Q3 | INFLATION REPORT

2020
THIRD 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 22 October 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.

[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 28 July 2020, 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
Peter B. Favila
Antonio S. Abacan, Jr.
V. Bruce J. Tolentino
Anita Linda R. Aquino

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) (MB Meeting No. 3)	16 (Thu) (19 Mar 2020 MB meeting)	24 (Fri) (Q1 2020 IR)
May	15 (Fri) (AC Meeting No. 3)			
Jun	16 (Tue) (AC Meeting No. 4)	25 (Thu) (MB Meeting No. 4)	18 (Thu) (16 Apr 2020 MB meeting)	
Jul			23 (Thu) (25 Jun 2020 MB meeting)	23 (Thu) (Q2 2020 IR)
Aug	17 (Mon) (AC Meeting No. 5)	20 (Thu) (MB Meeting No. 5)		
Sep	28 (Mon) (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)	29 (Thu) (Q3 2020 IR)
Nov	16 (Mon) (AC Meeting No. 7)	19 (Thu) (MB Meeting No. 7)		
Dec	14 (Mon) (AC Meeting No. 8)	17 (Thu) (MB Meeting No. 8)	17 (Thu) (19 Nov 2020 MB meeting)	

List of Acronyms, Abbreviations, and Symbols

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	Bank of Canada
	Bureau of Customs
BOE	Bank of England
BoP	Balance of Payments
BOT	Bank of Thailand
bp	Basis Point
BSPB	Bangko Sentral ng Pilipinas Bills
BTr	Bureau of the Treasury
BvD	Bureau van Dijk
CALABARZON	Cavite, Laguna, Batangas, Rizal and Quezon
CAMPI	Chamber of Automative 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
CREL	Commercial Real Estate Loan
DBCC	Development Budget Coordination Committee
DBM	Department of Budget and Management
DI	Diffusion Index
DOF	Department of Finance
ECB	European Central Bank
ECQ	Enhanced Community Quarantine
EIA	Energy Information Administration
EMBIG	Emerging Market Bond Index Global
ERC	Energy Regulatory Commission
FCD	Foreign Currency Deposit
GCQ	General Community Quarantine
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
IMTS	International Merchandise Trade Statistics
IPP	Independent Power Producers
IRC	Interest Rate Corridor
JMMC	Joint Ministerial Monitoring Committee
kWh	Kilowatt Hour
LFS	Labor Force Survey
LGU	Local Government Unit
LSOUR	Lifeline Subsidy Over/Under Recovery
MB	Monetary Board
mb/d	Million Barrels per Day
MECQ	Modified Enhanced Community Quarantine
MERALCO	Manila Electric Company
MISSI	Monthly Integrated Survey of Selected Industries
m-o-m	Month-on-Month
MTP	Major Trading Partner
NAP	National Accounts of the Philippines
NBFIs	Non-Bank Financial Intermediaries
NBQBs	Non-Banks with Quasi-Banking Functions
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
NNPL	Net Non-Performing Loans
NPC	National Power Corporation
NSFR	Net Stable Funding Ratio
ODF	Overnight Deposit Facility
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
RBA	Reserve Bank of Australia
RBNZ	Reserve Bank of New Zealand
RBs	Rural Banks
RCEF	Rice Competitiveness Enhancement Fund
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
RTBs	Retail Treasury Bonds
SBL	Substandard or Below Loan
SDA	Special Deposit Account
SLOS	Senior Bank Loan Officers' Survey
SONA	Sate of the Nation Address
SLOUR	System Loss Over/Under Recovery
SME	Small and Medium Enterprise
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
TMA	Truck Manufacturers Association
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
WAIR	Weighted Average Interest Rate
WESM	Wholesale Electricity Spot Market
y-o-y	Year-on-Year
y-t-d	Year -to-Date

Contents

Overview

Headline inflation inches up, remains within target range. Inflation for Q3 2020 rose to 2.5 percent year-on-year (y-o-y), higher than the quarter- and year-ago rates of 2.3 percent and 1.7 percent, respectively. The uptick in headline inflation was driven by non-food items, primarily transport services and domestic petroleum products, which offset the lower inflation for food items. The year-to-date (y-t-d) inflation, thus, settled at 2.5 percent, remaining within the National Government's (NG) target of 3.0 percent ± 1.0 percentage point (ppt) for 2020.

Headline inflation rises slightly, stays within 2-4 percent target range

Core inflation, which measures underlying price pressures, also went up to 3.2 percent in Q3 2020 from 2.9 percent in the previous quarter. In contrast, preliminary estimates of the BSP-computed alternative measures for core inflation continued to ease. Moreover, the number of CPI items with inflation rates higher than the threshold of 4.0 percent declined to 51 items in Q3 2020 from 55 items in the previous quarter. These items accounted for a lower proportion of the CPI basket at around 17.4 percent.

Inflation expectations over the policy horizon continue to be manageable. The results of the BSP's survey of private sector economists for September 2020 showed higher mean inflation forecasts for 2020 and 2022 relative to the June 2020 survey, and a lower mean inflation forecast for 2021. Mean inflation forecast for 2020 and 2022 increased to 2.5 percent from 2.3 percent and 3.0 percent from 2.9 percent, respectively. Meanwhile, mean inflation forecast for 2021 eased to 2.8 percent from 2.9 percent. Analysts expect inflation to remain at the lower end of the target range in 2020, with broadly balanced risks to the inflation outlook.

Domestic economy contracts further. The Q2 2020 real gross domestic product (GDP) declined further by 16.5 percent y-o-y from a contraction of 0.7 percent a quarter ago and a reversal from the 5.4-percent expansion a year ago. This brought real GDP for the first half of 2020 to a 9.0-percent contraction. The Q2 GDP outturn reflected the impact of the implementation of strict community quarantine measures. On the demand side, household consumption and investments declined further by 15.5 percent and 53.5 percent, respectively, offsetting the 22.0-percent increase in government spending. On the supply side, the services sector reversed to a decline by 15.8 percent while the industry sector deteriorated further by 22.9 percent.

Real GDP contracts further in Q2 2020

High-frequency demand indicators continue to suggest a below-optimal domestic activity in the near term. The composite Purchasing Managers' Index (PMI) in September 2020 showed signs of improvement but remained below the expansion threshold. In the manufacturing sector, volume and value of production orders continue to deteriorate. Similarly, the Q3 2020 survey for business and consumer sentiment reflected pessimism for the current and next quarters. Other indicators point to continued demand weakness as well, such as lower sales of new vehicles and energy consumption. Moreover, real estate values in central business districts eased while vacancy rates increased.

Nevertheless, global economy is seeing signs of recovery. The JP Morgan Global All-Industry Output Index stood at 52.1 in September 2020. Most of the sub-sectors surveyed registered output growth during the month, with the strongest performance posted by the investment goods industry. At the country-level statistics, real GDP in Q2 2020 contracted in major economies such as the US, euro area and Japan, although their PMIs for September signaled a recovery in demand, except for Japan. Meanwhile, China's economy grew in Q2 with September PMI registering an expansion. The uneven pace of global recovery as well as risk of disruptions as key cities reopen prompted central banks to maintain accommodative policy settings to support their respective economies.

The domestic financial system remains stable amid ample liquidity. The gradual easing of quarantine measures in key areas in the country buoyed the Philippine Stock Exchange index (PSEi) to increase by 2.7 percent quarter-on-quarter (q-o-q) to average 5,990.40 index points in Q3 2020. In the government securities (GS) market, Treasury bills auctions by the Bureau of the Treasury (BTr) were oversubscribed, with the T-bill rates lower than in the previous quarter, reflecting strong market interest amid ample liquidity in the financial system. The BTr also issued about ₱516.3 billion worth of 5-year Retail Treasury Bonds (RTBs) during the quarter. Similarly, GS yields at the short-end of the curve were lower as of end-September 2020 compared to end-June 2020. In the foreign exchange market, the peso averaged ₱48.94/US$1 in Q3 2020, appreciating by 3.09 percent from the Q2 2020 average of ₱50.45/US$1. The sustained strength of the peso is due in part to the country's high level of international reserves. Finally, the banking system continued to show resilience and stability in Q3 2020, with financial transactions increasing following the easing of quarantine measures. As of end-August, gross non-performing loans (GNPL) ratio rose to 2.8 percent which stayed below the pre-Asian crisis level of 3.5 percent. Capital adequacy ratios (CAR) likewise remained above the BSP's and Bank for International Settlements' (BIS) prescribed levels.

The BSP maintains key policy rate in Q3 2020. The BSP kept the interest rate for the overnight reverse repurchase (RRP) facility steady at 2.25 percent in its August and October monetary policy meetings. The BSP's decision to keep the policy rate unchanged was based on the assessment that prevailing monetary policy settings remain appropriate.

Key policy rate remains steady during the quarter

The latest baseline inflation forecasts show a slightly lower path within the NG's 2-4 percent target range, reflecting the lower-than-expected inflation in August, the moderation in global crude oil prices, and the appreciation of the peso. The balance of risks to the inflation outlook also continues to lean toward the downside from 2020 until 2022, owing largely to the risk of potential disruptions to domestic and global economic activity amid the ongoing pandemic. Equally important, inflation expectations remain firmly anchored within the inflation target band.

Given these considerations, the BSP is of the view that prevailing monetary policy settings remain appropriate. A prudent pause will enable the cumulative 175-basis-point (bp) reduction in the policy rate as well as other monetary and regulatory relief measures by the BSP to fully work their way through the economy.

Looking ahead, the benign inflation environment gives the BSP ample room to keep the monetary stance sufficiently accommodative to mitigate the strong downside risks to growth. Moreover, 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.

I. Inflation and Real Sector Developments

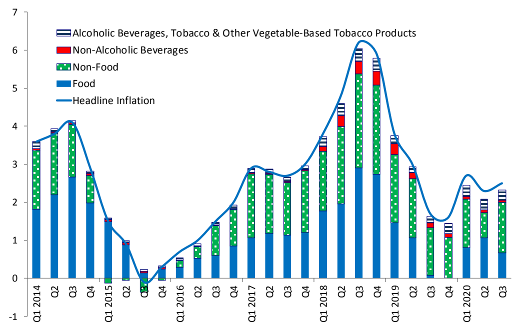
Prices

Headline inflation. Headline inflation increased to 2.5 percent y-o-y in Q3 2020, which was higher than the quarter- and year-ago rates of 2.3 percent and 1.7 percent, respectively. The headline inflation outturn was a result of the acceleration in non-food inflation, which more than offset the slowdown in food inflation.

Headline inflation rises in Q3 2020 but remains within target

The year-to-date inflation of 2.5 percent for the period January-September 2020 remains within the NG's inflation target range of 3.0 percent ± 1.0 ppt for the year.

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



Source: Philippine Statistical Authority (PSA), BSP

Core Inflation. Core inflation—which excludes selected volatile food and energy items to measure underlying price pressures—also went up to 3.2 percent y-o-y in Q3 2020 from 2.9 percent in the previous quarter.

Official core inflation also rises in Q3 2020

By contrast, preliminary estimates showed that all three BSP-computed alternative core inflation measures continued to ease in Q3 2020 compared to their respective rates in the previous quarter.

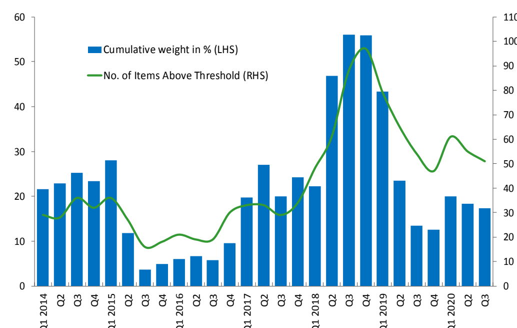
Table 1. Alternative Core Inflation Measure
Quarterly averages of year-on-year change

Quarter	Official Headline Inflation	Official Core Inflation	Trimmed Mean [1]	Weighted Median [2]	Net of Volatile Items [3]
2018					
Q1	3.8	3.0	2.9	2.8	3.8
Q2	4.8	3.8	3.6	3.8	4.3
Q3	6.2	4.7	5.0	4.6	4.7
Q4	5.9	4.9	5.2	5.2	4.9
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
Q3	**2.5**	**3.2**	**2.0**	**2.2**	**3.0**

[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, BSP estimates

The number of CPI items with inflation rates higher than the threshold declined to 51 items in Q3 2020 from 55 items in the previous quarter and accounted for a lower proportion of the CPI basket at around 17.4 percent in Q3 2020 from 18.3 percent in the previous quarter.

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



Source: PSA, BSP staff estimates

Food Inflation. Food inflation slowed down to 1.9 percent y-o-y in Q3 2020 from 3.0 percent in the previous quarter as selected key food items registered lower inflation rates. On a y-o-y basis, fish inflation eased from the previous quarter owing to sufficient domestic supply while vegetable inflation turned negative.

Food inflation slows down...

Meanwhile, y-o-y rice inflation continued to decline in Q3 2020 albeit at a lesser extent compared to the previous quarter. Weekly rice prices remained broadly stable despite the ongoing lean season and the reinstatement of stricter community quarantine measures in the National Capital Region (NCR) and nearby provinces in the first half of August, due to the improved output for the dry-season crop and additional supply from private sector importation.

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

Commodity	2019	2020	
	Q3	Q2	Q3
Food and Non-Alcoholic Beverages	**0.5**	**3.0**	**1.9**
Food	0.2	3.0	1.9
Bread and Cereals	-3.6	-1.4	-0.2
Rice	-5.8	-2.8	-0.9
Corn	-3.6	-0.2	-0.4
Meat	2.8	2.7	3.9
Fish	2.7	8.0	2.9
Milk, Cheese and Eggs	2.7	3.6	2.9
Oils and Fats	1.8	2.0	2.4
Fruit	7.3	11.1	7.2
Vegetables	-1.0	7.4	-0.9
Sugar, Jam, Honey, Chocolate and Confectionery	-2.8	-0.8	0.1
Food Products, N.E.C.	6.5	6.6	5.3
Non-Alcoholic Beverages	4.2	2.6	2.1
Alcoholic Beverages and Tobacco	11.1	18.1	16.5

Source of Basic Data: PSA, BSP

Non-food Inflation. By contrast, non-food inflation increased to 2.2 percent in Q3 2020, higher than the quarter- and year-ago rates of 1.1 percent and 2.1 percent, respectively, due largely to the acceleration in transport services inflation. Tricycle fare hikes along with the higher inflation for jeepney, bus and ship fares drove transport services inflation higher in Q3 2020. At the same time, y-o-y inflation for operation of personal transport equipment also turned less negative compared to the previous quarter. Inflation for housing, water, electricity, gas, and other fuels went up y-o-y during the quarter, which also contributed to the rise in non-food inflation.

… while non-food inflation accelerates during the quarter

Meanwhile, other major commodity groups under the non-food category registered lower or unchanged inflation rates in Q3 2020 compared to the previous quarter. Inflation for education eased markedly while that for recreation and culture also slowed down as prices for lotto tickets were reverted to ₱20.00 from ₱24.00 during the quarter.

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

Commodity	2019	2020	
	Q3	Q2	Q3
Non-Food	**2.1**	**1.1**	**2.2**
Clothing and Footwear	2.6	2.5	2.0
Housing, Water, Electricity, Gas and Other Fuels	1.6	0.2	1.0
Furnishings, Household Equipment & Routine Household Maintenance	2.9	4.1	3.9
Health	3.1	2.8	2.8
Transport	-0.2	-3.1	7.0
Communication	0.3	0.3	0.3
Recreation and Culture	2.1	1.4	0.2
Education	4.4	3.6	0.5
Restaurant and Miscellaneous Goods and Services	3.2	2.4	2.3

Source of Basic Data: PSA, BSP

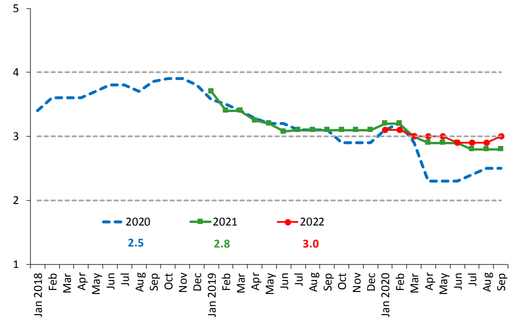
Private Sector Economists' Inflation Forecasts. The results of the BSP's survey of private sector economists for September 2020 showed higher mean inflation forecasts for 2020 and 2022 relative to the June 2020 survey, and a lower mean inflation forecast for 2021.[4]

Inflation expectations are higher for 2020 and 2022, but lower for 2021

Based on the September 2020 survey, the mean inflation forecast for 2020 increased to 2.5 percent from 2.3 percent. Likewise, mean inflation forecast for 2022 rose to 3.0 percent from 2.9 percent. By contrast, the mean inflation forecast for 2021 eased to 2.8 percent from 2.9 percent.

[4] There were 24 respondents in the BSP's survey of private sector economists in September 2020. The survey was conducted from 7 to 22 September 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 September 2020 (2012=100)



*Based on forecasts provided by 24 respondents.
Source: BSP

Analysts expect inflation to remain at the lower end of the target range in 2020, with broadly balanced risks to the inflation outlook.

The key upside risks to inflation include:

(a) a rebound in domestic demand as the economy gradually re-opens;
(b) higher transport prices;
(c) the supply chain disruptions due to the quarantine measures;
(d) higher prices of basic and essential items such as food; and
(e) higher headline inflation brought about by the additional liquidity from the BSP's series of policy easing.

Table 4. Private Sector Forecasts for Inflation
Annual percentage change; September 2020 (2012=100)

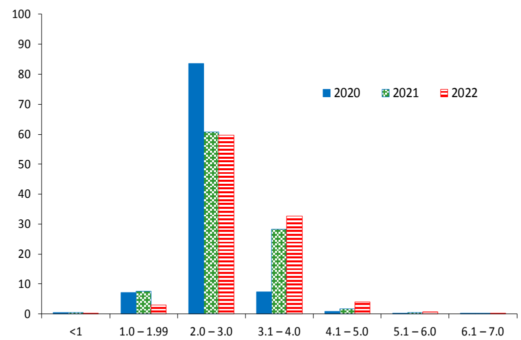
	2020		2021	2022
	Q4	FY	FY	FY
1) Al-Amanah Islamic Bank	3.00	2.80	3.00	3.50
2) Banco De Oro	2.67	2.53	2.70	3.00
3) Bangkok Bank	2.50	2.50	3.00	3.00
4) Bank of Commerce	2.39	2.46	-	-
5) Bank of China Ltd.	2.50	2.00	2.50	2.50
6) Barclays	2.30	2.50	3.00	-
7) Chinabank	2.60	2.50	2.60	2.60
8) CTBC Bank	2.00-2.50	2.00-2.50	2.50-3.50	2.50-3.50
9) Deutsche Bank	-	2.30	2.90	-
10) Eastwest Bank	3.30	2.70	2.40	3.10
11) Global Source	2.30	2.50	2.70	2.90
12) Korea Exchange Bank	2.50	2.50	2.70	2.90
13) Land Bank of the Phils	2.50	2.30	2.00	2.20
14) Maybank	2.77	2.55	3.20	3.00
15) Maybank-ATR KimEng	2.10	2.40	2.50	2.50
16) Metrobank	-	2.60	2.60	2.50-3.50
17) Nomura	2.30	2.50	2.90	3.30
18) RCBC	2.40	2.50	2.60-3.10	2.90-3.40
19) Robinsons Bank	2.30	2.40	3.00	3.00
20) Philippine Equity Partners	2.50	2.50	3.10	-
21) Security Bank	2.60	2.50	3.00	3.50
22) Standard Chartered	2.30	2.40	2.90	3.00
23) Union Bank of the Phils.	2.20	2.40	2.80	3.10
24) UBS	2.70	2.60	2.70	-
Median Forecast	2.5	2.5	2.9	3.0
Mean Forecast	**2.5**	**2.5**	**2.8**	**3.0**
High	3.3	2.8	3.2	3.5
Low	2.1	2.0	2.0	2.2
Number of Observations	22	24	23	19
Government Target	**3.0±1.00**	**3.0±1.00**	**3.0±1.00**	**3.0±1.00**

Source: BSP

Meanwhile, downside risks to inflation are seen to emanate from: (a) subdued domestic demand due to prolonged lockdown restrictions, lower consumer spending, and high unemployment resulting from the closure of businesses;
(b) downside pressures on global crude oil prices; and (c) oversupply of discretionary goods resulting as consumer demand were limited to essential goods.

Based on the probability distribution of the forecasts provided by 20 out of 24 respondents, there is a 90.9-percent probability that average inflation for 2020 will settle between the 2-4 percent range, while there is a 7.6 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 89 percent and 92.3 percent, respectively.

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



*Probability distributions were averages of those provided by 20 out of 24 respondents.
Source: September 2020 BSP Survey

Based on the Q3 2020 BSP Business Expectations Survey (BES), a lower number of respondents expect inflation to increase in the current quarter compared to the Q1 2020 survey results.[5] Similarly, the respondents continue to generally anticipate higher inflation in the next quarter.

Firms and consumers expect inflation to remain within the government's target range

Nevertheless, businesses expect that the rate of increase in commodity prices will remain within

[5] The conduct of the Q2 2020 BES and CES in April 2020 was cancelled due to the implementation of the Enhanced Community Quarantine (ECQ) from 16 March to 31 May 2020. As such, no reports and statistics on the said surveys was published on 26 June 2020.

the NG's 2 to 4 percent inflation target range for 2020 and 2021. In particular, firms generally anticipated that inflation will be at 2.3 percent for Q3 2020, 2.4 percent for Q4 2020, and 2.5 percent for the next 12 months.

Consumer Expectations Survey (CES) results for Q3 2020 indicated that consumers expect inflation to remain within the government's target range in 2020-2021. In particular, households generally anticipate inflation to fall below the midpoint of the target at 2.5 percent for Q3 2020, 2.6 percent for Q4 2020, and 2.8 percent for the next 12 months. Meanwhile, inflation is expected to decrease for the following items: bread and cereals (4.2 percent); fish and seafood (6.8 percent); vegetables (4.5 percent); milk, cheese, and eggs (5.5 percent); non-alcoholic beverages (4.1 percent); alcoholic beverages (7.8 percent); clothing (0.8 percent); house rent (2.0 percent); communication (1.2 percent); education (1.7 percent); recreation (0.7 percent); personal care (3.2 percent); and restaurants and cafes (1.9 percent).

Energy prices. The average price of Dubai crude oil increased by 40.5 percent q-o-q in Q3 2020 amid signs of some demand recovery as lockdown measures eased and manufacturing activity improved, which was generally reflected in the gradual pickup in global oil consumption.[6]

International oil prices increase during the review quarter

At the same time, the Organization of Petroleum Exporting Countries (OPEC) and other participating non-OPEC producers' (OPEC+) decision to extend the first phase of their production cut to July along with a high degree of compliance to the agreement within the group has also contributed to the price increase. Compliance within the OPEC+ was reported at 97 percent in July[7] and 102 percent in August.[8] In September 2020, the Joint Ministerial Monitoring Committee (JMMC) has also reiterated the importance of adhering to the OPEC+ production agreement.

However, oil demand outlook continues to be uncertain given rising COVID-19 cases. In its September 2020 report, OPEC revised its world oil demand projections[9] downward by 0.40 million barrels per day (mb/d) and 0.77 mb/d in 2020 and 2021, respectively, compared to their previous month's report. Likewise, the US Energy Information Administration (EIA)[10] has also cut its forecast for global oil consumption by 0.1 mb/d in 2020 and 0.6 mb/d in 2021 compared to the previous month's projections. By contrast, US EIA raised its forecast for world oil production by 0.4 mb/d in 2020 while keeping its 2021 forecast broadly unchanged in September relative to its August report.

Meanwhile, on a y-t-d basis, there was a net price decrease for domestic petroleum products as of 29 September 2020 in Metro Manila. Domestic prices of gasoline, diesel, and kerosene decreased by ₱7.00 per liter, ₱7.07 per liter, and ₱13.02 per liter, respectively, compared to end-2019 levels.

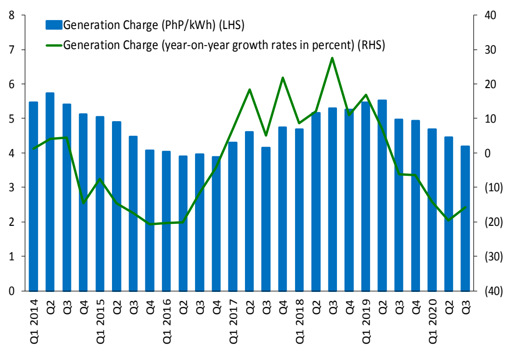
Power. The overall electricity rate in the Meralco-serviced area declined by around ₱0.28 per kilowatt hour (kWh) to about ₱8.54 per kWh (from ₱8.82 per kWh in Q2 2020) on the back of lower generation charge. According to Meralco, the downward adjustment in the generation cost was due primarily to the reduction in fixed costs for generation capacity as a result of Meralco's Force Majeure claim. Meralco continued to invoke the Force Majeure provision in its Power Supply Agreements (PSAs) in Q3 2020, owing to the significant reduction in power demand in its service area during the implementation of community quarantine. Further contributing to the decline in generation charges during the review period was the decrease in cost of power from the Independent Power Producers (IPPs) in July and August as a result of lower natural gas prices owing to quarterly repricing and improved average plant dispatch. Likewise, charges from the Wholesale Electricity Spot Market (WESM) declined in August and September driven by improved supply conditions in the Luzon grid as well as the decrease in Luzon demand as some areas returned to Modified Enhanced Community Quarantine (MECQ) for the period 4-18 August.

[6] Based on US EIA data, world oil consumption has been rising to 94.31 mb/d in August after dropping to 80.87 mb/d in April. US EIA Short-Term Energy Outlook, September 2020
[7] "OPEC : JMMC Reiterates the Importance of Attaining Full Conformity for Market Stability," August 19, 2020, https://www.opec.org/opec_web/en/press_room/6079.htm.
[8] "OPEC : JMMC Focuses on Market Stability and Full Conformity," September 17, 2020, https://www.opec.org/opec_web/en/press_room/6099.htm.
[9] OPEC Monthly Oil Market Report, September 2020
[10] US EIA Short-Term Energy Outlook, September 2020

Retail electricity prices go down relative to Q2 2020

There are potential sources of upside pressures on electricity charges. Meralco has existing petitions for rate increases with the Energy Regulatory Commission (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.

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



Source: Meralco

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.

Aggregate Demand and Supply[11]

The Q2 2020 real gross domestic product (GDP) contracted by 16.5 percent y-o-y from -0.7 percent in Q1 2020 and 5.4 percent in Q2 2019. This was also the lowest recorded since the start of the quarterly series data in 1981. On a seasonally-adjusted basis, q-o-q GDP continued to decline by 15.2 percent in Q2 2020, lower than the 5.7-percent contraction in Q1 2020.

Real GDP contracts in Q2 2020

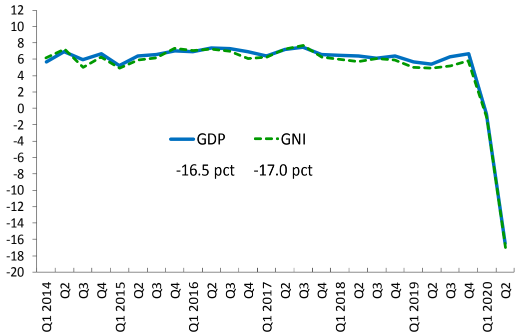
Gross national income (GNI) fell further by 17.0 percent in Q2 2020 from -1.2 percent in Q1 2020 and 4.9 percent in Q2 2019. Likewise, net primary income went down further by 22.0 percent in Q2 2020 from -5.9 percent in Q1 2020 and 0.3 percent in Q2 2019.

On the demand side, consumer and investor sentiment weakened in Q2 2020 following the heightened uncertainty and quarantine restrictions due to the COVID-19 pandemic. In particular, both household consumption (-15.5 percent) and investments (-53.5 percent) declined significantly during the period. These offset the increase in government consumption spending (22.1 percent), which reduced domestic demand by 19.7 percent in Q2 2020. Moreover, exports dropped further by 37.0 percent, while imports declined by 40.0 percent in Q2 2020.

On the supply side, measures implemented to contain the spread of COVID-19 resulted in supply chain disruptions and affected several industries. In Q2 2020, the services sector declined by 15.8 percent (a reversal of the 0.6-percent growth in the previous quarter) as most of its subsectors recorded double-digit contractions. Likewise, the industry sector contracted further by 22.9 percent in Q2 2020 (from -3.4 percent in Q1 2020) due largely to the decline in manufacturing and construction. Only the agriculture sector expanded in Q2 2020 by 1.6 percent from -0.3 percent in the previous quarter.

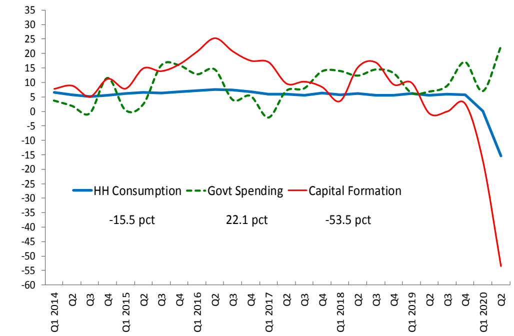
[11] Estimates on the second quarter 2020 National Accounts of the Philippines (NAP) are based on the 2018 base year following the recent revision and rebasing of the NAP series.

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



Source: PSA

Chart 7. Gross Domestic Product by Expenditure Shares
At constant 2018 prices



Source: PSA

Aggregate Demand. Under the expenditure approach, household spending, government spending, net exports, and investments (or capital formation) contributed -10.7 ppts, 3.1 ppts, 4.9 ppts, and -13.9 ppts, respectively, to total GDP growth in Q2 2020.

Contractions in household consumption and investments weigh down aggregate demand

Household expenditures, which accounted for 70.1 percent of GDP in Q2 2020, contracted by 15.5 percent in Q2 2020 from the 0.2-percent and 5.6-percent expansions in Q1 2020 and Q2 2019, respectively. The substantial decline in household spending was due to the stringent lockdown measures and travel restrictions imposed beginning mid-March, with varying levels of community quarantine in the succeeding months to prevent the transmission of COVID-19.

Additionally, the unprecedented increase in unemployment, loss in income, and drop in foreign remittances in Q2 2020 also affected the households' purchasing power. This resulted in the double-digit contractions in consumption of most commodities except for essential items particularly food and non-alcoholic beverages, housing, water, electricity, gas and other fuels, and communication.

Government expenditures grew by 22.1 percent in Q2 2020, significantly higher than the 6.8-percent and 7.0-percent growth in Q2 2019 and Q1 2020, respectively. The increase in government expenditures was attributed to the various programs to support the Filipinos adversely affected by the pandemic. In particular, the government's maintenance and other operating expenses rose by 120.8 percent in Q2 2020 following the implementation of various COVID-19 emergency measures pursuant to the Bayanihan to Heal as One Act (R.A. 11469). These include ₱37 billion grants to local government units (LGUs), ₱205 billion for the social amelioration program, ₱51 billion for the small business wage subsidy, and about ₱50 billion in health-related expenses for test kits, quarantine facilities, personal protective equipment, ventilators, x-ray machines, among others.

Moreover, expenditures on personnel services grew by 12.8 percent in Q2 2020 due to the increased hiring of health personnel and filling of positions in various agencies. The first tranche of the Salary Standardization Law of 2019 (R.A. 11466) and the release of the mid-year bonus of government personnel were also implemented in May 2020.

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

BY EXPENDITURE ITEM	2019	2020	
	Q2	Q1	Q2
Household Consumption	5.6	0.2	-15.5
Government Consumption	6.8	7.0	22.1
Capital Formation	-0.8	-17.4	-53.5
Fixed Capital Formation	-2.9	-4.4	-37.8
Exports	3.1	-4.4	-37.0
Imports	0.1	-8.7	-40.0

Source: PSA

Overall exports went down by 37.0 percent in Q2 2020 from -4.4 percent in Q1 2020 due mainly to the contraction in exports of services (-43.4 percent in Q2 2020 from -5.0 percent in Q1 2020). The Department of Tourism estimated foreign tourist arrivals to have decreased by 68.0 percent in the first half of 2020 due to the travel restrictions and quarantine measures imposed worldwide amid the COVID-19 pandemic. Merchandise exports also sustained its downtrend largely due to the contraction of sales for semiconductors and most export items as the health crisis dampened global economic activity. Overall imports declined further by 40.0 percent in Q2 2020, from the 8.7-percent contraction in Q1 2020. The continued downtrend in imports of goods was due largely to the substantial drop in merchandise imports. Likewise, imports of services weakened during Q2 2020, except for telecoms and government services.

Other Demand Indicators.[12] High-frequency demand indicators continue to suggest a below-optimal domestic activity in the near term. Composite PMI in September 2020 showed a slight improvement but remained below the 50-point expansion threshold while volume and value of production orders in the manufacturing sector continue to deteriorate. Other data indicators point to continued weak demand-as well, such as sales of new vehicles and energy consumption. Moreover, real estate values in key business districts are easing while vacancy rates are increasing.

Property Prices

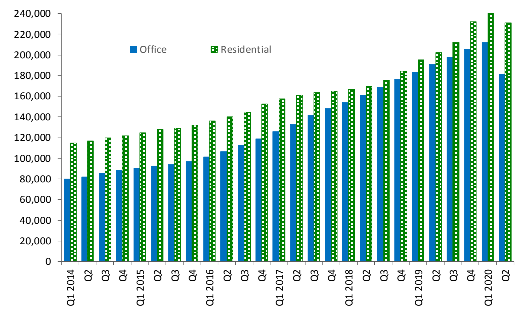
Capital Values, Metro Manila. Average capital values[13] for office buildings in Metro Manila[14] in Q2 2020 declined to ₱181,316/sq.m., lower by 4.9 percent and 14.5 percent compared to the year- and quarter-ago levels, respectively. The decline was due mainly to the decrease in capital values for office buildings in major business hubs in Metro Manila such as the Makati Central Business District (CBD), Ortigas Center, Fort Bonifacio, and Manila Bay Area.

Capital values for residential buildings increase y-o-y, but decrease q-o-q

Meanwhile, average capital values for luxury residential buildings[15] in Metro Manila[16] in Q2 2020 reached ₱230,900/sq.m., higher by 14.2 percent y-o-y but lower by 6.1 percent q-o-q.

In terms of location, three-bedroom luxury residential condominium units in Makati CBD, Fort Bonifacio, and Ortigas Center recorded increases in capital values compared to the same period last year.

Chart 8. Capital Values, Metro Manila
Price per square meter



Source: Colliers International Philippines

Rental Values, Metro Manila.[17] Average monthly office rents in Metro Manila reached ₱968/sq.m. in Q2 2020, which decreased by 6.0 percent from the previous quarter. This was also lower by 1.7 percent relative to Q2 2019. The depreciation in office rental rates was due to the reduced demand from offshore gaming, outsourcing, and traditional firms.

Rental values for office and residential spaces decrease

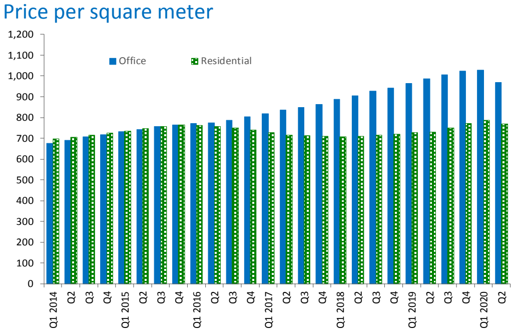
[12] There were no surveys conducted for Q2 2020 Business Expectations Survey and Consumer Expectations Survey.
[13] Probable price that the property would have fetched if sold on the date of the valuation. The valuation includes imputed land and building value.
[14] This includes Makati CBD, Fort Bonifacio,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

[15] 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.
[16] This includes Makati CBD, Fort Bonifacio, Ortigas, Eastwood, and Rockwell.
[17] 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.

Average monthly rents for luxury three-bedroom condominium units in Metro Manila was recorded at ₱770/sq.m. in Q2 2020, lower by 2.0 percent compared to the previous quarter but 5.5 percent higher compared to year-ago levels. The q-o-q slowdown in rents in Metro Manila could be attributed to the lesser demand from foreign and local employees, especially in business districts.

Chart 9. Rental Values, Metro Manila

Price per square meter



Source: Colliers International Philippines

Vacancy Rates, Metro Manila. The overall office vacancy rate in Metro Manila went up to 4.9 percent in Q2 2020 from 4.1 percent in the Q1 2020 due mainly to slower leasing from all segments and a rise in vacated spaces.

Vacancy rates for offices and residences increase

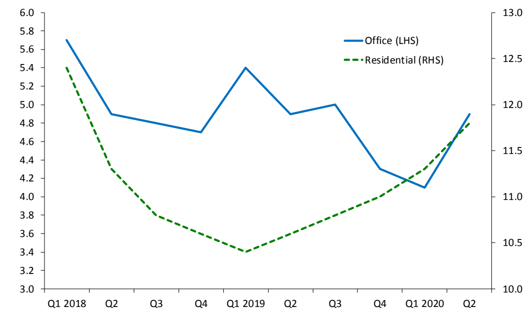
In terms of location, the office vacancy rates in Makati CBD (1.8 percent from 1.7 percent), Fort Bonifacio (3.9 percent from 3.4 percent), and Ortigas Center (5.3 percent from 4.1 percent) increased in Q2 2020 compared to the previous quarter. By contrast, office vacancy rates in Manila Bay Area (4.8 percent from 4.9 percent) slightly declined in Q2 2020 compared to the previous quarter.

Following the adverse impacts of the pandemic and community quarantine, higher office vacancy rate is expected in 2020 due mainly to slowdown in leasing activities, weak demand, and a cautious market. With the rise in vacancy and a greater leeway for rent negotiations and concessions, according to Colliers, rent will decline in 2020 before recovering in 2021.[18]

Meanwhile, the overall residential vacancy rate in Metro Manila increased to 11.8 percent in Q2 2020 from 11.3 percent in Q1 2020 due to the slower take-up of units in areas near the core business districts. In particular, residential vacancy rates were higher in Makati CBD (11.4 percent from 11.1 percent), Fort Bonifacio (15.9 percent from 15.2 percent), Rockwell Center (10.4 percent from 10.2 percent), Ortigas Center (4.9 percent from 4.6 percent), Eastwood City (4.6 percent from 4.4 percent), and Manila Bay area (14.1 percent from 13.2 percent).

Chart 10. Vacancy Rates

In percent



Source: Colliers International Philippines

The condominium market is starting to feel the adverse impact of the pandemic and lockdown measures. Colliers sees a drop in condominium completions and an appetite for both existing and pre-selling units. Moreover, according to Colliers, the full impact of the pandemic may be more apparent in the second half of 2020. The government-projected economic recovery in 2021 is likely to help boost residential leasing and sales in Metro Manila.

[18] Q2 2020 Colliers Report

BSP Residential Real Estate Price Index (RREPI).[19] Residential real estate prices of various types of housing units nationwide rose by 27.1 percent y-o-y in Q2 2020 based on the RREPI. This is the highest y-o-y growth rate recorded since the start of the series in Q1 2016.

Residential real estate prices continue to rise

Respondent banks cited the following reasons for the uptick in real estate prices in Q2 2020: higher demand for high-end projects, which drove the average price per square meter upwards; and rising prices of construction materials, labor costs, and other indirect costs (e.g., higher marketing costs of appraised premium properties). Furthermore, in terms of area and type of housing unit, the highest contributors to the increase in housing prices were loans for the purchase of condominium units, particularly those in the NCR and single attached/detached houses. Likewise, low base effects contributed to the price growth.

By area, residential property prices increased y-o-y in both the NCR and in Areas Outside the NCR (AONCR). Residential property prices in NCR rose by 34.9 percent in Q2 2020 relative to the same period in 2019, which is higher than the 18.1-percentgrowth in AONCR. In NCR, all types of housing units registered an increase in prices, except for duplexes as no loans for the purchase of duplexes in the said area were granted and reported in Q2 2020. Similarly, prices in AONCR increased across all types of housing units.

[19] 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

Quarter	Residential Real Estate Price Index [1] (By Housing Type)				
	Overall [2]	Single Detached/ Attached	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
Q2	149.4	125.0	112.3	148.4	197.5
	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
Q2	27.1	24.1	0.8	10.8	30.1
	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
Q2	10.7	10.5	-32.9	4.7	10.0

[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: BSP

In Q2 2020, the purchase of new housing units accounted for 84.8 percent of residential real estate loans (RRELs). Meanwhile, by type of housing unit, more than half of residential property loans were used for the acquisition of condominium units (62.7 percent), followed by single attached/detached houses (32.1 percent), and townhouses (4.8 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/attached houses. By region, NCR accounted for more than half (58.6 percent) of the total number of RRELs granted in Q2 2020, followed by CALABARZON (21.0 percent), Central Luzon (5.5 percent), Western Visayas (3.3 percent), Central Visayas (3.2 percent), Davao Region (2.5 percent) and Northern Mindanao (1.9 percent). NCR and these six other regions combined accounted for 96.0 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

Quarter	Residential Real Estate Price Index [1] (By Area)		
	Overall	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
Q2	149.4	178.3	130.8
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
Q2	27.1	34.9	18.1
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
Q2	10.7	13.8	6.6

[1] Based on bank reports on residential real estate loans granted per BSP Circular No. 892 dated 16 November 2015.

Source: BSP

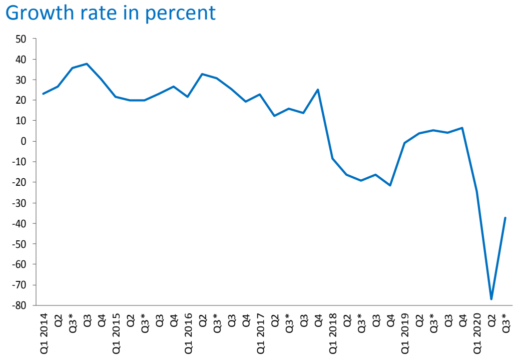
Vehicle Sales. The sales of new vehicles from CAMPI-TMA[20] members decreased by 37.4 percent y-o-y for the period July-August 2020, a turnaround from the 5.2-percent expansion recorded in the same period in 2019. The decline was due mainly to lower sales of passenger and commercial vehicles amid a stricter lockdown for two weeks[21] during the period.

New vehicle sales decline

Commercial vehicle sales, which account for about 69.8 percent of total vehicle sales, went down by 37.9 percent y-o-y for the period July-August 2020 from the 1.2-percent increase in the same period in 2019. Commercial vehicles sold during the period reached 26,837 units from 43,231 units in the same period a year ago.

Chart 11. Vehicle Sales

Growth rate in percent



* July to August

Source: Chamber of Automotive Manufacturers of the Philippines, Inc. (CAMPI)

Similarly, passenger car sales decreased by 36.1 percent y-o-y for the period July-August 2020, a reversal from the 16.1-percent growth in the same period in 2019. New passenger car sales accrued to a total of 11,611 units for the period July-August 2020 from 18,178 units in the same period a year ago.

[20] 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.

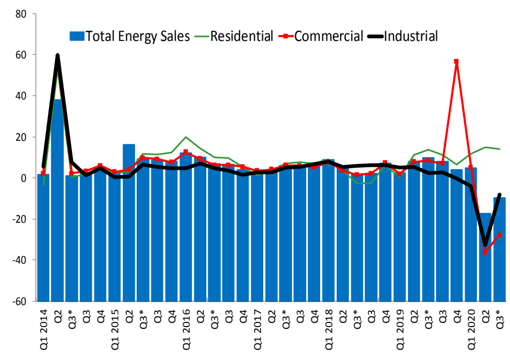
[21] Metro Manila and nearby provinces were once again placed under MECQ for the first two weeks of August in an attempt to curb the rise in coronavirus cases.

Energy Sales. Energy sales of Meralco contracted by 9.5 percent y-o-y in Q3 2020 (July-August), a reversal from the 9.8-percent growth in the same period a year-ago.

Energy sales contract in Q3 2020

The contraction in Q3 2020 still reflects the impact of the implementation of the quarantine protocols in Meralco's service area. Energy sales from the residential sector increased by 14.1 percent, while energy sales from the commercial sector and industrial sectors contracted by 27.7 percent and 8.2 percent, respectively.

Chart 12. Energy Sales
Year-on-year growth in percent



* July to August
Source: Meralco, BSP calculations

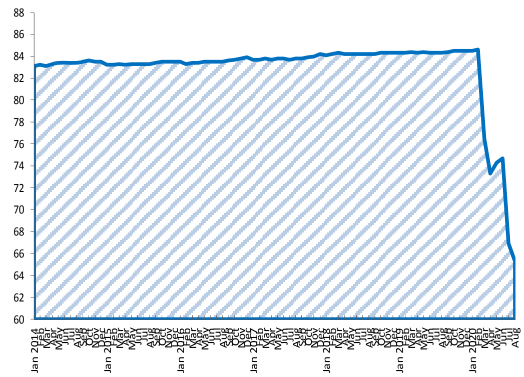
Capacity Utilization. The average capacity utilization rate of the manufacturing sector stood at 65.3 percent in August 2020, lower than the month-ago level at 66.9 percent (revised) based on the Philippine Statistics Authority's Monthly Integrated Survey of Selected Industries (MISSI).

Utilization rate in August 2020 remains below optimal capacity

The last time that average capacity utilization rate declined below 80-percent optimal capacity was in February 2009 at 78.5 following the global financial crisis. Of the 498 respondent-establishments, only 38.4 percent operated at a capacity of at least 80.0 percent in August 2020.

The 498 respondents are significantly lower than the July level at 627 firms (revised), and only takes account for about 55.8 percent of the 893 sample establishments.

Chart 13. Monthly Average of Capacity Utilization for Manufacturing
In percent



Source: PSA

Firms managed to show improvement in business activities despite operating at limited capacity amid the MECQ implementation in key business areas (i.e., Metro Manila, Laguna, Cavite, Rizal, and Bulacan) from 4 to 18 August 2020, and general community quarantine thereafter. Only seven (out of 20) major industries in the sector operated at least at the 80-percent capacity level that include the following: machinery except electrical (87.9 percent), rubber and plastic products (84.7 percent), printing (84.4 percent), paper and paper products (82.5 percent), electrical machinery (81.7 percent), textiles (81.3 percent), and furniture and fixtures (80. 4percent). Meanwhile, six major industries (from the previous month's 9 industries) operated at the 70-79 percent capacity range namely, non-metallic mineral products (77.3 percent), wood and wood products (76.6 percent), food manufacturing (76.5 percent), leather products (75 percent), transport equipment (72.9 percent), and beverages (70.7 percent). Meanwhile, the petroleum industry operated at 0.1 percent capacity in August as the refineries reportedly shut down operations to do maintenance work.

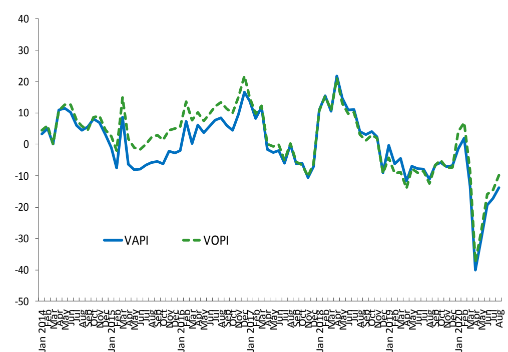
Volume and Value of Production. Preliminary MISSI data for August 2020 continued to decline at a slower pace in both volume and value indices, an improvement for the fourth consecutive month, indicative that the Philippine economy is on the road to recovery. However, the implementation of stricter quarantine measures in key business areas during the first half of August weighed down on firms' average capacity utilization as it deteriorated further from month-ago level.

Preliminary results of the MISSI showed that volume of production index (VoPI) declined by 9.9 percent y-o-y in August 2020 from a deeper contraction of 14.6 percent (revised) in July.

Manufacturing output continues to deteriorate

Of the 20 major industries, 18 sub-sectors posted negative growth rates: petroleum products (-96.2 percent), electrical machinery (-18 percent), machinery except electrical (-34 percent), transport equipment (-36.8 percent), food manufacturing (-5.6 percent), footwear and wearing apparel (-30.2 percent), tobacco products (-38.7 percent), non-metallic mineral products (-22.6 percent), beverages (-13 percent), printing (-42.3 percent), textiles (-24.2 percent), furniture and fixtures (-37.8 percent), rubber and plastic products (-10.2 percent), fabricated metal products (-15.4 percent), paper and paper products (-9.8 percent), wood and wood products (-31.3 percent), leather products (-60.3 percent), and miscellaneous manufactures (-0.5 percent).

Chart 14. Volume and Value Indices of Manufacturing Production
Year-on-year in percent



Source: PSA

Likewise, the value of production index (VaPI) posted a 13.8-percent drop in August 2020 from a 17.2-percent (revised) decline in the previous month. This was attributed to the deceleration of 18 out of 20 sub-sectors: petroleum products (-96.6 percent), machinery except electrical (-38.5 percent), electrical machinery (-20.2 percent), transport equipment (-43.5 percent), footwear and wearing apparel (-35.7 percent), food manufacturing (-4.6 percent),tobacco products (-36.6 percent), non-metallic mineral products (-23.7 percent), printing (-43.1 percent), textiles (-25.1 percent), beverages (-8.5 percent), paper and paper products (-18.9 percent), rubber and plastic products (-12.4 percent), fabricated metal products (-15.4 percent), furniture and fixtures (-27.5 percent), wood and wood products (-35.8 percent), leather products (-62.1 percent), and miscellaneous manufactures (-4.4 percent).

Business Expectations. Business confidence on the economy turned negative in Q3 2020, after posting 43 quarters of optimism (from Q3 2009 to Q1 2020), as the overall confidence index (CI)[22] of the Business Expectations Survey (BES)[23] registered at -5.3 percent from 22.3 percent in Q1 2020.[24] The negative reading indicated that respondents with a negative outlook outnumbered those with a positive outlook.

Business sentiment turns pessimistic in Q3 2020

The respondents' pessimism for Q3 2020 was attributed to the impact on the business outlook of the COVID-19 pandemic as well as the community quarantine restrictions; decrease in orders, sales, and income; slowdown/temporary shutdown in business operations; and concerns over government policies, primarily on the perceived insufficient mitigation measures to counter the impact of COVID-19.

The sentiment of businesses in the Philippines mirrored the business outlook in Australia, which turned pessimistic. Further, business confidence in Denmark, Greece, Hungary, Mexico, and New Zealand was more pessimistic; while that of Chile, Croatia, Euro area, France, Hong Kong, Israel, Netherlands, Norway, South Korea, Thailand, and the United Kingdom was less pessimistic. However,

[22] The CI is computed as the percentage of firms that answered in the affirmative less the percentage of firms that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.
[23] The Q3 2020 BES was conducted during the period 8 July- 10 September 2020. There were 1,517 firms surveyed nationwide. Samples were drawn from the Top 7,000 Corporations ranked based on total assets in 2016 from the Bureau van Dijk (BvD) database, consisting of 586 companies in NCR and 931 firms in AONCR, covering all 16 regions nationwide.
[24] Due to the implementation of the Community Quarantine nationwide from 16 March to 31 May 2020, the conduct of the Q2 2020 BES was cancelled.

view of businesses in Brazil, Bulgaria, Canada, China, Germany, and the US was optimistic.

Table 8. Business Expectations Survey Current Quarter Next Quarter

BUSINESS OUTLOOK INDEX		Current Quarter	Next Quarter	Next 12 Months
2016	Q1	41.9	49.6	-
	Q2	48.7	45.3	-
	Q3	45.4	56.8	-
	Q4	39.8	34.5	-
2017	Q1	39.4	47.2	-
	Q2	43.0	42.7	-
	Q3	37.9	51.3	-
	Q4	43.3	39.7	-
2018	Q1	39.5	47.8	-
	Q2	39.3	40.4	-
	Q3	30.1	42.6	-
	Q4	27.2	29.4	-
2019	Q1	35.2	52.0	-
	Q2	40.5	47.6	-
	Q3	37.3	56.1	-
	Q4	40.2	40.3	59.6
2020	Q1	22.3	42.3	55.8
	Q2	-	-	-
	Q3	-5.3	16.8	37.5

Source: BSP

For the quarter ahead (Q4 2020), weak business sentiment persisted, with the next quarter CI moderating to 16.8 percent from 42.3 percent in the Q1 2020 survey results. Respondents' less buoyant outlook for Q4 2020 was associated mainly with expectations of the continuing negative effects of the COVID-19 pandemic affecting the volume of orders, sales, and income, and overall economic activity, in general. Similarly, business outlook on the country's economy was less upbeat for the next 12 months as the CI declined to 37.5 percent from 55.8 percent in Q1 2020 survey results due also to the aforementioned reasons.

Consumer Expectations.[25] The country's consumer outlook turned pessimistic for Q3 2020 as the overall CI[26] fell to a record low of -54.5 percent from 1.3 percent in Q1 2020.[27] A negative CI indicates that the number of pessimists exceeds the number of optimists for the review period.

Consumer confidence falls on pandemic-related uncertainty

Respondents attributed their negative sentiment for Q3 2020 generally to the COVID-19 pandemic. Other reasons cited by the respondents included high unemployment rate and less working family members; low and reduced income; and faster increase in the prices of goods.

Table 9. Consumer Expectations Survey Current Quarter Next Quarter Next 12 Months

CONSUMER OUTLOOK INDEX		Current Quarter	Next 3 Months	Next 12 Months
2016	Q1	-5.7	9.1	25.4
	Q2	-6.4	5.6	26.6
	Q3	2.5	27.3	43.8
	Q4	9.2	18.8	33.4
2017	Q1	8.7	16.5	31.7
	Q2	13.1	13.6	34.3
	Q3	10.2	17.8	33.7
	Q4	9.5	17.5	32.0
2018	Q1	1.7	8.8	24.0
	Q2	3.8	8.7	23.1
	Q3	-7.1	3.8	13.0
	Q4	-22.5	-0.8	10.7
2019	Q1	-0.5	10.7	28.4
	Q2	-1.3	9.7	25.2
	Q3	4.6	15.8	29.8
	Q4	1.3	15.7	26.4
2020	Q1	1.3	9.2	19.9
	Q2	-	-	-
	Q3	-54.5	-4.1	25.5

Source: BSP

The sentiment of consumers in the Philippines was comparable to the more pessimistic outlook of consumers in Australia, Euro area, and France for Q3 2020. Meanwhile, consumer outlook in Czech Republic, Indonesia, Japan, Poland, South Korea, Switzerland, Taiwan, Thailand, United Kingdom, and the US were less pessimistic.

Consumer pessimism continued for the next quarter (Q4 2020) as the CI moved into negative territory at -4.1 percent from the Q1 2020 survey result of 9.2 percent for Q2 2020. Apart from concerns over the COVID-19, consumers also cited anticipation of high unemployment rate; low, reduced, and no increase in income; and faster increase in the prices of goods as reasons behind their pessimistic outlook for Q4 2020. Meanwhile, consumers were more optimistic for the next 12 months as the CI increased to 25.5 percent from the Q1 2020 survey result of 19.9 percent for the next 12 months. The consumer outlook was more upbeat for the next 12 months due mainly to expectations of an end in the COVID-19

[25] The CES is a quarterly survey of a random sample of around 5,500 households in the Philippines. The Q3 2020 CES was conducted during the period 1-14 July 2020.
[26] The CI is computed as the percentage of households that answered in the affirmative less the percentage of households that answered in the negative with respect to their views on a given indicator. A positive CI indicates an optimistic outlook while a negative CI indicates a pessimistic outlook.
[27] Due to the implementation of the Community Quarantine nationwide from 16 March to 31 May 2020, the conduct of the Q2 2020 BES was cancelled.

pandemic or return to normal as well as the consumers' anticipation of availability of more jobs, additional or high income, and stable prices of goods.

Purchasing Managers' Index.[28] The preliminary composite PMI in September 2020 remained below the 50-point expansion threshold[29] at 43.4 slightly higher than the August PMI of 42.4. The slower contraction of the services sector more than offset the faster contraction of the manufacturing sector and retail and wholesale sector. This may be attributed to the gradual easing of lockdown restrictions in September from the stricter quarantine measures a month ago. Respondent-firms expect favorable business environment in October.

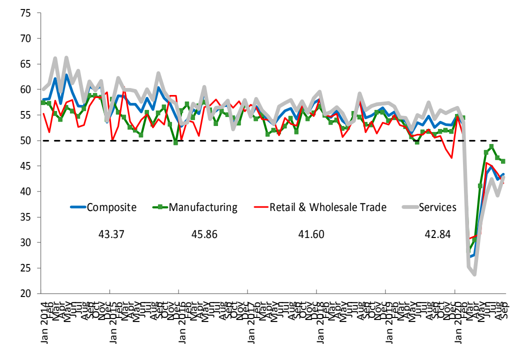
Composite PMI below optimal but registers slight improvement

The services PMI increased by 3.6 index points to 42.8 in September from 39.2 in August, in line with respondents' expectations of a higher PMI. All the indices in review recorded slower contraction during the month, except the Employment Index, indicative that businesses had the opportunity to re-open after suffering from the MECQ implementation in key business areas last month. In particular, demand for services improved, evident in the higher PMIs of Business Activity Index and New Orders Index. Outstanding Business Index – which measures work in progress but not yet completed – also posted a higher PMI. The average price charged to all services also increased month-on-month (m-o-m). Survey respondents anticipate favorable outcome for the sector in October.

By contrast, the manufacturing PMI declined marginally by 0.6 index point to 45.9 in September 2020 from 46.5 a month ago, contrary with business managers' expectations of a turnaround. The sector decelerated in August and September, after increasing for four consecutive months, due mainly to muted demand amid the pandemic.

In particular, the New Orders Index – which is a measure of overall demand – shed 1.8 index points in September. Consequently, delivery lead time moved at a faster pace, as seen in the slower expansion of the Supplier Deliveries Index. By contrast, improvements were seen in Production, Inventory, and Employment. Meanwhile, firms are optimistic about the sector's performance next month.

Chart 15. Purchasing Managers' Index



Source: Philippine Institute of Supply Management (PISM)

Similarly, the retail and wholesale PMI decreased by 1.9 index points to 41.6 in September from 43.5 in the previous month, which is contrary with managers' expectations. All the indices contracted at a faster pace, except for the Employment Index which gained 1.3 index points m-o-m following the re-opening of the economy. Meanwhile, managers are anticipating an improvement for the retail and wholesale sector in the month ahead.

External Demand[30]

Exports. Export of goods went down by 29.2 percent y-o-y in Q2 2020, lower than the 5.1-percent contraction in Q1 2020 and a reversal from the 2.9-percent expansion in Q2 2019.

Goods exports contract in Q2 2020

The lower outbound shipments of coconut products, sugar products, fruits and vegetables, other agro-based products, forest products, mineral products, and manufactures outpaced the growth in exports of petroleum products in Q2 2020.

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

[29] 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.

[30] International Merchandise Trade Statistics (IMTS) concept

Table 10. Export of Goods
Growth rate in percent, year-on-year

COMMODITY GROUP	2019 Q2	2020 Q1	2020 Q2
Coconut Products	-3.3	1.5	-28.4
Sugar and Products	139.2	10.3	-60.0
Fruits and Vegetables	49.4	20.4	-15.7
Other Agro-Based Products	-4.0	-7.9	-14.2
Forest Products	37.0	-16.2	-44.9
Mineral Products	17.2	5.6	-9.7
Petroleum Products	-92.4	13.6	713.1
Manufactures	1.3	-6.7	-31.6
Special Transactions	-9.3	-30.4	-46.8
Total Exports	**2.9**	**-5.1**	**-29.2**

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

Imports. Import of goods fell by 43.4 percent y-o-y in Q2 2020, a further decline from the 13.6-percent and the 1.9-percent contraction in Q1 2020 and Q2 2019, respectively.

Merchandise imports decline in Q2 2020

The reduction 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 11. Import of Goods
Growth rate in percent, year-on-year

COMMODITY GROUP	2019 Q2	2020 Q1	2020 Q2
Capital Goods	4.2	-14.7	-41.2
Raw Materials and Intermediate Goods	-11.0	-13.6	-33.3
Mineral Fuels and Lubricants	4.5	-12.4	-74.8
Consumer Goods	2.9	-12.1	-46.1
Special Transactions	51.1	-12.5	-38.6
Total Imports	**-1.9**	**-13.6**	**-43.4**

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

Aggregate Supply

On the production side of the economy, growth emanated from agriculture, which contributed 0.1 ppt. Meanwhile, the industry and services sectors shrank by -6.9 ppt and -9.7 ppt, respectively, to total GDP growth in Q2 2020.

Services and industry sectors contract supply-side activity

The agriculture sector expanded by 1.6 percent in Q2 2020, a turnaround from the 0.3-percent decline in Q1 2020 and higher than the 0.7-percent increment in Q2 2019. The growth in agricultural output was primarily on account of increased production of palay (7.2 percent in Q2 2020 from -1.9 percent in Q1 2020), corn (15.6 percent from -4.4 percent), and sugarcane (76.0 percent from 8.9 percent). The increased output of these crops made up for 8.5 percent and 4.7 percent contractions in the livestock and poultry sectors, respectively. Favorable weather conditions, which supported good crop and fisheries yields, the accelerated implementation of the Rice Competitiveness Enhancement Fund (RCEF) program as well as other agricultural production and marketing support towards ensuring food security during the pandemic also contributed to the increase in total agricultural output during the period.

Table 12. Gross Domestic Product by Industrial Origin
At constant 2018 prices; growth rate in percent

BY INDUSTRIAL ORIGIN	2019 Q2	2020 Q1	2020 Q2
Agri., Hunting, Forestry and Fishing	0.7	-0.3	1.6
Industry Sector	2.5	-3.4	-22.9
Mining and Quarrying	14.2	-21.0	-24.5
Manufacturing	2.0	-3.8	-21.3
Electricity, Gas and Water Supply			
Construction	-0.1	-2.9	-33.5
Service Sector	7.5	0.6	-15.8
Wholesale and Retail Trade and Repair of Motor Vehicles and Motorcycles	8.6	1.9	-13.1
Transportation and Storage	6.1	-11.4	-59.2
Accomodation and Food Service Activities	4.9	-16.4	-68.0
Information and Communcation	5.6	5.1	6.6
Financial and Insurance Activities	10.7	9.1	6.8
Real Estate and Ownership of Dwellings	4.9	-2.3	-20.1
Professional and Business Services	3.0	0.2	-18.4
Public Administration and Defense; Compulsory Social Security	11.4	5.5	8.3
Education	12.0	1.1	-12.2
Human Heath and Social Work Activities	-0.6	4.7	-15.4
Other Services	6.6	-10.6	-63.0

Source: PSA

The industry sector declined further by 22.9 percent in Q2 2020, from the 3.4-percent contraction in Q1 2020. This was attributed to the weaker performance of the manufacturing, construction, electricity, steam, water and waste management, and mining and quarrying subsectors. The manufacturing sector contracted by 21.3 percent in Q2 2020, down from the 3.8-percent decline in Q1 2020. Nearly all subsectors posted double-digit negative growth, including export-oriented manufactures such as computer, electronic and optical products, basic metals, and transport equipment. Despite being categorized as essential industries, manufacture of food products, chemical and chemical products, and beverages also declined on account of subdued global and domestic demand. Mining and quarrying sector fell by 24.5 percent in Q2 2020, sharper than the 21.0 percent dropped in Q1 2020. This was largely due to the substantial decline in stone quarrying, nickel, gold, and crude petroleum and natural gas production. Electricity, steam, water and waste management contracted by 5.8 percent in Q2 2020, a reversal from the 4.9 percent growth in Q1 2020, due mainly to the contraction in electricity. Meralco and the National Grid Corporation of the Philippines (NGCP) both reported lower income generated in Q2 2020. Construction continued to decline in Q2 2020 by 33.5 percent from -0.1 percent in Q2 2019 and -2.9 percent in Q1 2020. The slowdown in private and government construction projects could be attributed to the temporary discontinuation of construction activities during the ECQ and MECQ periods.

Services declined by 15.8 percent in Q2 2020 from the 0.6-percent growth posted in Q1 2020. This was due primarily to the significant drop in almost all subsectors excluding finance, public administration, and information and communication. Trade and repair of motor vehicles, motorcycles, and personal and household goods weakened further to -13.1 percent in Q2 2020 from 1.9 percent in Q1 2020. All subsectors contracted during the reference period, with substantial declines noted in retail trade, wholesale trade, and sale and repair of motor vehicles. The lower performance of sale and repair of motor vehicles and motorcycles reflected the double-digit drop in both passenger car sales and commercial vehicles in Q2 2020, as well as the impact of mobility restrictions on transport demand. Transport and storage segment fell by 59.2 percent in Q2 2020 from the 11.4-percent contraction in Q1 2020. In particular, land transport, air transport, water transport, and warehousing and storage registered significant declines attributed to the imposition of community quarantine measures in different parts of the country. Accommodation and food service activities dropped sharply by 68.0 percent in Q2 2020 from -16.4 percent in Q1 2020. The continued downtrend was due mainly to the substantial contractions in food and beverage service activities and accommodation during the quarantine period. Financial and insurance activities decelerated to 6.8 percent in Q2 2020, slower than the 9.1-percent growth in Q1 2020. This was largely stemmed from the decline in non-bank financial intermediation, insurance, and slowdown in auxiliary activities. Real estate and ownership of dwellings contracted further by 20.1 percent in Q2 2020 from -2.3 percent in Q1 2020. Major real estate companies reported significant declines in rental income and sales due to waived rental fees, lower collection and lower completion of projects during the quarantine period. Professional and business service activities registered an 18.4-percent contraction in Q2 2020, lower than the 0.2-percent and 3.0-percent increments in Q1 2020 and Q2 2019, respectively. The contraction in the performance of the subsector was attributed to the implementation of community quarantine measures which halted business operations in major business hubs particularly Metro Manila, CALABARZON, and Cebu City. The education sector was down by 12.2 percent in Q2 2020, from the 1.1-percent growth in Q1 2020. This was due to the schools being unable to offer summer or mid-year classes given the quarantine restrictions, uncollected tuition fee balances, decline in enrolment for the school year 2020-2021, and students transferring from private to public learning institutions. Growth in health and social work sector dropped by 15.4 percent in Q2 2020, down from the 4.7-percent growth in Q1 2020 due to the contraction in private health, which offset the gains in social work and public health. The contraction in other services deepened to -63.0 percent in Q2 2020 from -10.6 percent in Q1 2020. Activities related to arts, entertainment and recreation and other service activities were restricted during the reference quarter to prevent mass gatherings and non-essential activities amid the pandemic.

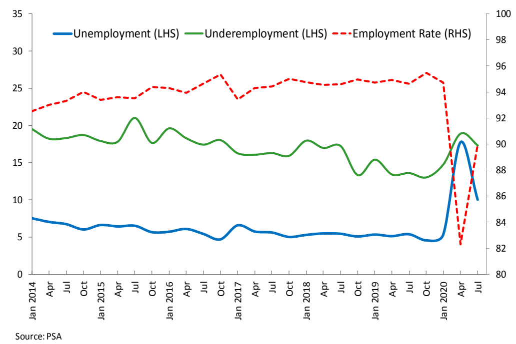
Labor Market Conditions

Results of the July 2020 labor force survey (LFS) showed that, compared to the same period a year ago, the country's employment rate dropped to 90.0 percent (from 94.6 percent), unemployment rate rose to 10.0 percent (from 5.4 percent), underemployment rate increased to 17.3 percent (from 13.6 percent), and youth unemployment rate surged to 22.4 percent (from 14.7 percent).

Employment conditions deteriorate in Q3 2020

However, relative to April 2020 when labor market conditions deteriorated considerably, the quantity and quality of employment improved in the July survey round, with the gradual resumption of economic activities.[31] As a result, unemployment rate in the first three quarters of 2020 averaged 11.0 percent, which is at the low end of the 11.0-13.0 percent unemployment rate projection of the government for the year.[32]

Chart 16. Unemployment, Underemployment and Employment Rate
in percent

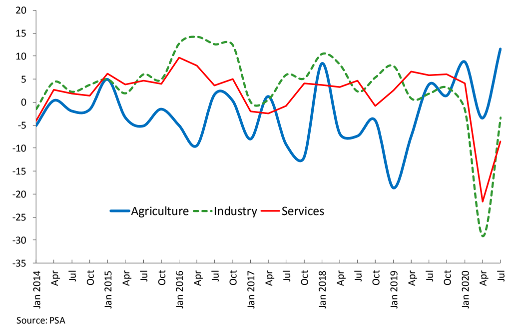


The lower employment rate in July 2020 was equivalent to 41.3 million employed individuals, 2.9 percent lower compared to 42.5 million employed persons in the same period a year ago. Employment in the agriculture sector bounced back with 2.7 percent growth, which helped offset lower employment in services and industry sectors. Employment in the services sector contracted by 4.9 percent, mainly due to lower employment in accommodation and food service activities, other service activities, and transportation and storage. Employment in the industry sector also declined by 0.6 percent largely on account of the manufacturing subsector. Notwithstanding, some subsectors under these two major sectors benefited from less stringent quarantine measures during the quarter, particularly, wholesale and retail trade, mining and quarrying and construction.

[31] In July 2020, employment rate improved to 90.0 percent, from 82.3 percent in April 2020; unemployment rate declined to 10.0 percent from 17.7 percent in the previous quarter; underemployment rate dropped to 17.3 percent from 18.9 percent, and youth unemployment rate fell to 22.4 percent from 31.6 percent.

[32] Development Budget Coordination Committee (2020), "Table A.1. Macroeconomic Parameters, 2019-2022," Budget of Expenditures and Sources of Financing FY 2021.

Chart 17. Employment by Sector
in percent



The double-digit unemployment rate in July 2020 translated to 4.6 million unemployed individuals or an 87.5 percent increase during the quarter.

Unemployment registers double-digit rate

In terms of educational attainment, majority of the unemployed were junior high school graduates (27.8 percent) and college graduates (24.8 percent share). In terms of age, majority of unemployed reverted to the 15-24 age group or the youth (38.0 percent), followed by 25-34-year-old age group (30.8 percent). The number of unemployed youth increased by 55.4 percent during the period.

The reduced number of work hours caused by lower domestic demand contributed to higher underemployment rate during the period, with higher share of the visibly underemployed and the lower share of the invisibly underemployed. Similar to April 2020, other aspects of employment quality worsened in July 2020. The share of remunerative work or wage and salary workers declined to 60.4 percent in July 2020 from 63.9 percent a year ago. Moreover, the overall mean hours of work[33] fell from 41.8 in July 2019 to 38.2 in July 2020. The nature of work and enhanced community quarantine are the principal reasons for working less than 40 hours per week in July 2020.

To improve the country's employment condition, the government intends to open the economy further while expediting the implementation of its recovery program, particularly the Bayanihan 2 and the Build, Build, Build infrastructure program.

[33] Hours per week.

II. Monetary and Financial Market Conditions

Domestic Liquidity

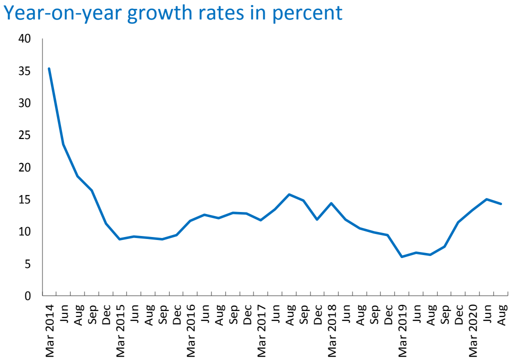
Domestic liquidity (M3) grew by 14.2 percent y-o-y in August 2020 to ₱13.6 trillion, slower than the 15.0-percent (revised) expansion as of end-Q2 2020.

Domestic liquidity continues to expand in August

Demand for credit remained the principal driver of money supply growth. Domestic claims rose by 10.6 percent in August from 13.3 percent as of end-Q2 2020 due to the sustained growth in credit to the private sector. Meanwhile, net claims on the central government increased by 49.8 percent in August, slower than the 53.4-percent growth as of end-Q2 2020. This reflects partly the government's continued funding requirement for its efforts against the COVID-19 pandemic.

Chart 18. Domestic Liquidity

Year-on-year growth rates in percent



Source: BSP

Net foreign assets (NFA) in peso terms grew by 17.8 percent y-o-y in August from a growth of 15.7 percent in end-Q2 2020. The expansion in the BSP's NFA position reflected the increase in gross international reserves (GIR). Meanwhile, the growth in the NFA of banks accelerated, as banks' foreign assets rose on account of higher interbank loans and deposits with other banks.

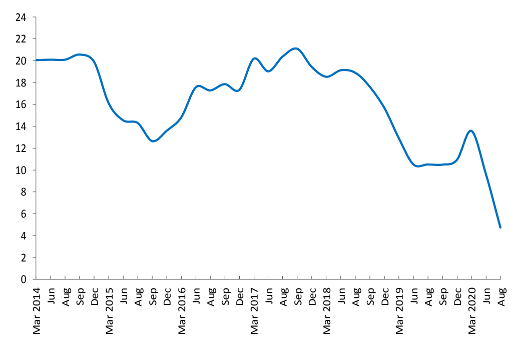
Outstanding loans of commercial banks, net of RRP placements with the BSP, increased by 4.7 percent y-o-y in August 2020, slower than the 9.6-percent growth rate posted at end-Q2 2020 and the 10.5-percent growth rate reported in end-Q3 2019. Bank lending growth moderated during the quarter as a result of weaker corporate sector performance, declining loan demand, and risk aversion among banks.

Bank lending growth eases amid decline in production activities

Loans for production activities increased by 4.2 percent y-o-y in August 2020 from 8.2 percent in end-Q2 2020 and 9.0 percent in end-Q3 2019. Lending to key sectors, particularly manufacturing activities as well as wholesale and retail trade and repair of motor vehicles and motorcycles declined further in August.

Chart 19. Loans Outstanding of Commercial Banks

Year-on-year growth rates in percent



Source: BSP

Meanwhile, growth in loans for households decelerated to 12.9 percent in August 2020 from 27.0 percent in end-Q2 2020 and 26.2 percent in end-Q3 2019, following the continued slowdown in credit card, motor vehicle, and salary-based general purpose consumption loans.

Monetary Operations

As of end-Q3 2020, total outstanding amount absorbed in the BSP liquidity facilities stood at ₱1.8 trillion. Bulk of the BSP's liquidity-absorbing monetary operations had been through the term deposit facility (TDF) and the overnight deposit facility (ODF), comprising about 80.2 percent of the combined outstanding amount of liquidity absorbed through the BSP liquidity facilities. Meanwhile, placements in the reverse repurchase agreement or RRP facility and BSP Securities facility (BSP-SF) made up 17.0 percent and 2.8 percent, respectively.

Following the reduction in scale of its monetary operations for liquidity absorption in response to the COVID-19 crisis for the most part of Q2 2020, the BSP started reconfiguring its monetary operations beginning on 10 June 2020 amid improvements in the domestic liquidity conditions and market functioning. In particular, the BSP gradually re-offered the other tenors in the TDF, beginning with the re-opening of the 14-day TDF on 10 June followed by the 28-day TDF on 1 July. At the same time, the BSP increased the daily RRP offer volume at a measured pace from ₱100 billion to ₱200 billion for the period 10 June – 7 July 2020 and back to its pre-ECQ level at ₱305 billion starting on 8 July 2020.

Given the reconfiguration of BSP's monetary operations which started on 10 June 2020, the average weekly total offer volume in the TDF auctions was higher at about ₱292.2 billion in Q3 2020 relative to ₱131.5 billion average weekly volume offered in the previous quarter (covering 15 April - 24 June). The average bid-to-cover ratios for the 7-, 14-, and 28-day tenors were recorded at 1.5, 1.6, and 1.8. Meanwhile, the average bid-to-cover ratio for the daily RRP offerings was at around 4.0 during the quarter from 5.2 in Q2 2020.

Moreover, on 18 September 2020, the BSP successfully launched the BSP Securities as a new instrument for its monetary implementation. This marked the first time for the BSP to issue its own debt securities since its establishment in July 1993. The reinstatement of the BSP's authority to issue its own bills and bonds provides an additional instrument to enhance further the implementation of monetary policy. It is a purely operational refinement under the Interest Rate Corridor (IRC) system and does not represent any change in the BSP's current monetary policy stance.

Since its inception, market reception has been positive on the issuance of BSP Securities particularly on the 28-day BSP Bills (BSPB). For the period 18 September to 9 October, oversubscriptions were observed during the BSPB auctions, with average bid-to-cover ratio recorded at 2.010.

Credit Conditions

Credit Standards. Results of the Q3 2020 Senior Bank Loan Officers' Survey (SLOS)[34] showed almost the same portion of respondent banks reporting tighter and unchanged overall credit standards at close to 50 percent. For loans to enterprises, the percentage of respondent banks that reported tighter credit standards was only marginally higher than those that indicated unchanged overall credit standards during the quarter. Meanwhile, for loans to households, the percentage of respondent banks that reported maintained overall credit standards was only slightly higher than the portion that indicated tighter standards in Q3 2020.[35] The results for Q3 2020 survey reflected a slight improvement from the previous survey results where more than half of the respondent banks stated that they tightened credit standards amid the implementation of stricter quarantine measures due to the COVID-19 pandemic in Q2 2020.

Meanwhile, results based on the diffusion index (DI) approach,[36,37] indicated a net tightening of overall credit standards for both loans to enterprises and households in Q3 2020. In the previous quarter, overall credit standards for loans to businesses and households also showed a net tightening based on the DI approach.

[34] 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, 48 banks responded to the current survey representing a response rate of 75.0 percent.

[35] In the modal approach, the results of the survey are analyzed by looking at the option with the highest share of responses.

[36] 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").

[37] During the Q1 2010 to Q4 2012 survey rounds, the BSP used the DI approach in the analysis of survey results. Beginning in Q1 2013, the BSP used both the modal and DI approaches in assessing the results of the survey.

Respondent banks point to general tightening in credit standards

It should be noted that the period covered in the latest survey (Q3 2020) coincided with the government's implementation of general community quarantine (GCQ) measures in the NCR and various areas outside the NCR. The gathering of banks' responses for the SLOS was conducted between 2 September and 13 October 2020.

Lending to Enterprises. Almost half of the respondent banks (47.7 percent) indicated tighter overall credit standards for loans to enterprises during the quarter which resulted in a net tightening of lending standards based on the results using the DI approach. A comparable percentage of banks (45.5 percent), meanwhile, reported unchanged overall credit standards for the period. The net tightening of credit standards was also reflected across all borrower firm sizes, specifically, top corporations, large middle-market enterprises, small and medium enterprises (SMEs), and micro enterprises.

Table 13. General Credit Standards for Loans to Enterprises (Overall)

	2019				2020		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Tightened Considerably	2.1	4.8	4.1	0.0	2.8	20.4	20.5
Tightened Somewhat	22.9	11.9	12.2	15.2	30.6	49.0	27.3
Remained Basically Unchanged	**72.9**	**81.0**	**81.6**	**84.8**	**66.7**	**24.5**	**45.5**
Eased Somewhat	0.0	0.0	0.0	0.0	0.0	6.1	6.8
Eased Considerably	2.1	2.4	2.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Diffusion Index for Credit Standards	**22.9**	**14.3**	**14.3**	**15.2**	**33.3**	**63.3**	**40.9**
Number of Banks Responding	**48**	**42**	**49**	**46**	**36**	**49**	**44**

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").
Source: BSP

Respondent banks attributed the tightening of credit standards largely to less favorable economic outlook, deterioration in the profitability of bank's portfolio and profiles of borrowers, and reduced tolerance for risk, among other factors. In terms of specific credit standards, the net tightening of overall credit standards was manifested in terms of reduced credit line sizes; stricter collateral requirements and loan covenants; and increased use of interest rate floors. Meanwhile, some form of easing was observed in terms of narrower loan margins and longer loan maturities.

Over the next quarter, while most of the respondent banks expect to maintain overall credit standards for loans to enterprises, a large percentage also anticipate tighter credit standards on the back of a more uncertain economic outlook along with expected deterioration in borrowers' profiles and profitability of banks' portfolios, including banks' lower tolerance for risk.

Lending to Households. Half of the respondent banks (50.0 percent) kept their overall credit standards unchanged for loans extended to households during the quarter. At the same time, close to 50 percent of respondent banks indicated that they tightened their overall credit standards in Q3 2020. Consequently, the DI-based results showed a net tightening of credit standards for household loans as observed across all types of consumer loans, namely, housing, credit card, auto, and personal/salary loans. Respondent banks cited less favorable economic outlook, a deterioration in borrowers' profile, and a reduced tolerance for risk as the key factors that contributed to the overall tightening of credit standards for loans to households.

Table 14. General Credit Standards for Loans to Households (Overall)

	2019				2020		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3
Tightened Considerably	3.3	4.0	3.1	0.0	0.0	39.4	16.7
Tightened Somewhat	16.7	8.0	6.3	6.9	21.7	21.2	30.0
Remained Basically Unchanged	**73.3**	**88.0**	**81.3**	**89.7**	**69.6**	**33.3**	**50.0**
Eased Somewhat	3.3	0.0	9.4	3.4	8.7	6.1	3.3
Eased Considerably	3.3	0.0	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
Diffusion Index for Credit Standards	**13.3**	**12.0**	**0.0**	**3.4**	**13.0**	**54.5**	**43.3**
Number of Banks Responding	**30**	**25**	**32**	**29**	**23**	**33**	**30**

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").
Source: BSP

On specific credit standards, the overall net tightening of credit standards for loans to households was revealed in reduced credit line sizes, stricter collateral requirements and loan covenants, and increased use of interest rate floors by respondent banks. Nonetheless, some form of easing of credit standards was also noted across all types of loans to households in terms of narrower loan margins and longer loan maturities.

In terms of respondent banks' outlook for the next quarter, results based on both the modal and DI approaches pointed to expectations of tighter overall credit standards for household loans driven by uncertain economic outlook, expected deterioration in borrowers' profile, and lower risk tolerance of banks.

Loan demand. Survey results revealed mixed responses in terms of demand for business and consumer loans in Q3 2020. Most of the respondent banks observed an unchanged overall demand for loans from enterprises in Q3 2020. Meanwhile, the majority of respondent banks reported a decline in loan demand from households during the quarter. Similarly, DI-based results manifested mixed trends as the overall loan demand from enterprises pointed to a net increase (specifically for top corporations), while loan demand from households registered a net decline across all types of household loans.

The overall net increase in loan demand from firms was attributed by respondents to a decrease in clients' internally-generated funds and higher customers' inventory and capital financing needs, along with lack of other sources of funds. Meanwhile, respondent banks associated their observed decline in consumer loan demand largely to lower household consumption and housing investment.

Loan demand remains unchanged for firms; declines for households

Over the next quarter, most of the respondent banks expect broadly unchanged overall loan demand from both enterprises and households reflecting improved sentiments following the partial re-opening of the economy. Results based on the DI approach suggested expectations of a net increase in overall demand for business loans, associated largely with corporate clients' higher working capital requirements, a rise in customer inventory financing needs, a decline in clients' internally-generated funds, and lack of other sources of funds. DI-based results for loans extended to households, meanwhile, showed expectations of a net decline in overall demand including housing, auto, and personal/salary loans. The expected net decrease in demand for housing, auto, and personal/salary loans was attributed by respondent banks largely to lower household consumption and housing investment.

Real Estate Loans. Half of the respondent banks reported that overall credit standards for commercial real estate loans (CRELs) tightened while the other half reported unchanged overall credit standards in Q3 2020. DI-based results, meanwhile, continued to reflect a net tightening of overall credit standards for CRELs for the 19th consecutive quarter. Respondent banks cited a less favorable economic outlook, deterioration in borrowers' profile and profitability of banks' portfolio as well as a reduced tolerance for risk as the major reasons for the tightening of overall credit standards for CRELs. In terms of specific credit standards, the net tightening of overall credit standards for CRELs reflected reduced credit line sizes, stricter collateral requirements and loan covenants, wider loan margins, shortened loan maturities, and increased use of interest rate floors. Over the next quarter, most of the respondent banks anticipate tighter credit standards for CRELs.

Majority of banks tighten credit standards for real estate loans

Majority of the respondents reported unchanged demand for CRELs in Q3 2020, while DI-based results indicated a net decrease in loan demand. Over the next quarter, an equal number of respondent banks anticipate both a generally steady loan demand and a decline in demand for real estate loans. However, DI-based results pointed to expectations of a net decrease in demand for CRELs largely driven by an anticipated deterioration in customers' economic outlook.

For housing loans extended to households, half of the respondent banks (50.0 percent) reported tighter credit standards in Q3 2020 followed by a similarly large portion of banks indicating unchanged credit standards (46.4 percent). Over the next quarter, majority of the respondent banks continue to expect tighter overall credit standards for housing loans largely due to more uncertain economic prospects, deterioration in borrowers' profile, and lower risk tolerance of banks.

Results based on both the modal and DI approaches also pointed to a decrease in demand for housing loans in Q3 2020, which was attributed by respondent banks largely to lower housing investment and household consumption amid the lingering effects of community quarantine measures on economic activities. Over the next quarter, DI-based results continue to indicate expectations of reduced demand for housing loans reflecting lower housing investment.

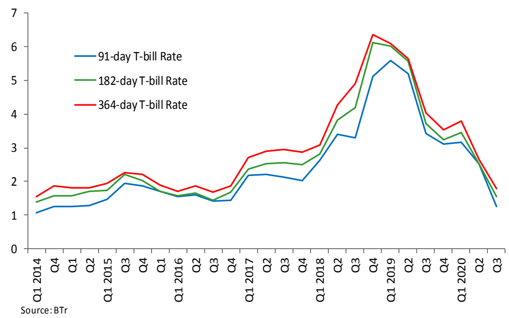
Interest Rates

Primary Interest Rates. The weighted average interest rates (WAIRs) for the 91-, 182- and 364-day T-bills in the primary market fell to 1.264 percent, 1.548 percent, and 1.788 percent in Q3 2020 from 2.516 percent, 2.523 percent, and 2.664 percent, respectively, in the previous quarter. Similarly, the WAIR for the issued 35-day T-bills declined to 1.160 percent from 2.105 percent in Q2 2020.

Treasury bill rates are lower

The results of the auction during the quarter reflected robust demand for safe-haven government notes amid ample amount of liquidity in the financial system as a result of the BSP's liquidity-enhancing measures in response to the COVID-19 pandemic.

Chart 20. Treasury Bill Rates
In percent

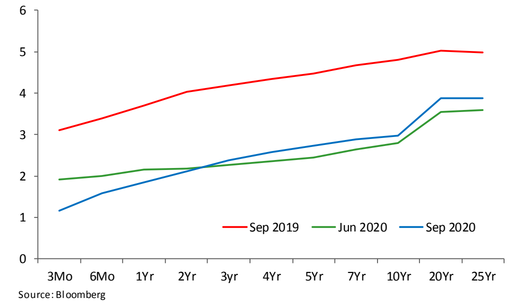


Yield Curve.[38] As of end-September 2020, the secondary market yield for government securities (GS) for all maturities (except for the 3-month, 6-month, 1-year and 2-year tenors) rose relative to the end-June 2020 levels. Market players sought additional returns on longer tenors on expectation that interest rates will remain low for some time.

GS yields rise in Q3 2020

Debt paper yields were higher by a range of 10.8 bps for the 3-year GS to 33.3 bps for the 20-year GS compared to end-June 2020 levels. Meanwhile, yields for the 3-month, 6-month, 1-year and 2-year GS were lower by 73.8 bps, 42.0 bps, 31.6 bps and 5.1 bps, respectively.

Chart 21. Yields of Government Securities in the Secondary Market
In percent



Relative to year-ago levels, the secondary market yields for GS for all maturities decreased by a range of 111.4 bps (for the 25-year GS) to 193.7 bps (for the 3-month GS).

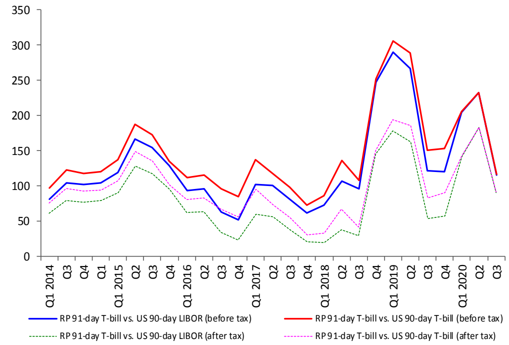
Interest Rate Differentials. The average differentials between domestic and US interest rates, gross and net of tax, narrowed in Q3 2020 relative to the previous quarter.

Interest rate differentials narrow in Q3 2020

The average 91-day RP T-bill rate declined q-o-q by 120.0 bps to 1.272 percent in Q3 2020 from 2.472 percent in Q2 2020. Likewise, the average US 90-day LIBOR and the US 90-day T-bill rate declined by 3.2 bps and 4.6 bps, respectively, to 0.115 percent and 0.103 percent in Q3 2020. These developments led generally to narrower 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 during the quarter.

[38] 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.

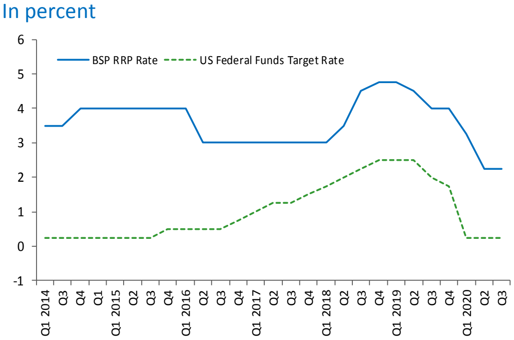
Chart 22. Interest Rate Differentials
Quarterly averages; in basis points



Source: Bloomberg, BTr and BSP

The positive differential between the BSP's overnight borrowing or RRP rate and the US Fed funds target rate remained unchanged at a range of 200-225 bps in Q3 2020, as the BSP’s overnight RRP rate and the US federal funds target rate were kept steady at 2.25 percent and 0.00-0.25 percent, respectively.

Chart 23. BSP RRP Rate and US Federal Funds Target Rate
In percent

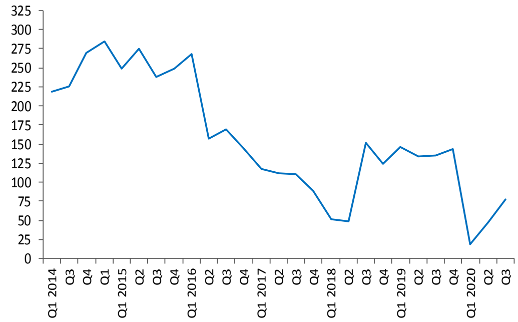


Source: Bloomberg and BSP

Meanwhile, the interest rate differential between the BSP’s overnight RRP rate and the US Fed funds target rate adjusted for risk[39] widened further to 78 bps as of end-September 2020 from 47 bps in end-June 2020.

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

Chart 24. Risk-Adjusted Differentials
In basis points


Source: Bloomberg and BSP

This development could be traced to the 31-bp decrease in the country risk premium following the 31-bp decrease in the 10-year ROP note along with the 1-bp increase in the 10-year US note.

Financial Market Conditions

Financial conditions normalized in Q3 2020 amid ample liquidity. Stock market performance improved while the bond market continued to see robust demand as market participants invested their excess funds. The country’s debt spreads likewise narrowed on optimism as quarantine restrictions were eased. Moreover, the banking system continued to exhibit resilience and stability during the review quarter.

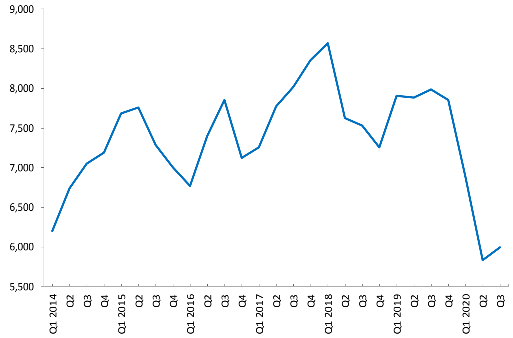
Stock Market. In Q3 2020, the Philippine stock market index inched up amid the gradual easing of quarantine restrictions in some parts of the country,[40] which allowed some businesses to resume operations. Sentiment likewise improved following substantial monetary stimulus measures from the BSP[41] that provided support to the economy amid the pandemic’s negative impact. Reports of possible coronavirus vaccines from

[40] Between mid-March to May, the President imposed strict lockdown protocols (enhanced community quarantine or ECQ) in Metro Manila and key areas. Since then, quarantine measures have been slowly eased to the general community quarantine (GCQ), which is more lenient than the ECQ. However, from August 4 to 18, as infections surged, restrictions were tightened anew thru the MECQ imposition in Metro Manila, which is stricter than a GCQ. Starting August 19, quarantine measures in Metro Manila and its neighboring provinces were again eased to GCQ, which was extended until end-September as the number of local coronavirus cases continued to grow.

[41] In addition to the 175-bp cut in policy rates in 2020, the BSP also reduced the RRR of universal and commercial banks by 200 bps, effective April 3, to release ₱200 billion in system. Moreover, BSP also reduced 100 bps in the RRR of thrift banks and rural/cooperative banks effective on 31 July 2020, which is estimated to release ₱10 billion.

Russia and China as well as the recent passage of the fresh ₱165.5-billion stimulus program[42] also boosted trading sentiment. Hence, q-o-q, the average PSEi went up by 2.7 percent to average 5,990.40 index points during the period July to September.

Chart 25. Quarterly Average PSEi
In index points



Source: Philippine Stock Exchange, BSP

Comparing the end-quarter levels of the PSEi between the second and third quarter, the main index dropped by 5.5 percent from 6,207.72 index points in end-June to 5,864.23 index points in end-September. The decline was amid investors' concern over the continued rise in the number of local coronavirus cases. The sustained increase in Covid-19 infections resulted in the government's slower-than-expected pace in easing current quarantine protocols. This, in turn, limited the number of industries allowed to reopen, further heightening investors' apprehension over the outlook for the country's economic recovery, particularly after the sharp contraction in the Philippine GDP in the first semester of 2020. Perceptions of inadequate institutional support also put pressure on the local equity market.[43] Negative developments abroad (e.g., worsening US-China trade relations; uncertainty over the proposed US stimulus plan; the US Federal Reserve (Fed) Chair's dovish statement that rates will stay low until 2023, indicating US Fed officials' mostly pessimistic view about the US economic recovery; renewed coronavirus lockdown measures in Europe;[44] and rising tensions between North and South Korea) also pushed the index lower.

Other stock market indicators mirrored the general downtrend in the benchmark index during the period-in-review. Total market capitalization declined by 0.2 percent from ₱13.17 trillion in end-June to reach ₱13.15 trillion as of 25 September. Foreign investors also continued to withdraw from the local bourse, posting net sales of ₱35.6 billion during the period July to September, slightly lower than the ₱36.6-billion net sales registered in the preceding quarter.

Government Securities. Results of the T-bill auctions conducted in July-September 2020 showed market players' continued strong demand for government securities (GS) with total subscription for the quarter amounting to around ₱970.5 billion or about 3.3 times the ₱290.0-billion aggregated original amounts on offer. With a lower total offer volume in Q3 2020 relative to the previous quarter, the oversubscription for Q3 2020 likewise decreased to about ₱680.5 billion from the ₱1.0-trillion oversubscription recorded in the previous quarter.

Strong demand for Treasury bills

The healthy demand for T-bills prompted the BTr to award in full the offered amounts in almost all the auctions during the quarter, except for the 364-day T-bills offered on 14 September 2020 wherein bids were fully rejected. At the same time, the strong demand has allowed the BTr to increase the amount awarded for non-competitive bids for the T-bill auctions on 6 July, 14 September, and 28 September. Consequently, the total accepted amounts on 6 July and 28 September were higher than the original weekly offered amount. Meanwhile, the BTr offered the 35-day T-bills only twice in Q3 2020 (compared to six times in Q2 2020) with the BTr awarding in full the ₱15.0-billion offered amount in both auctions.[45]

[42] On 11 September, the President signed Bayanihan 2, the second piece of legislation that aims to mitigate the impact of the coronavirus pandemic on the economy. The program consists of a ₱140-billion stimulus package and a ₱25.5-billion standby fund to total ₱165.5 billion.

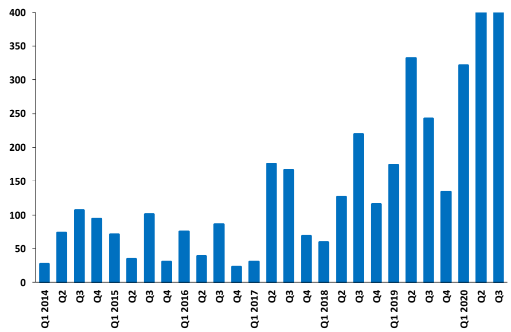
[43] The government has so far unveiled fiscal support packages equivalent to around three percent of GDP, mainly in the form of subsidies to families worst hit by the crisis. Distribution of the support was seen as a problem. Local governments have experienced difficulties identifying people who qualify for benefits. Source: Capital Economics, Philippines: weak recovery, new currency forecasts, 25 September 2020.

[44] On 22 September, several European countries (e.g., Spain, France and the UK) have again imposed restrictions as COVID-19 cases there surged to 4.49 million. The new round of restrictions threatens a nascent recovery and further pressure equity markets.

[45] The 35-day T-bill auctions were originally scheduled on 14 July, 28 July, 4 August, and 18 August. However, to give way

The BTr also offered 5-year RTBS during the quarter with a coupon rate of 2.625 percent. The BTr sold about ₱516.3 billion worth of 5-year RTBs, equivalent to around 17.2 times the planned minimum issuance size of ₱30 billion, on the back of strong demand from the public.[46] At the same time, results of the T-bond auctions during the quarter showed robust demand for longer-term GS amid the ample liquidity in the financial system.

Chart 26. Total Oversubscription of T-bill Auctions
in billion pesos



Sovereign Bond and Credit Default Swap (CDS) Spreads. In July, debt spreads narrowed over the government's decision to lift the MECQ in major parts of the country. The lifting of the quarantine allowed a number of businesses to resume operations.

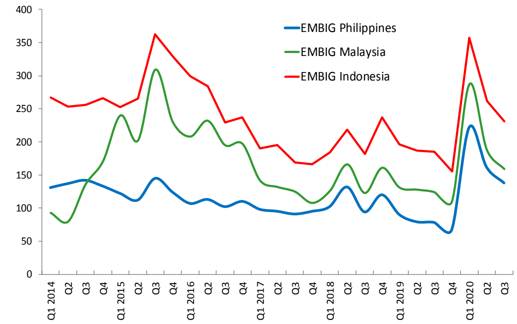
Debt spreads narrow on optimism over response to pandemic

In August, debt spreads narrowed further due to improved market optimism as the economy gradually adjusted to the new normal.

In September, debt spreads continued to narrow as more fiscal relief measures were put in place such as the passage of Bayanihan 2, the law that provides the needed fiscal support to the economy.

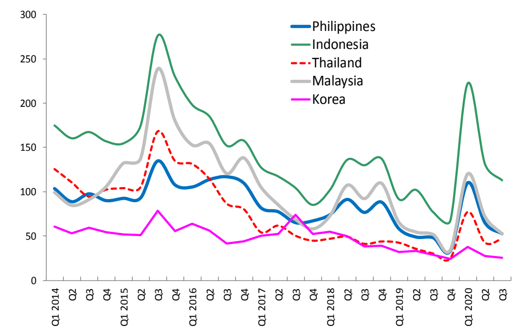
As of 30 September 2020, the extra yield investors demanded to own Philippine sovereign debt over US Treasuries or the Emerging Market Bond Index Global (EMBIG) Philippines spread stood at 138 bps from the end-June level of 162 bps.

Chart 27. EMBIG Spreads of Selected ASEAN Countries
In basis points



Similarly, the country's 5-year sovereign CDS decreased to 53 bps from its end-June level of 65 bps. Against other neighboring economies, the Philippine CDS traded at par with that of Malaysia while narrower than Indonesia's 113 bps but wider than Thailand's 47 bps and Korea's 25 bps spreads.

Chart 28. Five-Year CDS Spreads of Selected ASEAN Countries
In basis points



for the RTB offering, the two scheduled 35-day T-bill auctions in July were cancelled.
[46] The public offer period for the 3-year RTBs was scheduled on 16 July-7 August 2020 while the settlement date was set on 12 August 2020.

Banking System

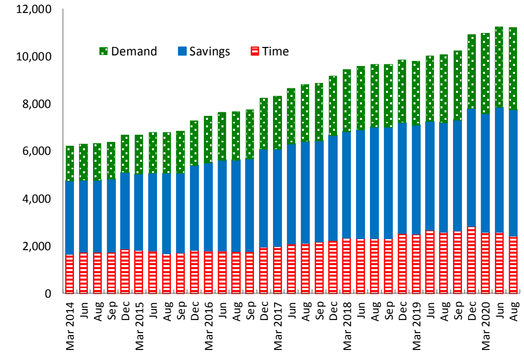
The Philippine banking system showed resilience and stability in Q3 2020 as the country's economic activities and financial transactions continued to recover from the disruption caused by the pandemic and quarantine measures.

Banking system assets and deposits continue to grow

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.[47] 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 (NBFIs) have the widest physical network, consisting mainly of pawnshops.

Savings Mobilization. Savings deposits remained the primary source of funds for the banking system. Banks' total deposits as of end-August 2020 amounted to ₱11.2 trillion, 11.6 percent higher than the level in end-August 2019 but 0.2 percent lower than the level in end-June 2020.[48]

Chart 29. Deposit Liabilities of Banks
In billion pesos



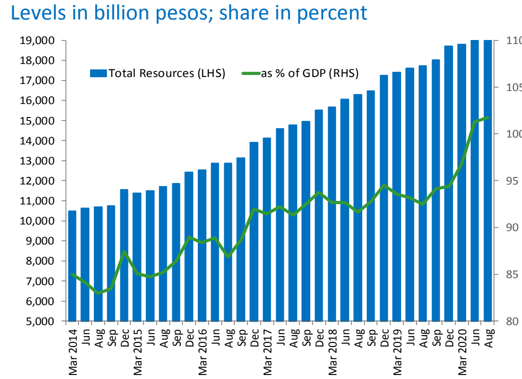
Source: BSP

Meanwhile, foreign currency deposits owned by residents (FCD-Residents) reached ₱2.1 trillion as of end-August 2020, 2.9 percent higher than the level a year ago.[49]

Institutional Developments. The total resources of the banking system grew by 8.2 percent to reach ₱19.2 trillion as of end-August 2020 from ₱17.7 trillion a year ago. Relative to the end-June 2020 level, total resources of the banking system likewise increased by 0.5 percent. As a percent of GDP, total resources stood at 101.7 percent.[50]

Total resources of the banking system sustain growth

Chart 30. Total Resources of the Banking System
Levels in billion pesos; share in percent



Source: BSP

[47] 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 CAR. 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.

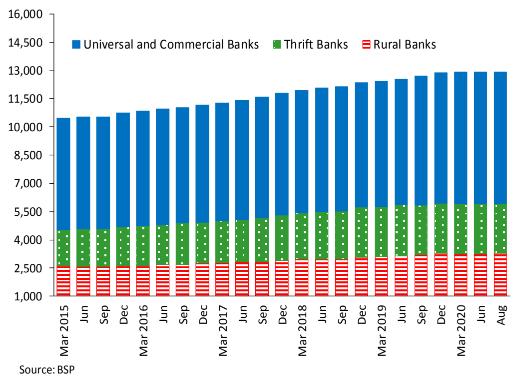
[48] This refers to the total peso-denominated deposits of the banking system.

[49] 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.

[50] GDP as of end-June 2020.

The number of banking institutions (head offices) as of end-August 2020 decreased slightly to 538 offices from 541 in end-June 2020. The banks' head offices are comprised of 46 U/KBs, 48 TBs, and 444 rural banks (RBs). During the same period, the operating network (head offices and branches/agencies) of the banking system increased to 12,925 offices from 12,912 offices in end-June 2020.

Chart 31. Number of Banking Institutions

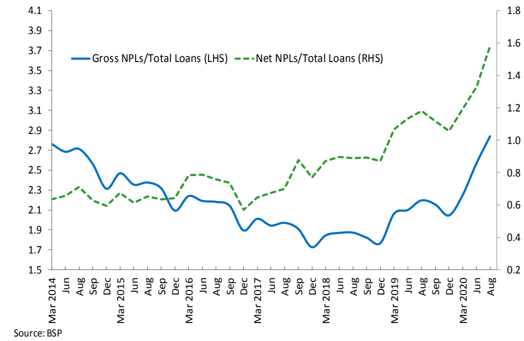


In terms of asset quality, the Philippine banking system's gross non-performing loans (GNPL) ratio rose to 2.8 percent as of end-August 2020 relative to the 2.2 percent posted a year ago and 2.6 percent posted in end-June 2020.

Stable asset quality indicates banks remain 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.[51,52]

Chart 32. Ratios of Gross Non-Performing Loans and Net Non-Performing Loans to Total Loans
In percent



Similarly, the net non-performing loan (NNPL) ratio increased to 1.6 percent as of end-August 2020 relative to the 1.2 percent and 1.3 percent posted a year- and a quarter- ago.

Compared with regional counterparts, the Philippine banking system's GNPL ratio of 2.8 percent was higher with respect to those of Malaysia (0.9 percent) and South Korea (0.7 percent) but was lower than those of Indonesia (2.9 percent) and Thailand (3.0 percent).[53]

Loan exposures of banks remained adequately covered with the banking system's NPL coverage ratio at 107.4 percent as of end-August 2020. This was higher than the previous year's ratio of 91.7 percent and lower than the previous month's 109.9 percent.

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

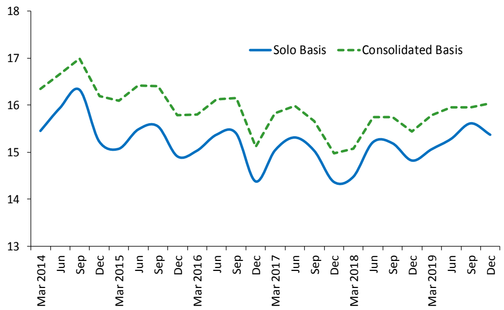
The capital adequacy ratio (CAR) of U/KBs at end-December 2019, on solo basis, decreased marginally to 15.4 percent from 15.6 percent as of end-September 2019. Meanwhile, on a consolidated basis, CAR of U/KBs remained unchanged at 16.0 percent relative to the previous quarter. These figures remained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

[51] The regulatory relief package includes the following, among others: (1) exclusion of the exposure of affected borrowers from the computation of the past due loan ratios; waiver of BSP documentary requirements for restructured loans, and (2) 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).
[52] The 3.5 percent NPL ratio was based on the pre-2013 definition.

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

Chart 33. Capital Adequacy Ratio of Universal and Commercial Banks

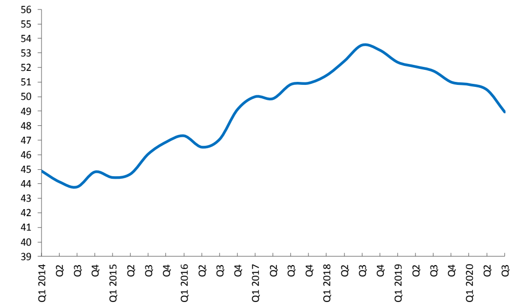
In percent



Source: BSP

Chart 34. Quarterly Peso-Dollar Rate

PHp/US$; average per quarter



Source: Reference Exchange Rate Bulletin, Treasury Department, BSP

The CAR of Philippine U/KBs, on consolidated basis, was higher than that of South Korea (14.5 percent) but lower than those of Malaysia (18.3 percent), Thailand (19.1 percent) and Indonesia (22.5 percent).[54]

Exchange Rate

The peso averaged ₱48.94/US$1 in Q3 2020, appreciating by 3.09 percent from the Q2 2020 average of ₱50.45/US$1.

Peso appreciates reflecting improvement in the country's external position

The country's macroeconomic fundamentals, which include a manageable inflation environment, 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 5.68 percent relative to the ₱51.72/US$1 average in Q3 2019.[55]

In July, the peso continued to appreciate, breaching the ₱49:US$1 territory. The peso averaged ₱49.47/US$1 during the month, 1.27 percent higher than the average in June. The appreciation was due mainly to market optimism on (i) wider balance of payments (BoP) surplus in May 2020;[56] (ii) accommodative signals from the US Federal Reserve; (iii) news of progress in an antiviral drug for COVID-19; (iv) the slight decline in global oil prices; and (v) the State of the Nation Address (SONA) of President Duterte, which outlined some measures to support economic recovery amid the pandemic. The appreciation of the peso was also due to the general weakness of the US dollar amid rising coronavirus infections in the US as well as the protracted tensions between the US and China.

In August, the peso appreciated further, breaching the ₱48:US$1 territory. The peso averaged ₱48.84/US$1 during the month, 1.29 percent higher than previous month's average. The peso appreciated amid (i) concerns over the contraction in the US GDP in Q2 2020; (ii) dovish signals from the US Federal Reserve; (iii) the expected reduction in demand for imports following the MECQ reimposition in Metro Manila and nearby provinces; (iv) market expectation that the BSP interest rates are likely to be maintained in the 20 August 2020 policy-setting meeting; (v) the ratification of the Bayanihan II bill by Congress which aims to assist the government in its COVID-19 response and economic recovery plan; and (vi) the release of narrower-than-expected trade deficit in June 2020.

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

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

[56] Data from the BSP showed BoP stood at a surplus of $2.43 billion in May 2020, wider than the $928 million and $1.666-billion surplus registered a year- and a month ago, respectively.

In September 2020, the peso appreciated to an average of ₱48.51/US$1, 0.68 percent higher than the ₱48.84/US$1 average during the previous month. The peso appreciated due mainly to positive market sentiment following (i) the release of the country's stronger-than-expected current account data for Q2 2020; (ii) the extension of the general community quarantine in Metro Manila until end October 2020; and (iii) renewed talks on the approval of a coronavirus stimulus package by the US government. Meanwhile, the US Federal Reserve's decision to keep its policy rates steady in its 15-16 September 2020 meeting likewise provided support to the peso.

On a y-t-d basis, the peso appreciated against the US dollar by 4.41 percent to close at ₱48.50/US$1 on 30 September 2020 from the end-December 2019 closing rate of ₱50.64/US$1.[57]

Meanwhile, the volatility of the peso's daily closing rates (as measured by the coefficient of variation) stood at 0.86 percent in Q3 2020, higher than the 0.17 percent registered in the previous quarter.[58] The volatility of the peso in the review quarter was, however, lower than the volatility of most currencies in the region.

On a real trade-weighted basis, the peso gained external price competitiveness in Q3 2020 against the basket of currencies of all trading partners (TPI) and trading partners in advanced (TPI-A) and developing (TPI-D) countries relative to Q2 2020. This was indicated by the slight decrease in the real effective exchange rate (REER) index of the peso by 0.47 percent, 0.68 percent and 0.36 percent against the TPI, TPI-A and TPI-D baskets, respectively.

Relative to Q3 2019, the peso meanwhile 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 vis-à-vis trading partners resulting in the increase in the REER index of the peso by 6.64 percent, 5.81 percent and 7.11 percent against the TPI, TPI-A and TPI-D baskets, respectively.[59,60]

---

[57] Based on the last done deal transaction in the afternoon.

[58] 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.

[59] 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 include 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 include China, Singapore, South Korea, Hong Kong, Malaysia, Taiwan, Indonesia, Saudi Arabia, United Arab Emirates, and Thailand.

[60] 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 a ₱740.7-billion fiscal deficit for January-August 2020, significantly higher than the previous year's budget gap.

NG records a fiscal deficit for January to August 2020

Netting out the interest payments in NG expenditures, the primary deficit amounted to ₱471.1 billion, which is a turnaround from the primary surplus recorded in 2019.

Table 15. National Government Fiscal Performance
In billion pesos

	2019		2020		Growth Rate (in percent)	
	Aug	Jan-Aug	Aug	Jan-Aug	Aug	Jan-Aug
Surplus/(Deficit)	-2.5	-120.4	-40.1	-740.7	1,510.6	515.0
Revenues	279.7	2,091.4	243.2	1,931.0	-13.1	-7.7
Expenditures	282.2	2,211.8	283.3	2,671.7	0.4	20.8

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

Revenues decreased by 7.7 percent to ₱1,931.0 billion in August 2020 compared to ₱2,091.4 billion in the same period last year. The Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC) contributed ₱1,303.3 billion and ₱347.3 billion, respectively. Revenue collections by the BIR and BOC were lower by 10.3 percent and 15.6 percent, respectively. The agencies' lower collection was attributed to the economic restrictions brought about by the COVID-19 pandemic. Meanwhile, the BTr recorded an income of ₱192.9 billion, 78.8 percent higher than the income recorded last year on account of higher dividends.

Expenditures for the period in review amounted to ₱2,671.7 billion, 20.8 percent higher than the expenditures in January-August 2019. Excluding interest payments, expenditures went up by 22.5 percent to ₱2,402.1 billion. Meanwhile, interest payment was 7.6 percent higher compared to its year-ago level, reaching ₱269.6 billion in January-August 2020.

IV. External Developments

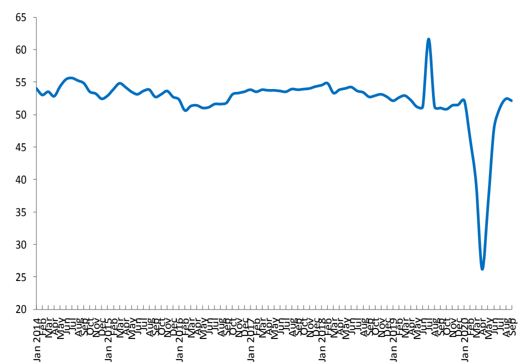
The JP Morgan Global All-Industry Output Index fell to 52.1 in September from 52.4 in August as rates of expansion in both the manufacturing and service sectors eased. Five out of the six sub-sectors covered by the survey registered output growth during the month, with the strongest performance posted by the investment goods industry.

Global economic output expands

Moreover, output expansions were observed in the US, Germany, the UK, Italy, Brazil, Russia, Australia, and Kazakhstan, offsetting the contractions seen in Japan, France, Spain, and Ireland.[61]

Chart 35. 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 31.4 percent in Q2 2020 from a 5.0-percent decline in Q1 2020. On a y-o-y basis, real output decreased by 9.0 percent in Q2 2020 following a 0.3-percent expansion in the previous quarter.

US manufacturing activity expands at a slower pace

The decline in real GDP in the second quarter reflected decreases in personal consumption expenditures, exports, nonresidential fixed investment, private inventory investment, residential fixed investment, and state and local government spending. These movements were partly offset by an increase in federal government spending.[62]

Meanwhile, the US manufacturing PMI eased to 55.4 percent in September from 56.0 percent in August due to a decline in the new orders and production indices.[63]

The unemployment rate decreased to 7.9 percent in September from 8.4 percent in August, reflecting the continued resumption of economic activity that had been curtailed due to the COVID-19 pandemic and efforts to contain it. Total nonfarm payroll employment rose by 661,000 during the month, with notable employment gains in leisure and hospitality, retail trade, health care and social assistance, and professional and business services. Meanwhile, on a y-o-y basis, inflation rose to 1.4 percent in September from 1.3 percent in August due partly to the smaller decline in the energy price index as well as faster inflation for new vehicles and used cars and trucks.

The Conference Board Consumer Confidence Index increased to 101.8 in September from 86.3 in August due to consumers' more favorable assessment of the short-term outlook on business conditions and the labor market. Meanwhile, the preliminary Thomson-Reuters/University of Michigan Index of Consumer Sentiment went up to 81.2 in October from 80.4 in September due to the continued small gains in economic prospects for the year ahead which offset consumers' concerns on current economic conditions amid slowing employment growth, resurgence in COVID-19 infections, and the absence of additional federal relief payments.[64]

Euro Area. On a q-o-q basis, real GDP in the euro area shrank by 11.8 percent in Q2 2020 after declining by 3.7 percent in Q1 2020. On a y-o-y basis, real GDP contracted by 14.7 percent in Q2 2020 following a 3.2-percent decrease in the previous quarter.[65]

[61] JP Morgan Global Composite PMI, http://www.markiteconomics.com/

[62] US Bureau of Economic Analysis, "Gross Domestic Product: Second Quarter 2020 (Third Estimate)," news release, 30 September 2020. https://www.bea.gov/sites/default/files/2020-09/gdp2q20_3rd_0.pdf

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

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

[65] Eurostat news release 133/2020 dated 8 September 2020

Meanwhile, the composite PMI for the euro area fell slightly to 50.4 in September from 51.9 in August. Business activity stalled as rising infection rates and ongoing social distancing measures hampered demand, particularly for consumer-facing services.[66]

Economic activity in the euro area expands at a weaker pace

Inflation in the euro area fell to -0.3 percent in September from -0.2 percent in August due to lower prices of energy and non-energy industrial goods as well as slower inflation for services.[67] Meanwhile, the seasonally adjusted unemployment rate rose to 8.1 percent in August from 8.0 percent in the previous month.

The European Commission's Economic Sentiment Indicator in the euro area rose to 91.1 in September from 87.5 in August, driven by waning pessimism in industry, retail trade, construction, and,in particular, services, as well as improved confidence among consumers.

Japan. On a q-o-q seasonally-adjusted basis, real GDP declined by 7.9 percent in Q2 2020 after a 0.6-percent contraction in Q1 2020. Similarly, on a y-o-y basis, real GDP fell by 9.9 percent in Q2 2020 after contracting by 1.8 percent in the previous quarter as both private and public demand declined.[68]

Activity in Japan shows signs of recovery, but manufacturing remains in contraction

The seasonally adjusted manufacturing PMI rose to 47.7 in September from 47.2 in August, reflecting the weakest decline in production volumes since February.[69]

Inflation eased slightly to 0.2 percent in August from 0.3 percent in July due to slower inflation for fuel, light, and water charges; education; and culture and recreation. Meanwhile, the seasonally adjusted unemployment rate rose to 3.0 percent in August from 2.9 percent in July.

China. Real GDP in China expanded by 3.2 percent y-o-y in Q2 2020 from a 6.8-percent contraction in the previous quarter, reflecting China's gradual economic recovery amid the relaxation of COVID-19 containment measures and the rollout of stimulus measures to prop up the economy.

Chinese manufacturing activity improves in August

Meanwhile, China's seasonally adjusted manufacturing PMI was fairly steady at 53.0 in September from 53.1 in August amid the surge in new export orders on the back of a recovery in overseas demand.[70]

Inflation decreased to 1.7 percent in September from 2.4 percent in August due to lower food inflation during the month.

India. Real GDP in India contracted by 23.9 percent in Q2 2020 following a 3.1-percent growth in the previous quarter.[71]

Economic activity in India returns to expansion territory

Meanwhile, the composite PMI rose to 54.6 in September from 46.0 in August due mainly to the sharp upturn in manufacturing production.

Inflation in India rose to 7.3 percent in September from 6.7 percent in August due to higher inflation for food and beverages as well as clothing and footwear.

[66] Flash Markit Eurozone PMI, http://www.markiteconomics.com/
[67] Eurostat news release 152/2020 dated 16 October 2020
[68] Second Preliminary Estimate. Department of National Accounts, Economic and Social Research Institute, Cabinet Office. http://www/esri.cao.go.jp/
[69] Jibun Bank Japan Manufacturing PMI, http://www.markiteconomics .com/
[70] Caixin China General Manufacturing PMI, http://www.markiteconomics.com/
[71] No details were provided on the Q2 2020 GDP growth of India. The imposed restrictions to contain the spread of the COVID-19 pandemic affected data collection mechanisms in India and thus estimates are likely to undergo revisions. (Source: Ministry of Statistics and Programme Implementation. http://mospi.nic.in/)

ASEAN Region. The Nikkei ASEAN Manufacturing PMI fell to 48.3 in September from 49.0 in August due to a renewed contraction in manufacturing output as well as order volumes.

Manufacturing conditions in the ASEAN region deteriorate

Across the seven monitored countries, Myanmar posted a significant deterioration in manufacturing conditions. Contractions were also recorded in Indonesia, Singapore, and Malaysia. Meanwhile, operating conditions were broadly stable in Thailand and the Philippines, while Vietnam posted an improvement in manufacturing activity.[72]

Policy Actions by Other Central Banks.
On 16 July 2020, Bank Indonesia (BI) reduced the 7-day reverse repurchase rate by 25 bps to 4.0 percent. The BI considered its decision as consistent with low projected inflation as well as to maintain external stability and support national economic recovery during the COVID-19 pandemic.

Central banks' policy stance remains accommodative

Similarly, on 7 July 2020, Bank Negara Malaysia (BNM) decided to lower the overnight policy rate (OPR) by 25 bps to 1.75 percent to provide additional policy stimulus to accelerate the pace of economic recovery. According to BNM, global economic conditions remain weak, while broad-based weakness in labor markets and precautionary behavior by households and businesses could affect economic recovery going forward.

In September, the US Federal Reserve, BI, Bank of Japan, Central Bank of the Republic of China (Taiwan), Bank of England, the Reserve Bank of New Zealand (RBNZ), Bank of Thailand (BOT), Reserve Bank of Australia (RBA), Bank of Canada (BOC), the European Central Bank (ECB), and BNM decided to keep their respective policy rates steady.

Meanwhile, the People's Bank of China (PBOC) has not announced any change in the one-year loan prime rate thus far in September.

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

V. Monetary Policy Developments

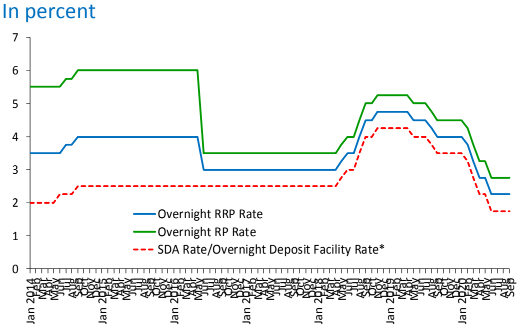
At its monetary policy meetings on 20 August and 1 October, the BSP decided to maintain the interest rate on the BSP's overnight RRP facility at 2.25 percent. The interest rates on the overnight deposit and lending facilities were likewise kept at 1.75 percent and 2.75 percent, respectively.

The BSP maintains policy rates in Q3 2020

The BSP's decision to keep the policy rate steady was based on the assessment that prevailing monetary policy settings remain appropriate during the quarter. The BSP noted that the future inflation path remains firmly within the Government's 2-4 percent target. During the October policy meeting, latest baseline inflation forecasts show a slightly lower path within the Government's 2-4 percent target range, reflecting the lower-than-expected inflation in August, the moderation in global crude oil prices, and the appreciation of the peso. The balance of risks to the inflation outlook also continues to lean toward the downside from 2020 until 2022 owing largely to the risk of potential disruptions to domestic and global economic activity amid the ongoing pandemic. Equally important, inflation expectations remain firmly anchored within the inflation target band.

Chart 36. BSP Policy Rates

In percent



* On 3 June 2016, Special Deposit Accounts (SDAs) were replaced by the Overnight Deposit Facility (ODF) in line with the implementation of the Interest Rate Corridor (IRC) System.
Source: BSP

The BSP also noted that global economic activity has stabilized in recent weeks. However, uncertainty remains elevated with the resurgence of COVID-19 cases in some jurisdictions. At the same time, the BSP observed encouraging signs of recovery in domestic economic activity, supported by ample liquidity in the financial system.

The BSP concluded, given these considerations, that a continued pause would allow prior measures by the BSP to further work their way through the economy. The gradual easing of restrictions, along with sustained efforts by the Government to protect human health and livelihood, should also help lift market sentiment and aid the recovery of the economy in succeeding months.

The BSP emphasized that, looking ahead, it stands ready to deploy its full arsenal of instruments as needed in fulfillment of its mandate to maintain price and financial stability conducive to sustainable economic growth.

VI. Inflation Outlook

BSP Inflation Forecasts

The latest baseline forecasts continue to suggest a benign inflation environment over the policy horizon. Inflation is expected to average at 2.3 percent for 2020, 2.8 percent for 2021, and 3.0 percent for 2022.

The forecasts for 2020 and 2022 were left unchanged compared to the previous report. Meanwhile, the forecast path for 2021 is slightly higher due to the higher-than-expected inflation outturns for Q3 2020 which were partly offset by slower domestic and global economic activity as well as the continued appreciation of the peso.

The latest forecasts continue to suggest benign inflation environment throughout the policy horizon due to the impact of COVID-19 pandemic on global demand, domestic economic conditions, and commodity prices. Inflation is projected to decelerate close to the low-end of the target range in Q4 2020 due largely to negative base effects but is seen to approach the midpoint of the target range in Q2 2021 as oil prices rise and domestic growth prospects improve. Inflation is likely to settle close to the midpoint from H2 2021 to 2022.

The risks to the inflation outlook remain 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 are the main upside risks to inflation.

Inflation remains benign over the policy horizon

Demand Conditions. Domestic growth contracted further in Q2 2020 by 16.5 percent from 0.7 percent decline in Q1 2020 and 5.4-percent expansion in Q1 2019. On the production side, growth in industry and services sectors moderated significantly, reflecting the impact of the community quarantine measures, while agriculture sector increased during the quarter. On the expenditure side, the weak global environment and the impact of community quarantine adversely affected consumption, investments, and trade during the quarter.

The nowcast for Q3 2020 growth indicates that the economy could continue to contract but at a slower pace compared to the previous quarter. The decline in GDP could be driven primarily by the further deterioration in industry and services, which remain heavily affected despite some easing in quarantine measures. In particular, the continued weakness in manufacturing and construction activities is expected to drive the decline in industry, although at a slower pace compared to Q2 2020. Similarly, services could continue to contract, driven primarily by the slowdown in transport, tourism, and other service activities. Meanwhile, the growth in agriculture is projected to accelerate in the quarter due to higher *palay* and corn production.

High-frequency real sector indicators point to weak growth prospects but show signs of recovery. Manufacturing’s volume of production index for August 2020 remains in negative territory but contracted at a slower rate compared to the previous months. The composite PMI (PMI) remained below the 50-point mark as of August 2020, suggesting contraction across all sectors. Similarly, results of the BSP expectations surveys have indicated that consumer and business confidence have turned pessimistic for Q3 2020.

The persistent surge in local COVID-19 cases could continue to dampen consumer and business sentiments in the coming months. Nonetheless, improvements in mobility indicators could indicate that firms and households are beginning to adjust to the pandemic operating environment, which could support resurgence in economic activity in the near term.

Growth is expected to recover in 2021 and 2022

Over the medium term, domestic economic activity is expected to recover in 2021 and 2022 as the impact of government policy measures fully gains traction with the passage of the *Bayanihan* II Act. Moreover, the implementation of well-targeted amelioration and recovery programs as well as the restart of the infrastructure spending program will help the country regain confidence, 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. In addition, the BSP's timely actions to enhance liquidity conditions and bolster sentiment are expected to provide support to the economy.

Supply Conditions. Food prices are expected to remain benign over the near term due to the continued growth in domestic agricultural production. Moreover, the projections of a weak-to-moderate *La Niña* episode could further improve domestic supply conditions.

The continued concerns over weak global demand and increased inventories in Asia exerted downward pressures on oil prices during the quarter. Consequently, the global crude oil price assumptions were broadly unchanged compared to the previous forecast round.

Economic activity is projected to operate below its full capacity 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.[73]

Based on the Q2 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. This implies that the economy will likely operate below its full capacity over the policy horizon as firms and households gradually adjust to the post-pandemic economic conditions. However, the projected contraction in economic activity could be temporary in nature, as public health measures to control the spread of the pandemic alongside macroeconomic policy gain full traction in reviving the economy.

[73] 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).

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 October 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. [74]

Compared to the previous inflation report, the latest fan chart is broadly stable with a slightly higher path for 2021 due largely to higher-than-expected inflation outturns for Q3 2020 which

[74] 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.

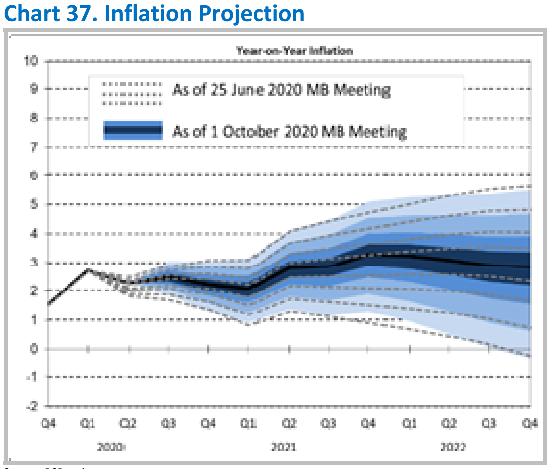
were partly offset by slower domestic and global economic activity as well as the continued appreciation of the peso.

The BSP's review of current inflation dynamics suggests that the risks surrounding the inflation outlook appear to be on the downside for 2021 to 2022.

A more disruptive impact of COVID-19 could lead to a deeper slowdown in global and domestic economic activity. 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. 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 2021 to 2022

Chart 37. Inflation Projection



Source: BSP estimates

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 ERC's approval. PSALM's petitions cover adjustments for fuel and foreign exchange costs.

Implications for the Monetary Policy Stance

The BSP held its monetary policy settings steady during the meetings of the Monetary Board on 20 August 2020 and 1 October 2020.

The BSP recognized that inflation is projected to be relatively benign for 2020 up to 2022, while inflation expectations continue to be well-anchored within the target range of 3.0 percent ± 1 ppt. The balance of risks to the inflation outlook also remains 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, global economic activity has stabilized during the quarter, although uncertainty remains elevated with the resurgence of COVID-19 cases in some jurisdictions. Meanwhile, the BSP has observed encouraging signs of recovery in domestic economic activity, supported by the continued stabilization of domestic liquidity conditions.

Given these considerations, the BSP is of the view that prevailing monetary policy settings remain appropriate. A prudent pause will enable the cumulative 175-basis-point reduction in the policy rate as well as other monetary and regulatory relief measures by the BSP to fully work their way through the economy.

Looking ahead, the benign inflation environment gives the BSP ample room to keep the monetary stance sufficiently accommodative to mitigate the strong downside risks to growth. Meanwhile, the gradual easing of restrictions, along with sustained efforts by the National Government to protect human health and livelihood, should help lift market sentiment and aid the recovery of the economy in the succeeding months.

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	
2 0 0 8			
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 ppt target range in 2008 and the 3.5 ± 1 ppt 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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent) RRP Overnight	Levels (in percent) RP Overnight	Monetary Policy Decisions
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.
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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
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.
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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
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.
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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
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.
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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
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.
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.

Summary of Monetary Policy Decisions

Effectivity Date	Levels (in percent)		Monetary Policy Decisions
	RRP Overnight	RP Overnight	
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)			Monetary Policy Decisions
	Overnight Reverse Repurchase Facility	Overnight Deposit Facility	Overnight Lending Facility	
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	2.75	3.75	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	2.25	3.25	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	1.75	2.75	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.
20 Aug 2020	2.25	1.75	2.75	The MB decided to maintain the BSP's key policy interest rates at 2.25 percent for the overnight RRP facility, 2.75 percent for the OLF and1.75 percent for the ODF.

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

If you wish to receive an electronic copy of the latest BSP Inflation Report, please send an e-mail to bspmail@bsp.gov.ph.

The BSP also welcomes feedback from readers on the contents of the Inflation Report as well as suggestions on how to improve the presentation. Please send comments and suggestions to the following addresses:

By post: BSP Inflation Report
c/o Department of Economic Research
Bangko Sentral ng Pilipinas
A. Mabini Street, Malate, Manila
Philippines 1004

By e-mail: bspmail@bsp.gov.ph