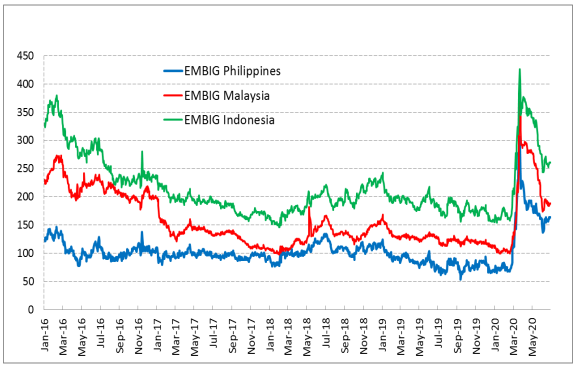
Source : Bureau of the Treasury

Sovereign Bond and Credit Default Swap (CDS) Spreads. In April and May, debt spreads narrowed as policy measures and regulatory relief measures were implemented to mitigate the adverse impact of COVID-related risks on the economy and the financial markets.

Debt spreads narrow on optimism over response to pandemic

In June, debt spreads continued to narrow over the government's decision to lift the modified enhanced community quarantine in major parts of the country. The lifting of the quarantine allowed businesses to resume operations.

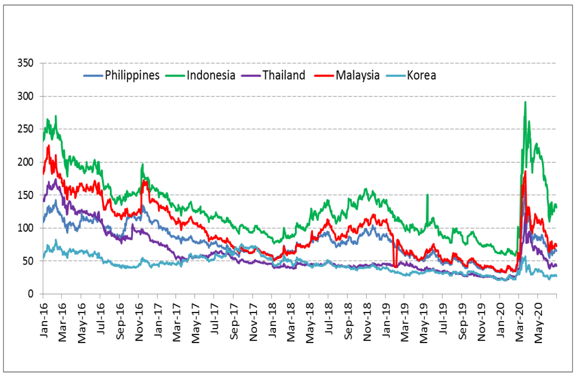
Chart 24. EMBIG Spreads of Selected ASEAN Countries
In basis points



Source: Bloomberg

As of 30 June 2020, the extra yield investors demanded to own Philippine sovereign debt over U.S. Treasuries or the Emerging Market Bond Index Global (EMBIG) Philippines spread stood at 164 basis points (bps) from the end-March level of 222 bps. Similarly, the country's 5-year sovereign credit default swap (CDS) decreased to 65 bps from its end-March level of 110 bps. Against other neighboring economies, the Philippine CDS traded narrower than Malaysia's 72 bps and Indonesia's 131 bps but wider than Thailand's 43 bps and Korea's 27 bps spreads.

Chart 25. Five-Year CDS Spreads of Selected ASEAN Countries
In basis points



Source: Bloomberg

[38] On 6 and 13 April T-bill auctions, offered amounts for the 91-, 182- and 364-day T-bills were ₱10 billion, ₱5 billion and ₱5 billion, respectively.

Banking System

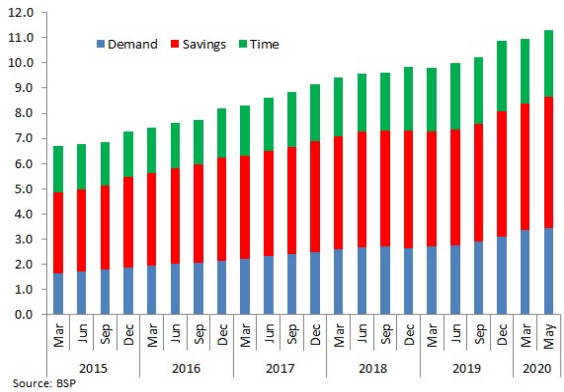
The Philippine banking system showed resilience and stability even as the country's economic activities and financial transactions were severely limited by the disruption caused by the pandemic and quarantine measures in Q2 2020.

Banking system exhibits asset and deposit growth

During the review period, banks' balance sheets sustained annual growth in assets and deposits. At the same time, asset quality remained steady while capital adequacy ratios stayed above international standards.[39] Banks maintained dominance in the financial sector, with U/KBs accounting for about 92 percent of total banks' resources. In terms of the number of head offices and branches/agencies, non-bank financial intermediaries have the widest physical network, consisting mainly of pawnshops.

Savings Mobilization. Savings deposits remained the primary sources of funds for the banking system. Banks' total deposits as of end-May 2020 amounted to ₱11.3 trillion, 3.2 percent and 14.2 percent higher than the quarter- and year-ago levels.[40]

Chart 26. Deposit Liabilities of Banks
In billion pesos



Source: BSP

Meanwhile, foreign currency deposits owned by residents (FCD-Residents) reached ₱2.1 trillion as of end-May 2020, posting a y-o-y growth of 4.1 percent. With respect to the end-March 2020 level, FCD-Residents decreased marginally by 0.5 percent.[41]

Institutional Developments. The total resources of the banking system grew by 9.7 percent to reach ₱19.1 trillion as of end-May 2020 from ₱17.5 trillion a year ago. Relative to the end-March 2020 level, total resources of the banking system likewise increased by 1.9 percent. As a percent of GDP, total resources stood at 97.8 percent.[42]

Total resources of the banking system continue to grow

[39] Beginning 1 July 2018, covered institutions (universal banks [UBs], commercial banks [KBs] and their subsidiary banks and quasi-banks [QBs]) must maintain a leverage ratio of no lower than five (5) percent. The leverage ratio is a non-risk based measure, which serves as a backstop to the Capital Adequacy Ratio. It is designed to constrain the potential build-up of leverage in the banking industry and to promote stability of the financial system. Also, the BSP sets an observation period of six months (from 1 July 2018 to 31 December 2018) for the Net Stable Funding Ratio (NSFR). This is to ensure a smooth transition to the new prudential standard and to allow prompt assessment and calibration of the components of the NSFR. Beginning 1 January 2019, however, the covered institutions (U/KBs) shall maintain an NSFR of 100.0 percent on both solo and consolidated bases.

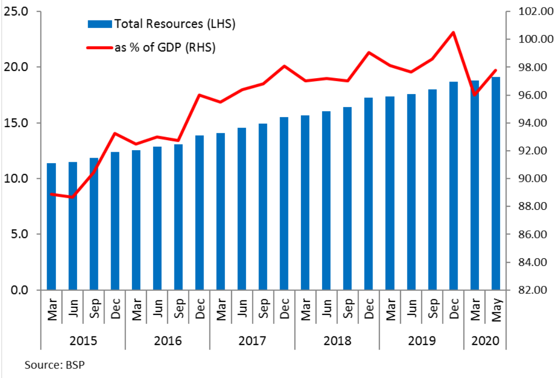
[40] This refers to the total peso-denominated deposits of the banking system.

[41] FCD-Residents, along with M3, forms part of a money supply measure called M4. Meanwhile, M3 consists of savings deposits, time deposits, demand deposits, currency in circulation, and deposit substitutes.

[42] GDP as of end-March 2020.

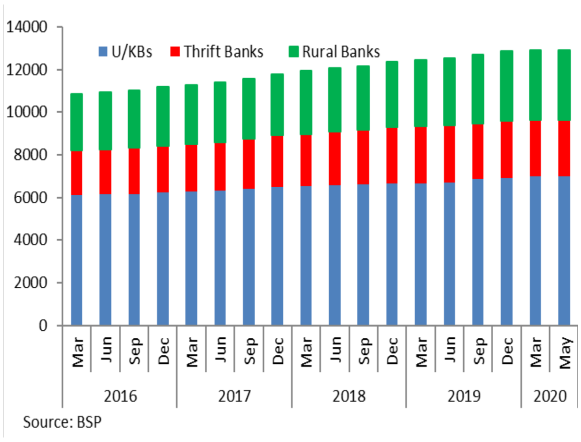
Chart 27. Total Resources of the Banking System

Levels in billion pesos; share in percent



The number of banking institutions (head offices) as of end-May 2020 decreased slightly to 541 offices from 542 in end-March 2020. The banks' head offices are comprised of 46 U/KBs, 48 TBs, and 447 rural banks (RBs). During the same period, the operating network (head offices and branches/agencies) of the banking system declined marginally to 12,890 offices from 12,892 offices in end-March 2020.

Chart 28. Number of Banking Institutions



In terms of asset quality, the Philippine banking system's gross non-performing loans (GNPL) ratio grew marginally to 2.4 percent as of end-May 2020 relative to the 2.2 percent posted in end-May 2019 and end-March 2020.

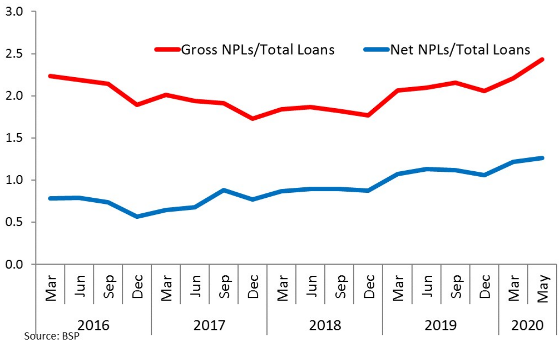
Asset quality of Philippine banks remains healthy

Nevertheless, even with the ongoing pandemic, the GNPL ratio remained below its pre-Asian crisis level of 3.5 percent on the back of banks' initiatives to improve their asset quality along with timely and prudent lending regulations.[43,44]

Similarly, the net non-performing loans (NNPL) ratio increased to 1.3 percent as of end-May 2020 relative to the 1.2 percent posted a year- and a quarter- ago.

Chart 29. Ratios of Gross Non-Performing Loans and Net Non-Performing Loans to Total Loans

In percent



Compared with regional counterparts, the Philippine banking system's GNPL ratio of 2.4 percent was higher with respect to those of Malaysia (1.0 percent) and South Korea (0.8 percent) but was lower than those of Indonesia (2.6 percent) and Thailand (3.0 percent).[45]

Loan exposures of banks remained adequately covered with the banking system's NPL coverage ratio at 96.5 percent as of end-May 2020. This was higher than the previous year's and quarter's ratios of 91.4 percent.

[43] The regulatory relief package include the following, among others: (1) exclude exposure of affected borrowers from the computation of the past due loan ratios; waiver of BSP documentary requirements for restructured loans, and (2) allow staggered booking of allowance for credit losses for loans extended to affected borrowers for a maximum period of five (5) years, subject to approval of the BSP (per BSP Memorandum No. M-2020-008).

[44] The 3.5 percent NPL ratio was based on the pre-2013 definition.

[45] Sources: Malaysia (Banking System's Ratio of net impaired loans to net total loans, April 2020); South Korea (Domestic Banks' Substandard or Below Loans [SBLs] ratio, March 2020); Indonesia (Commercial Banks' Nonperforming Loans to Gross Loans Ratio, March 2020); and Thailand (Total Commercial Banks' Gross NPLs ratio, December 2019).

U/KBs' CAR remains well above international and regulatory standards

The capital adequacy ratio (CAR) of U/KBs at end-December 2019, on solo basis, decreased marginally to 15.4 percent from 15.6 percent as of end-September 2019. Meanwhile, on a consolidated basis, CAR of U/KBs remained unchanged at 16.0 percent relative to the previous quarter. These figures remained well above the BSP's regulatory threshold of 10.0 percent and international standard of 8.0 percent.

Chart 30. Capital Adequacy Ratio of Universal and Commercial Banks
In percent

The CAR of Philippine U/KBs, on consolidated basis, was higher than that of South Korea (14.7 percent) but lower than those of Malaysia (18.0 percent), Thailand (19.2 percent) and Indonesia (21.6 percent).[46]

Exchange Rate

The peso averaged ₱50.45/US$1 in Q2 2020, appreciating by 0.75 percent from the Q1 2020 average of ₱51.83/US$1.

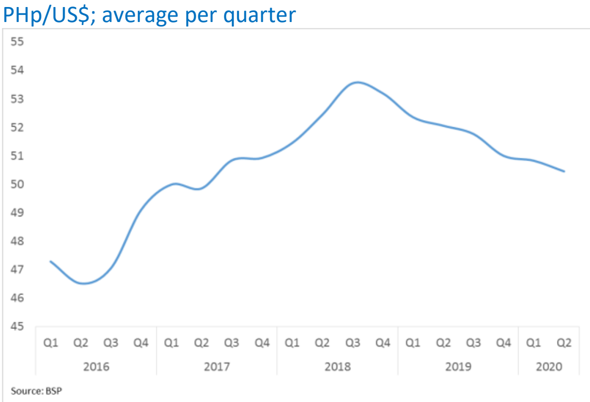
Peso appreciates on US Fed rate cut expectations

The country's macroeconomic fundamentals, which include the manageable inflation environment, a strong and resilient banking system, prudent fiscal position, and a high level of international reserve buffer continued to provide support to the peso. On a y-o-y basis, the peso likewise appreciated by 3.20 percent relative to the ₱52.07/US$1 average in Q2 2019.[47]

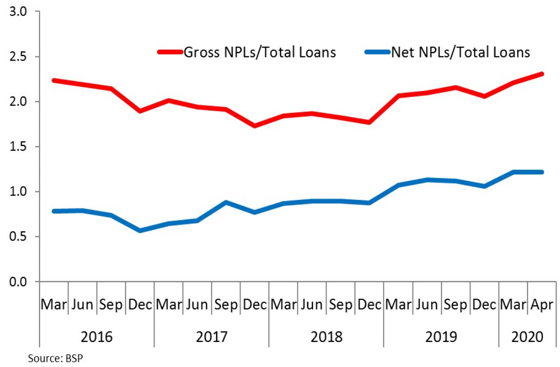
[46] Sources: South Korea (Domestic Banks' Total Capital Ratio, March 2020); Malaysia (Banking System's Total Capital Ratio, April 2020); Thailand (Commercial Banks' Capital Funds Percentage of Risk Assets, April 2020); and Indonesia (Commercial Banks' Regulatory Capital to Risk-Weighted Assets Ratio, March 2020).

[47] Dollar rates (per peso) or the reciprocal of the peso-dollar rates were used to compute for the percentage change.

Chart 31. Quarterly Peso-Dollar Rate
PHp/US$; average per quarter



In April, the peso appreciated to an average of ₱50.73/US$1, 0.33 percent higher than the ₱50.90/US$1 average in March. The peso appreciated on market optimism amid the government's cash aid for low income households;



the perceived slowdown in the number of infections in some virus hotspot countries; and the slower domestic inflation in March 2020. The BSP's moves to ensure sufficient liquidity in the system, such as lowering the minimum liquidity ratio (MLR) requirement of standalone thrift, rural and cooperative banks to 16 percent from 20 percent, likewise provided support to the peso.

The appreciation of the peso continued in May to an average of ₱50.56/US$1, 0.35 percent higher than the average during the previous month. The peso appreciated following the further easing of lockdown measures in some regions in the country (including the National Capital Region) to slowly reopen the economy; and improved prospects of a vaccine against COVID-19. In addition, S&P Global Ratings' affirmation of the country's sovereign credit rating as well as the slower domestic inflation in April 2020 have provided support to the peso.

In June, the peso averaged ₱50.13/US$1 appreciating by 0.85 percent from the average in

May. The appreciation of the peso reflected positive market sentiment due to: (i) narrower domestic trade deficit data in April 2020; (ii) slower domestic inflation and the country's record-high dollar reserves in May 2020; and (iii) the policy rate cut by the BSP on 25 June 2020 to further support economic recovery.

On a y-t-d basis, the peso appreciated against the US dollar by 1.62 percent to close at ₱49.83/US$1 on 30 June 2020 from the end-December 2019 closing rate of ₱50.64/US$1.[48]

Meanwhile, the volatility of the peso's daily closing rates (as measured by the coefficient of variation) stood at 0.17 percent in Q2 2020, lower than the 0.43 percent registered in the previous quarter.[49] The volatility of the peso in the review quarter was also lower than the volatility of most currencies in the region.

On a real trade-weighted basis, the peso lost external price competitiveness in Q2 2020 against the basket of currencies of all trading partners (TPI) and trading partners in developing (TPI-D) countries relative to Q1 2020. This was indicated by the increase in the real effective exchange rate (REER) index of the peso by 2.08 percent and 3.84 percent, against the TPI and TPI-D baskets, respectively. Meanwhile, against the basket of currencies of trading partners in advanced (TPI-A) countries, the REER index of the peso decreased slightly by 0.99 percent.

Relative to Q2 2019, the peso lost external price competitiveness across currency baskets during the review period. This developed following the nominal appreciation of the peso and the widening of inflation differentials, resulting in the increase in the REER index of the peso by 6.54 percent, 5.21 percent and 7.29 percent against the TPI, TPI-A and TPI-D baskets, respectively. [50,51]

[48] Based on the last done deal transaction in the afternoon.
[49] The coefficient of variation is computed as the standard deviation of the daily closing exchange rate divided by the average exchange rates for the period.

[50] The TPI measures the nominal and real effective exchange rates of the peso across the currencies of 14 major trading partners (MTP:s) of the Philippines, which includes US, Euro Area, Japan, Australia, China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand. The TPI-A measures the effective exchange rates of the peso across currencies of trading partners in advanced countries comprising of the US, Japan, Euro Area, and Australia. The TPI-D measures the effective exchange rates of the peso across 10 currencies of partner developing countries which includes China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.
[51] The REER index represents the Nominal Effective Exchange Rate (NEER) index of the peso, adjusted for inflation rate differentials with the countries whose currencies comprise the NEER index basket. A decrease in the REER index indicates some gain in the external price competitiveness of the peso, while a significant increase indicates the opposite. The NEER index, meanwhile, represents the weighted average exchange rate of the peso vis-à-vis a basket of foreign currencies.

III. Fiscal Developments

The NG recorded ₱562.2 billion fiscal deficit for January - May 2020, much higher than the previous year's budget gap.

NG records higher fiscal deficit

Netting out the interest payments in NG expenditures, the primary deficit for January – May 2020 amounted to ₱402.1 billion, a turnaround from the primary surplus recorded in the same period in 2019.

Table 11. National Government Fiscal Performance

In billion pesos

	2019		2020		Growth Rate (in percent)	
	May	Jan-May	May	Jan-May	May	Jan-May
Surplus/(Deficit)	2.6	-0.8	-202.1	-562.2	-7,983.6	69,390.2
Revenues	317.2	1,313.7	151.5	1,102.3	-52.3	-16.1
Expenditures	314.7	1,314.5	353.6	1,664.5	12.4	26.6

*Totals may not add up due to rounding
Source : Bureau of the Treasury (BTr)

Revenues decreased by 16.1 percent to ₱1,102.3 billion in January-May 2020 compared to ₱1,313.7 billion in the same period last year. The Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) contributed ₱673.7 billion and ₱210.5 billion, respectively. Revenue collections by the BIR and BOC were lower by 25.8 percent and 16.4 percent, respectively. Both decline in the agencies' revenue collection was attributed to the economic restrictions brought about by the COVID-19 pandemic. Meanwhile, the Bureau of the Treasury (BTr) recorded an income of ₱171.9 billion, more than twice the amount recorded last year on account of higher dividends.

Expenditures for the period in review amounted to ₱1,664.5 billion, 26.6 percent higher than the expenditures in January – May 2019. Excluding interest payments, expenditures went up by 29.3 percent to ₱1,504.4 billion. Meanwhile, interest payment was 6.1-percent higher compared to its year-ago level, reaching ₱160.1 billion in January – May 2020.

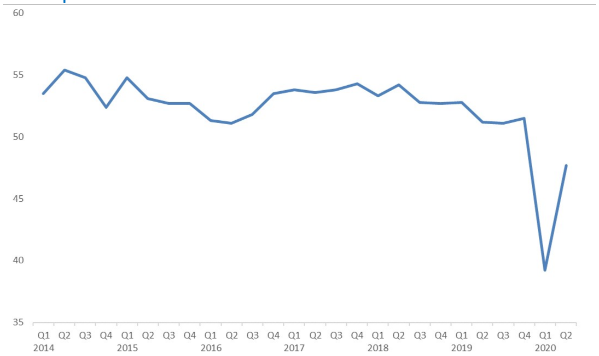
IV. External Developments

The JP Morgan Global All-Industry Output Index remained in contraction territory at 47.7 in June from 36.3 in May as new business volumes contracted for the fifth successive month.

Global economic output contracts at a slower rate

China, Australia, and France registered expansions, while the other countries for which composite output PMI data are calculated all saw their respective rates of contraction slow sharply relative to May.[52]

Chart 32. JP Morgan Global All-Industry Output Index
Index points



Source: Markit Economics

US. On a seasonally adjusted q-o-q basis, real GDP contracted by 5.0 percent in Q1 2020 from a 2.1-percent growth in Q4 2019. On a y-o-y basis, real output grew by 0.3 percent in Q1 2020 from the 2.3-percent expansion in the previous quarter.

US manufacturing activity improves

The decrease in real GDP in Q1 2020 reflected negative contributions from personal consumption expenditures, private inventory investment, exports, and nonresidential fixed investment. These movements were partly offset by positive contributions from residential fixed investment, federal government spending, and state and local government spending.[53]

Meanwhile, the US manufacturing PMI rose to 52.6 percent in June from 43.1 percent in May due to an increase in new orders amid improving demand conditions.[54]

The unemployment rate decreased to 11.1 percent in June from 13.3 percent in May, reflecting the continued resumption of economic activity that had been curtailed in March and April due to the COVID-19 pandemic and efforts to contain it. Total nonfarm payroll employment rose by 4.8 million during the month, with employment gains in leisure and hospitality, education and health services, other services, manufacturing, professional and business services, and retail trade. Meanwhile, on a y-o-y basis, inflation rose to 0.6 percent in June following a 0.1-percent decline in May due to higher food inflation.

The Conference Board Consumer Confidence Index increased to 98.1 in June from 85.9 in May,[55] while the Thomson-Reuters/University of Michigan Index of Consumer Sentiment rose to 78.1 in June from 72.3 in May.[56] Consumers' assessment of current business and labor market conditions was more positive following the re-opening of the US economy and the relative improvement in unemployment claims.

Euro Area. On a q-o-q basis, real GDP in the euro area decreased by 3.6 percent in Q1 2020 following a 0.1-percent expansion in Q4 2019. On a y-o-y basis, real GDP contracted by 3.1 percent after posting a 1.0-percent growth in the previous quarter.[57]

Meanwhile, the composite PMI for the euro area rose to 47.5 in June from 31.9 in May as the easing of COVID-19 containment measures helped many firms reopen and drove the demand for goods and services.[58]

[52] JP Morgan Global Manufacturing & Services PMI, http://www.markiteconomics.com/

[53] US Bureau of Economic Analysis, "Gross Domestic Product: First Quarter 2020 (Third Estimate)," news release, 25 June 2020. https://www.bea.gov/sites/default/files/2020-06/gdp1q20_3rd_1.pdf

[54] Institute for Supply Management, https://www.instituteforsupplymanagement.org

[55] The Conference Board, http://www.conference–board.org/

[56] University of Michigan Survey of Consumers, http://www.sca.isr.umich.edu/

[57] Eurostat news release 91/2020 dated 9 June 2020

[58] Flash Markit Eurozone PMI, http://www.markiteconomics.com/

Economic activity in the euro area show signs of recovery

Inflation in the euro area rose to 0.3 percent in June from 0.1 percent in May. Inflation was driven mainly by food, alcohol and tobacco, and services.[59] Meanwhile, the seasonally adjusted unemployment rate rose to 7.4 percent in May from 7.3 percent in the previous month.

The European Commission's Economic Sentiment Indicator in the euro area rose to 75.7 in June from 67.5 in May, reflecting the improvement in confidence across all business sectors (i.e., industry, services, retail trade, construction) and among consumers.

Japan. On a q-o-q seasonally adjusted basis, real GDP declined by 0.6 percent in Q1 2020 from a 1.9-percent contraction in Q4 2019. Similarly, on a y-o-y basis, real GDP fell by 1.7 percent in Q1 2020 after contracting by 0.7 percent in the previous quarter as both private and public demand declined during the quarter.[60]

Japan remains in contraction

The seasonally adjusted manufacturing PMI continued to signal a contraction even as it rose to 40.1 in June from 38.4 in May due to a sharp reduction in new orders, output, and purchasing activity.[61]

Inflation was 0.1 percent in May, the same rate recorded for April. The latest inflation figure was driven mainly by higher inflation for housing as well as culture and recreation. Meanwhile, the seasonally adjusted unemployment rate rose to 2.9 percent in May from 2.6 percent in April.

China. Real GDP in China contracted by 6.8 percent y-o-y in Q1 2020 from a 6.0-percent growth in Q4 2019 amid the disruptive impact of the COVID-19 outbreak on economic activity.

[59] Eurostat news release 114/2020 dated 17 July 2020

[60] Second Preliminary Estimate. Department of National Accounts, Economic and Social Research Institute, Cabinet Office. http://www/esri.cao.go.jp/

[61] Jibun Bank Japan Manufacturing PMI, http://www.markiteconomics .com/

Chinese manufacturing conditions strengthen

Meanwhile, China's seasonally adjusted manufacturing PMI rose to 51.2 in June from 50.7 in May amid a general improvement in market conditions, as the easing of COVID-19 containment measures enabled firms to resume normal business operations.[62]

Inflation increased to 2.5 percent in June from 2.4 percent in May due to higher food inflation.

India. Real GDP in India grew by 3.1 percent y-o-y in Q1 2020 from 4.1 percent in Q4 2019. Albeit slower, the latest GDP expansion was driven mainly by growth in agriculture, forestry, and fishing; mining and quarrying; as well as electricity, gas, water supply and other utility services.[63]

Economic activity in India continues to ease

Meanwhile, the composite PMI rose to 37.8 in June from 14.8 in May as manufacturing production fell moderately, while services activity continued to decrease substantially.

Inflation in India was at 6.1 percent in June. Meanwhile, retail food inflation, measured by the consumer food price index, fell to 7.87 percent in June from 9.20 percent in May.[64]

[62] Caixin China General Manufacturing PMI, http://www.markiteconomics.com/

[63] Ministry of Statistics and Programme Implementation. http://mospi.nic.in/

[64] All-India General CPI were not compiled for the months of April and May 2020. In view of the preventive measures and announcement of nationwide lockdown by the government of India to contain the spread of the COVID-19 pandemic, the price collection of CPI through personal visits of price collectors was suspended effective 19 March 2020.

ASEAN Region. The Nikkei ASEAN Manufacturing PMI rose to 43.7 in June from 35.5 in May as both factory production and new orders continued to decline, although at softer rates than in the previous month.

Manufacturing conditions in the ASEAN region deteriorate at a softer pace

Vietnam and Malaysia saw an improvement in operating conditions during the month. The Philippines, Myanmar, Thailand, Indonesia, and Singapore remained in contraction territory, with Singapore reporting the most marked downturn across each of the monitored countries.[65]

Policy Actions by Other Central Banks. On 18 June 2020, Bank Indonesia (BI) decided to lower the 7-day reverse repo rate by 25 basis points (bps) to 4.25 percent from 4.5 percent. According to BI, their decision was consistent with efforts to maintain economic stability and support the momentum of recovery during the period of COVID-19. BI views that there is still monetary space to lower interest rates in line with mild inflationary pressures, maintained external stability, and the need to stimulate economic growth.

Central banks reduce their respective policy rates mainly in response to the COVID-19 outbreak

On 28 May 2020, Bank of Korea decided to lower its base rate by 25 bps to 0.50 percent from 0.75 percent as economic growth is expected to be sluggish and demand-side inflationary pressures are forecast to remain weak due to the COVID-19 pandemic.

Similarly, in an unscheduled monetary policy meeting on 22 May 2020, the Reserve Bank of India reduced its policy repo rate by 40 bps to 4.0 percent from 4.4 percent. The decision was based on the view that the macroeconomic impact of the COVID-19 pandemic is turning out to be more severe than initially anticipated and that various sectors of the Indian economy are experiencing acute stress.

On 20 May 2020, Bank of Thailand reduced its policy rate by 25 bps to 0.50 percent based on its assessment that the Thai economy would contract more than previously estimated due to the more-than-expected contraction of the global economy along with the impact of the COVID-19 containment measures worldwide.

On 5 May 2020, Bank Negara Malaysia (BNM) decided to reduce its overnight policy rate (OPR) by 50 bps to 2.0 percent from 2.5 percent. The reduction in the OPR, along with other monetary and financial measures by the BNM, were expected to cushion the impact of the COVID-19 outbreak on businesses and households and lend support to economic activity.

Meanwhile, on 20 April, the PBOC decided to reduce the one-year loan prime rate by 20 bps to 3.85 percent from 4.05 percent to lower the borrowing costs for firms and support the economy amid the impact of the COVID-19 outbreak. On 15 April, the PBOC also reduced the rate for the one-year medium-term lending facility (MLF) by 20 bps to 2.95 percent, releasing about 100 billion yuan (US$14 billion) into the system. The reduced rate was the lowest since the MLF tool was introduced in September 2014.

Meanwhile, the Reserve Bank of New Zealand, Bank of Thailand, Bank of Japan, Bank of England, Central Bank of the Republic of China (Taiwan), the US Federal Reserve, European Central Bank, Reserve Bank of Australia, and Bank of Canada decided to keep their respective policy rates steady during their policy meetings in June.

[65] Nikkei ASEAN Manufacturing PMI, http://www.markiteconomics.com/

V. Monetary Policy Developments

On 16 April 2020, the BSP announced an off-cycle key policy rate reduction by 50 basis points (bps) to 2.75 percent for the overnight reverse repurchase or RRP facility.[66] Moreover, in the 25-June monetary policy meeting, the BSP decided to cut the policy rate anew by another 50 bps to 2.25 percent. The interest rates on the overnight lending and deposit facilities were likewise lowered accordingly.

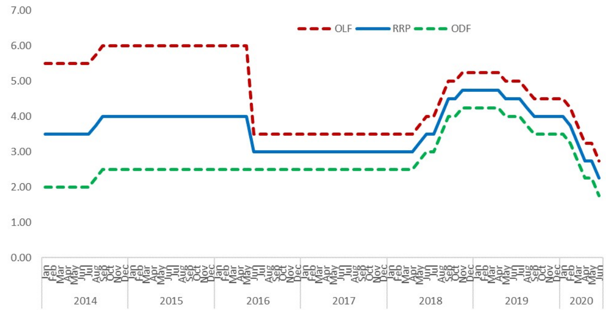
The BSP pursue 100-bp reduction in the key policy rate in Q2 2020

In deciding to reduce the key policy interest rate twice during the review quarter, the BSP assessed the impact of the COVID-19 pandemic on the Philippine economy.

Latest baseline forecasts during the review period indicate that inflation could settle near the low end of the target range of 3.0 percent ± 1 percentage point for 2020 up to 2022, with inflation expectations remaining firmly anchored over the policy horizon. Meanwhile, the balance of risks to the inflation outlook leans toward the downside from 2020 up to 2022 owing largely to the potential impact of a deeper and more disruptive pandemic on domestic and global demand conditions.

The BSP observed that domestic economic activity has slowed with the enforcement of necessary protocols to slow the spread of the virus in the country. Equally important, the outlook for global growth has deteriorated further as considerable uncertainty still surrounds the extent of the health crisis. The BSP noted that even as economies begin to reopen, the global recovery would likely be protracted and uneven. Hence, there remains a critical need for continuing measures to bolster economic activity and support financial conditions, especially the effective implementation of interventions to protect human health, boost agricultural productivity and build infrastructure.

Chart 33. BSP Policy Rates
In percent



Given these considerations, the BSP decided that a reduction in the policy rate amidst a benign inflation environment would help mitigate the downside risks to growth and boost market confidence. Even as domestic liquidity dynamics and market function continue to improve owing to prior liquidity-enhancing measures, the BSP believes that keeping an accommodative stance will further ease the cost of borrowing and ensure ample credit and liquidity in the financial system as the economy transitions toward recovery in the coming months.

Going forward, the BSP reiterates its support for the health and fiscal programs already being rolled out by the National Government in responding to the needs of Filipino households and businesses. The BSP remains committed to deploying its full range of monetary instruments and regulatory relief measures as needed in fulfillment of its mandate to promote non-inflationary and sustainable growth.

[66] The off-cycle policy rate decision substitutes for the scheduled monetary policy meeting on 21 May 2020.

VI. Inflation Outlook

BSP Inflation Forecasts

The latest baseline forecasts continue to suggest benign inflation environment over the policy horizon. Inflation is expected to average below the midpoint of the target range at 2.3 percent for 2020 and 2.6 percent for 2021. The preliminary forecasts for 2022 indicate that inflation could settle at the midpoint of the target range at 3.0 percent.

The forecast path for 2020 and 2021 is slightly higher compared to the outlook presented in the previous report. The policy and liquidity-enhancing measures implemented by the BSP in response to the pandemic as well as the higher domestic oil prices with the temporary increase in the import duties on imported crude oil and refined petroleum products contributed to the higher forecast path. These were partly offset by slower domestic and global economic activity as well as the continued appreciation of the peso.

The risks to the inflation outlook are tilted to the downside. The potential impact on global and domestic economic growth prospects of a more disruptive COVID-19 pandemic is the primary downside risk to inflation. Meanwhile, adjustments in utility rates and higher global rice prices are the main upside risks to inflation.

Inflation is projected to be generally benign throughout the policy horizon

Demand Conditions. Domestic growth contracted for the first time since Q4 1998, ending eighty-four (84) consecutive quarters of positive y-o-y growth in the country. GDP contracted by 0.2 percent in Q1 2020 compared to the 6.7-percent expansion in Q4 2019 and 5.7 percent in Q1 2019. On the production side, growth in all major sectors of the economy moderated, reflecting the initial impact of the community quarantine measures. On the expenditure side, the weak global environment and significant uncertainty owing to the COVID-19 pandemic adversely affected consumption, investments, and trade during the quarter.

Domestic economic activity is projected to follow a U-shaped quarterly recovery path with output likely to contract in the remaining quarters of 2020. Growth is expected to recover in 2021 once the impact of government policy measures fully gains traction. The BSP's timely actions to enhance liquidity conditions and bolster sentiment are expected to provide support once the economy restarts.

Growth is expected to follow a U-shaped quarterly recovery path

Moreover, the implementation of well-targeted amelioration and recovery programs as well as the restart of the Build Build Build program will help the country regain momentum, restore employment rates to pre-crisis levels, and attain higher economic growth. The country's recovery from the COVID-19 pandemic is expected to be fast-tracked by additional jobs that could be generated from higher infrastructure investments

High-frequency real sector indicators point to weak growth prospects in the near term. Manufacturing's volume of production index for May 2020 remains in negative territory. The composite Purchasing Managers' Index (PMI) also dropped below the 50-point mark as of June 2020, suggesting contraction across all sectors. Meanwhile, indicators on economic mobility suggest limited recovery thus far. Mobility reports from Google, Apple, and Waze suggest that activity in different locations, such as in retail and recreation areas, groceries, transit stations, and workplaces have been increasing but gradually since the start of the GCQ. However, these mobility indicators remain well below their levels prior to start of the containment measures.

Supply Conditions. Food prices are expected to remain benign over the near term with adequate domestic supply due to neutral weather conditions. Moreover, the initial production disruptions and logistical bottlenecks of several food items are likely to subside with the easing of quarantine measures. However, below-average rainfall had resulted in lower rice production volumes in the ASEAN. The droughts have caused the decline in harvested areas during the dry season. The US Department of Agriculture (USDA) projects that global rice production could decline by 0.5 percent in 2020. Moreover, production in major rice exporters in the ASEAN are expected to decline faster compared to the global average. Consequently, the decline in production could lead to export restrictions in these countries and lead to higher import prices.

Global crude oil prices initially declined to historic lows during the start of the quarter due to concerns on the impact of the pandemic on global demand. However, Dubai crude oil prices have almost doubled in June 2020 after bottoming out in April 2020 following the agreement among OPEC, Russia, and other major oil exporting countries to extend its coordinated production cut until July 2020.

Output gap is expected to remain negative over the policy horizon

The balance of demand and supply conditions as captured by the output gap (or the difference between actual and potential output), provides an indication of potential inflationary pressures in the near term.[67]

Based on the Q1 2020 GDP outturn, estimates by the BSP show that the output gap is projected to remain negative over the policy horizon. This reflects the potential adverse impact of the pandemic on economic activity and the country's production capacity.[68]

Key assumptions used to generate the BSP's inflation forecasts. The BSP's baseline inflation forecasts are based on the following assumptions:

1) BSP's overnight RRP rate at 2.25 percent from July 2020 to December 2022;

2) NG fiscal deficits for 2020 to 2022, which are consistent with the DBCC-approved estimates;

3) Dubai crude oil price assumptions consistent with the trend of futures prices of oil in the international market;

4) Increase in nominal wages consistent with historical wage increases and labor productivity growth;

5) Real GDP growth is endogenously determined; and

6) Foreign exchange rate is endogenously determined through the purchasing power parity and interest rate parity relationships.

Risks to the Inflation Outlook

The risks to the inflation outlook may be presented graphically through a fan chart. The fan chart depicts the probability of different inflation outcomes based on the central projection (corresponding to the baseline forecast of the BSP) and the risks surrounding the inflation outlook.

Compared to the previous inflation report, the latest fan chart shows a slightly higher inflation path due largely to faster domestic liquidity growth from the policy actions implemented by the BSP in response to the pandemic as well as the higher domestic oil prices with the temporary increase in the import duties on imported crude oil and refined petroleum products. These were partly offset by slower domestic and global economic activity as well as the continued appreciation of the peso.

Inflation path is slightly higher compared to the previous report

The BSP's review of current inflation dynamics suggests that the risks surrounding the inflation outlook appear to be on the downside for 2020 to 2022.

A more disruptive impact of COVID-19 could lead to a deeper slowdown in global growth with domestic implications. The risk of a second wave of the pandemic among major economies could result in the re-imposition of containment measures which is expected to further dampen consumer confidence and exacerbate the disruptions in supply chains and trade.

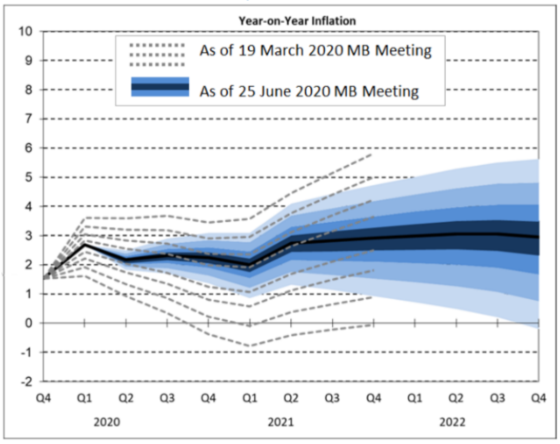
[67] Inflation tends to rise (fall) when demand for goods and services exert pressure on the economy's ability to produce goods and services, i.e., when the output gap is positive (negative).
[68] Based on the seasonally-adjusted GDP growth

Moreover, governments and central banks have implemented massive fiscal and monetary support during the first wave of the pandemic. The available policy space to provide the similar stimulus measures could be limited if a second wave develops. In the domestic front, a more severe pandemic could derail economic recovery and further heighten the uncertainty faced by firms and consumers.

The balance of risks to the inflation outlook leans to the downside for 2020 up to 2022

Various petitions for rate adjustments by Meralco and PSALM are considered as upside risks to inflation and have not yet been added to the baseline forecasts. Meralco's petitions include generation and transmission charges, system loss, lifeline subsidy, the December 2013 rate adjustment, which is the subject of Supreme Court temporary restraining order, and the ₱0.65/ kWh adjustment for the January 2014 billing period that is subject to the Energy Regulatory Commission's (ERC) approval. PSALM's petitions cover adjustments for fuel and foreign exchange costs.

Chart 34. Inflation Projection



Source: BSP estimates

Higher global rice prices also present an upside risk to the inflation outlook. More than 90 percent of the Philippines' rice imports are sourced from Thailand and Vietnam. While prices have remained stable in other source countries, like Bangladesh and India, lower export volumes in Thailand and Vietnam owing to unfavorable weather conditions could push global prices higher. In addition, tariffs from non-ASEAN countries are higher at 50 percent compared to rice imports from ASEAN countries.

The fan chart shows the probability of various outcomes for inflation over the forecast horizon. The darkest band depicts the central projection, which corresponds to the BSP's baseline inflation forecast. It covers 25 percent of the probability distribution. Each successive pair of bands is drawn to cover a further 25 percent of probability, until 75 percent of the probability distribution is covered. Lastly, the lightest band covers the lower and upper 90 percent of the probability distribution. The bands widen (i.e., "fan out") as the time frame is extended, indicating increasing uncertainty about outcomes. The band in wire mesh depicts the inflation profile in the previous report.

The shaded area, which measures the range of uncertainty, is based on the forecast errors from the past years. In greater detail, it can be enhanced by adjusting the level of skewness of the downside and upside shocks that could affect the inflationary process over the next two years in order to change the balance of the probability area lying above or below the central projection.

Implications for the Monetary Policy Stance

The BSP lowered the monetary policy interest rate twice in Q2 2020 for a cumulative reduction of 175 bps since the start of the year. In deciding on these follow-on policy actions, the BSP recognized that inflation is projected to be relatively benign for 2020 up to 2022 due to the impact of COVID-19 on global demand, domestic economic conditions, and commodity prices. Meanwhile, inflation expectations remain well within the target range of 3.0 percent ± 1 percentage point. The balance of risks to the inflation outlook are tilted to the downside over the policy horizon owing largely to the potential impact of a deeper and more disruptive pandemic on domestic and global demand conditions.

At the same time, the BSP has observed a considerable slowdown in domestic economic activity with the enforcement of necessary quarantine measures to control the spread of the virus across the country. Moreover, prospects for the global economy have deteriorated further amid considerable uncertainty surrounding the extent of the health crisis. Even as economies begin to reopen, the global recovery will likely be protracted and uneven.

Given these considerations, the BSP believes that there remains a critical need for continuing measures to bolster economic activity and support financial conditions. Keeping the monetary stance sufficiently accommodative amid a benign inflation environment will help mitigate the strong downside risks to growth and boost market confidence. Even with the improvement in domestic liquidity conditions and market function owing to prior liquidity-enhancing measures, the policy rate cuts during the quarter will also help ease the cost of borrowing further and ensure ample credit and liquidity in the financial system as the economy transitions toward recovery in the coming months.

Going forward, the BSP reiterates its support for the health and fiscal programs already being rolled out by the National Government in responding to the needs of Filipino households and businesses. The BSP remains committed to deploying its full range of monetary instruments and regulatory relief measures as needed in fulfillment of its mandate to promote non-inflationary and sustainable growth.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2008			
31 Jan 2008	5.00	7.00	The Monetary Board (MB) decided to reduce by 25 bps the BSP's key policy interest rates to 5 percent for the overnight borrowing or reverse repurchase (RRP) facility and 7 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts (SDAs) were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest inflation forecasts indicated that inflation would fall within the 4.0 percent ± 1 percentage point target range in 2008 and the 3.5 ± 1 percentage point target range in 2009.
13 Mar 2008 **24 Apr 2008**	5.00	7.00	The MB decided to keep the BSP's key policy interest rates at 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The MB also decided to implement immediately the following refinements in the SDA facility: (1) the closure of existing windows for the two-, three-, and six-month tenors; and (2) the reduction of the interest rates on the remaining tenors. The interest rates on term RRPs and RPs were also left unchanged.
5 Jun 2008	5.25	7.25	The MB decided to increase by 25 bps the BSP's key policy interest rates to 5.25 percent for the RRP facility and 7.25 percent for RP facility as emerging baseline forecasts indicate a likely breach of the inflation target for 2008 along with indications that supply-driven pressures are beginning to feed into demand. Given the early evidence of second-round effects, the MB recognized the need to act promptly to rein in inflationary expectations. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
17 Jul 2008	5.75	7.75	The MB increased by 50 bps the BSP's key policy interest rates to 5.75 percent for the overnight borrowing or RRP facility and 7.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
28 Aug 2008	6.00	8.00	The MB increased by 25 bps the BSP's key policy interest rates to 6.0 percent for the overnight borrowing or RRP facility and 8.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also increased accordingly.
6 Oct 2008 **6 Nov 2008**	6.00	8.00	The MB kept the BSP's key policy interest rates unchanged at 6.0 percent for RRP facility and 8.0 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
18 Dec 2008	5.50	7.50	The MB decided to reduce the BSP's key policy interest rates by 50 bps to 5.5 percent for the overnight borrowing or RRP facility and 7.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. This outlook is supported by the downward shift in the balance of risks, following the easing of commodity prices, the moderation in inflation expectations, and the expected slowdown in economic activity.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2009			
29 Jan 2009	5.00	7.00	The MB decided to reduce the BSP's key policy interest rates by another 50 bps to 5 percent for the overnight borrowing or RRP facility and 7 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also adjusted accordingly. Latest baseline forecasts showed a decelerating inflation path over the policy horizon, with inflation falling within target by 2010. The MB based its decision on the latest inflation outlook which shows inflation falling within the target range for 2009 and 2010. The Board noted that the balance of risks to inflation is tilted to the downside due to the softening prices of commodities, the slowdown in core inflation, significantly lower inflation expectations, and moderating demand.
5 Mar 2009	4.75	6.75	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.75 percent for the overnight borrowing or RRP facility and 6.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Given possible upside risks to inflation, notably the volatility in oil prices and in exchange rates, increases in utility rates, and potential price pressures coming from some agricultural commodities, the MB decided that a more measured adjustment of policy rates was needed.
16 Apr 2009	4.50	6.50	The MB reduced key policy rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility, effective immediately. This rate cut brings the cumulative reduction in the BSP's key policy rates to 150 bps since December last year. The current RRP rate is the lowest since 15 May 1992. Meanwhile, the interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. In its assessment of macroeconomic conditions, the MB noted that the latest baseline inflation forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the MB considered that the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.
28 May 2009	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. Baseline forecasts indicated a lower inflation path over the policy horizon, with average inflation expected to settle within the target ranges in 2009 and 2010. In addition, the Monetary Board considered that, on balance, the risks to inflation are skewed to the downside given expectations of weaker global and domestic demand conditions and a low probability of a significant near-term recovery in commodity prices.
9 Jul 2009	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility, effective immediately. The interest rates on term RRPs, RPs, and SDAs were reduced accordingly. This is the sixth time since December 2008 that the BSP has cut its policy interest rates.
20 Aug 2009 1 Oct 2009 5 Nov 2009 17 Dec 2009	4.00	6.00	The MB kept key policy rates unchanged at 4 percent for the RRP facility and 6 percent for the overnight lending RP facility. The decision to maintain the monetary policy stance comes after a series of policy rate cuts since December 2008 totaling 200 bps and other liquidity enhancing measures.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2010			
28 Jan 2010 **11 Mar 2010** **22 Apr 2010** **3 Jun 2010** **15 Jul 2010** **26 Aug 2010** **7 Oct 2010** **18 Nov 2010** **29 Dec 2010**	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4 percent for the RRP facility and 6 percent for the RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
2011			
10 Feb 2011	4.00	6.00	The MB decided to keep the BSP’s key policy interest rates steady at 4 percent for the overnight borrowing or RRP facility and 6 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
24 Mar 2011	4.25	6.25	The MB decided to increase by 25 bps the BSP’s key policy interest rates to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. The MB’s decision was based on signs of stronger and broadening inflation pressures as well as a further upward shift in the balance of inflation risks. International food and oil prices have continued to escalate due to the combination of sustained strong global demand and supply disruptions and constraints.
5 May 2011	4.50	6.50	The MB decided to increase the BSP’s key policy interest rates by another 25 bps to 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also raised accordingly. Baseline inflation forecasts continue to suggest that the 3-5 percent inflation target for 2011 remains at risk, mainly as a result of expected pressures from oil prices.
16 Jun 2011	4.50	6.50	The MB decided to keep policy rates steady at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board decided to raise the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on Friday, 24 June 2011. The MB's decision to raise the reserve requirement is a preemptive move to counter any additional inflationary pressures from excess liquidity.
28 Jul 2011	4.50	6.50	The MB maintained the BSP's key policy interest rates at 4.5 percent for the overnight borrowing or RRP facility and 6.5 percent for the overnight lending or RP facility. At the same time, the Board increased anew the reserve requirement on deposits and deposit substitutes of all banks and non-banks with quasi-banking functions by one percentage point effective on 5 August 2011. The MB's decision to raise the reserve requirement anew is a forward-looking move to better manage liquidity.
8 Sep 2011 **20 Oct 2011** **1 Dec 2011**	4.50	6.50	The MB decided to keep the overnight policy rates (OPR) steady. At the same time, the reserve requirement ratios (RRR) were kept unchanged.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
2012			
19 Jan 2012	4.25	6.25	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 4.25 percent for the overnight borrowing or RRP facility and 6.25 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB's decision is based on its assessment that the inflation outlook remains comfortably within the target range, with expectations well-anchored and as such, allowed some scope for a reduction in policy rates to help boost economic activity and support market confidence.
1 Mar 2012	4.00	6.00	The MB decided to reduce the BSP's key policy interest rates by another 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. The MB is of the view that the benign inflation outlook has allowed further scope for a measured reduction in policy rates to support economic activity and reinforce confidence.
19 Apr 2012	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged.
14 Jun 2012	4.00	6.00	The MB decided to keep the BSP's key policy interest rates steady at 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that the inflation environment remains manageable. Baseline forecasts continue to track the lower half of the 3-5 percent target range for 2012 and 2013, while inflation expectations remain firmly anchored. At the same time, domestic macroeconomic readings have improved significantly in Q1 2012.
26 Jul 2012	3.75	5.75	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the third time in 2012 that the BSP has cut its policy rates. The MB's decision was based on its assessment that price pressures have been receding, with risks to the inflation outlook slightly skewed to the downside. Baseline forecasts indicate that inflation is likely to settle within the lower half of the 3-5 percent target for 2012 and 2013, as pressures on global commodity prices are seen to continue to abate amid weaker global growth prospects. At the same time, the MB is of the view that prospects for global economic activity are likely to remain weak.
13 Sep 2012	3.75	5.75	The MB decided to keep the BSP's key policy interest rates steady at 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that the inflation environment remains benign, with the risks to the inflation outlook appearing to be broadly balanced.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
25 Oct 2012	3.50	5.50	The MB decided to reduce the BSP's key policy interest rates by 25 bps to 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also reduced accordingly. This is the fourth time in 2012 that the BSP has cut its policy rates. The MB's decision was based on its assessment that the inflation environment continued to be benign with latest baseline forecasts indicating that the future inflation path will remain within target for 2012-2014. A rate cut would also be consistent with a symmetric response to the risk of below-target inflation.
13 Dec 2012	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDAs were also left unchanged. The MB's decision was based on its assessment that current monetary settings remained appropriate, as the cumulative 100-bp reduction in policy rates in 2012 continued to work its way through the economy.
2013			
24 Jan 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained accordingly. The reserve requirement ratios were kept steady as well. At the same time, the MB decided to set the interest rates on the SDA facility at 3.00 percent regardless of tenor, effective immediately, consistent with the BSP's continuing efforts to fine-tune the operation of its monetary policy tools.
14 Mar 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Following its previous decision to rationalize the SDA facility in January 2013, the MB further reduced the interest rates on the SDA facility by 50 bps to 2.50 percent across all tenors effective immediately.
25 Apr 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rate on the RRP was also set at 3.50 percent regardless of tenor. Meanwhile, the SDA rate was further reduced by 50 bps to 2.0 percent across all tenors.
13 Jun 2013 25 Jul 2013 12 Sep 2013 24 Oct 2013 12 Dec 2013	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
2014			
6 Feb 2014	3.50	5.50	The MB decided to keep the BSP’s key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained.
27 Mar 2014	3.50	5.50	The MB decided to keep the BSP’s key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirement by one percentage point effective on 11 April 2014.
8 May 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also maintained. Meanwhile, the MB decided to increase the reserve requirements for U/KBs and TBs by a further one percentage point effective on 30 May 2014.
19 Jun 2014	3.50	5.50	The MB decided to keep the BSP's key policy interest rates steady at 3.50 percent for the overnight borrowing or RRP facility and 5.50 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also maintained. The reserve requirement ratios were left unchanged as well. Meanwhile, the MB decided to raise the interest rate on the SDA facility by 25 bps from 2.0 percent to 2.25 percent across all tenors effective immediately.
31 Jul 2014	3.75	5.75	The MB decided to increase the BSP's key policy rates by 25 bps to 3.75 percent for the overnight borrowing or RRP facility and 5.75 percent for the overnight lending or RP facility. The interest rates on term RRPs and RPs were also raised accordingly. The rate on special deposit accounts (SDA) was left unchanged. Meanwhile, the reserve requirement ratios were also kept steady.
11 Sep 2014	4.00	6.00	The MB decided to increase the BSP's key policy rates by 25 bps to 4.0 percent for the overnight borrowing or RRP facility and 6.0 percent for the overnight lending or RP facility. The interest rates on term RRPs, RPs, and SDA were also raised accordingly. Meanwhile, the reserve requirement ratios were left unchanged.
23 Oct 2014 **11 Dec 2014**	4.00	6.00	The MB decided to maintain the BSP’s key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.
2015			
12 Feb 2015 **26 Mar 2015** **14 May 2015** **25 Jun 2015** **13 Aug 2015** **24 Sep 2015** **12 Nov 2015** **17 Dec 2015**	4.00	6.00	The MB decided to maintain the BSP’s key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
2016				
11 Feb 2016 **23 Mar 2016** **12 May 2016**	4.00		6.00	The MB decided to maintain the BSP's key policy interest rates at 4.0 percent for the overnight borrowing or reverse repurchase (RRP) facility and 6.0 percent for the overnight lending or repurchase (RP) facility. The interest rates on term RRPs, RPs, and special deposit accounts were also kept steady. The reserve requirement ratios were left unchanged as well.
23 Jun 2016 **11 Aug 2016** **22 Sep 2016** **10 Nov 2016** **22 Dec 2016**	3.00	2.50	3.50	The BSP formally adopted an interest rate corridor (IRC) system as a framework for conducting its monetary operations. The shift to IRC is an operational adjustment and not a change in the monetary policy stance. The IRC is a system for guiding short-term market rates towards the BSP policy interest rate which is the overnight reverse repurchase (RRP) rate. The IRC system consists of the following instruments: standing liquidity facilities, namely, the overnight lending facility (OLF) and the overnight deposit facility (ODF); the overnight RRP facility; and a term deposit auction facility (TDF). The interest rates for the standing liquidity facilities form the upper and lower bound of the corridor while the overnight RRP rate is set at the middle of the corridor. The repurchase (RP) and Special Deposit Account (SDA) windows will be replaced by standing overnight lending and overnight deposit facilities, respectively. Meanwhile, the reverse repurchase (RRP) facility will be modified to a purely overnight RRP. In addition, the term deposit facility (TDF) will serve as the main tool for absorbing liquidity. The interest rates for these facilities will be set as follows starting 3 June 2016: • 3.5 percent in the overnight lending facility (a reduction of the interest rate for the upper bound of the corridor from the current overnight RP rate of 6.0 percent); • 3.0 percent in the overnight RRP rate (an adjustment from the current 4.0 percent); and • 2.5 percent in the overnight deposit facility (no change from the current SDA rate).
2017				
9 Feb 2017 **23 Mar 2017** **11 May 2017** **22 Jun 2017** **10 Aug 2017** **21 Sep 2017** **9 Nov 2017** **14 Dec 2017**	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight (RRP) facility, 3.5 percent for the overnight lending facility (OLF) and 2.5 percent for the overnight deposit facility (ODF). The reserve requirement ratios were left unchanged as well.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2018				
8 Feb 2018	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
15 Feb 2018				The reserve requirement ratio was reduced by one (1) percentage point as an operational adjustment to support the BSP's shift toward a more market-based implementation of monetary policy as well as its broad financial market reform agenda. The reduction will apply to the reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions with reserve requirement at twenty (20) percent.
22 Mar 2018	3.00	2.50	3.50	The MB decided to maintain the BSP's key policy interest rates at 3.0 percent for the overnight RRP facility, 3.5 percent for the OLF and 2.5 percent for the ODF.
10 May 2018	3.25	2.75	3.75	The MB decided to increase the BSP's key policy interest rates by 25 basis points to 3.25 percent for the overnight RRP facility, 3.75 percent for the OLF and 2.75 percent for the ODF.
24 May 2018				The reserve requirement ratio was reduced by one (1) percentage point as part of its medium-term financial market reform agenda to promote a more efficient financial system by lowering intermediation costs. The reduction will apply to those reservable liabilities of all banks and non-bank financial institutions with quasi-banking functions that are currently subject to a reserve requirement of nineteen (19) percent.
20 Jun 2018	3.50	3.00	4.00	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 3.50 percent for the overnight RRP facility, 4.00 percent for the OLF and 3.00 percent for the ODF.
9 Aug 2018	4.00	3.50	4.50	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2018	4.50	4.00	5.00	The MB decided to raise the BSP's key policy interest rates by 50 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
15 Nov 2018	4.75	4.25	5.25	The MB decided to raise the BSP's key policy interest rates by 25 basis points to 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
13 Dec 2018	4.75	4.25	5.25	The MB decided to maintain the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2019				
7 Feb 2019 **21 Mar 2019**	4.75	4.25	5.25	The MB decided to keep the BSP's key policy interest rates at 4.75 percent for the overnight RRP facility, 5.25 percent for the OLF and 4.25 percent for the ODF.
9 May 2019	4.50	4.00	5.00	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
16 May 2019	4.50	4.00	5.00	The MB decided to reduce the reserve requirements by 200 basis points (or 2 percentage points) which shall be implemented according to the following schedule: 100 basis points on 31 May 2019; 50 basis points on 28 Jun 2019; and 50 basis points on 26 Jul 2019. The reduction will apply to those reservable liabilities of universal and commercial banks (U/KBs) that are currently subject to a reserve requirement of eighteen (18) percent.
23 May 2019				The MB complemented the reduction in reserve requirements for universal and commercial banks (U/KBs) with a phased 200-basis-point reduction in the reserve requirements for thrift banks (TBs) and non-bank financial institutions with quasi-banking functions (NBQBs), as well as a 100-basis-point reduction for demand deposits and NOW accounts of rural and cooperative banks on 31 May 2019. Moreover, long-term negotiable certificates of time deposits issued by all banks and NBQBs will have reduced and uniform reserve requirement ratio of 4.0 percent. The reductions on reserve requirements will take effect for U/KBs, TBs, and NBQBs on the reserve weeks beginning 31 May 2019, 28 Jun 2019, and 26 Jul 2019. The lower ratios shall apply to all reservable liabilities except bonds and mortgage/chattel mortgage certificates as the BSP continues to assess the impact of a reduction in the reserve requirements on said instruments.
20 Jun 2019	4.50	4.00	5.00	The MB decided to maintain the BSP's key policy interest rates at 4.50 percent for the overnight RRP facility, 5.00 percent for the OLF and 4.00 percent for the ODF.
8 Aug 2019	4.25	3.75	4.75	The MB decided to reduce the BSP's key policy interest rates by 25 basis points to 4.25 percent for the overnight RRP facility, 4.75 percent for the OLF and 3.75 percent for the ODF.
26 Sep 2019	4.00	3.50	4.50	The MB decided to cut the BSP's key policy interest rates by 25 basis points to 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
27 Sep 2019				The MB decided to reduce the reserve requirements for U/KBs, TBs, and RBs by 100 bps (or one percentage point). The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks. The reserve requirement of U/KBs was reduced from 16 percent to 15 percent, TBs from 6 percent to 5 percent, and RBs from 4 percent to 3 percent. The reduction will be effective on the first day of the first reserve week of November 2019.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	Monetary Policy Decisions
2019				
24 Oct 2019				The MB decided to reduce the reserve requirements for U/KBs and TBs by 100 bps (or one percentage point). The MB complemented the move with a reduction in the RRs for NBQBs. The reduction in reserve requirements will apply to the deposits and deposit substitute liabilities in local currency of banks and NBQBs. The reserve requirement of U/KBs was reduced from 15 percent to 14 percent, TBs from 5 percent to 4 percent, and NBQBs from 16 percent to 14 percent. The reduction will be effective on the first day of the first reserve week of December 2019.
14 Nov 2019	4.00	3.50	4.50	The MB decided to maintain the BSP's key policy interest rate at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
12 Dec 2019	4.00	3.50	4.50	The MB decided to maintain the BSP's key policy interest rates at 4.00 percent for the overnight RRP facility, 4.50 percent for the OLF and 3.50 percent for the ODF.
2020				
6 Feb 2020	3.75	3.25	4.25	The MB decided to cut the key policy interest rate by 25 bps to 3.75 percent. The interest rates on the OLF and ODF were reduced to 4.25 percent and 3.25 percent, respectively.
19 Mar 2020	3.25	3.75	2.75	The MB decided to cut the key policy interest rate by 50 bps to 3.25 percent, effective 20 March 2020. The interest rates on the OLF and ODF were reduced to 3.75 percent and 2.75 percent, respectively.
24 Mar 2020				The MB announced a 200-bp reduction in the RR ratio of reservable liabilities of universal and commercial banks (U/KBs) effective 3 April 2020. This puts RRR of U/KBs to 12 percent. The RR cut is intended to calm the markets and to encourage banks to continue lending to both retail and corporate sectors. This will ensure sufficient domestic liquidity in support of economic activity amidst the global pandemic due to the COVID-19.
16 Apr 2020	2.75	3.25	2.25	The MB decided to cut the interest rate on the BSP's overnight reverse repurchase (RRP) facility by 50 basis points (bps) to 2.75 percent, effective Friday, 17 April 2020. The interest rates on the OLF and ODF were reduced to 3.25 percent and 2.25 percent, respectively. The off-cycle rate cut is meant to strongly encourage lending to various sectors, especially the most vulnerable, amid the COVID-19 pandemic.
25 Jun 2020	2.25	2.75	1.75	The MB decided to cut the interest rate on the BSP's overnight reverse repurchase (RRP) facility by 50 basis points (bps) to 2.25 percent, effective Friday, 26 June 2020. The interest rates on the OLF and ODF were reduced to 2.75 percent and 1.75 percent, respectively. Amidst a benign inflation outlook, the MB sees a critical need for continuing measures to bolster economic activity and support financial conditions.

The *BSP Inflation Report* is published every quarter by the Bangko Sentral ng Pilipinas. The report is available as a complete document in pdf format, together with other general information about inflation targeting and the monetary policy of the BSP, on the BSP's website:

www.bsp.gov.ph/monetary/inflation.asp

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