Benjamin E Diokno: Sustaining the Philippine growth momentum

Speech by Mr Benjamin E Diokno, Governor of Bangko Sentral ng Pilipinas (BSP, the central bank of the Philippines), at the Rotary Club of Manila centennial year celebration, Manila, 6 June 2019.

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President Susing Pineda, fellow rotarians, friends, all the RCM Journalism Awardees special guests, ladies and gentlemen, good afternoon.

Thank you for inviting me to be one of your speakers in this historical centennial anniversary celebration of the Rotary Club of Manila. Not many organizations have the distinction of reaching the all-important “century” milestone. Attaining this momentous landmark is certainly not a walk in the park for any organization. That the RCM have lasted this long is a reflection not only of its long-standing commitment to its ideals and goals, but also of its dynamism, relevance, and influence to the community it serves. For this, the men of the RCM deserve our congratulations! (Governor leads applause).

I thus consider it a privilege that I stand here before you today to share with you the BSP’s assessment of the country’s growth prospects. The Philippine economy is sound, its prospects are bright. Along many dimensions, allow me to highlight several factors that continue to steer our story of resilience and stability, and to point out some key challenges that need to be addressed in our drive towards sustainable and balanced growth.

Let me begin with this slide which shows that overall prospects for the Philippine economy for 2019 and in 2020 remain bright, amid mounting global uncertainties along with emerging domestic challenges.

While the Q1 2019 growth of the Philippine economy of 5.6 percent was short of our target of 6.0 to 7.0 percent, it remains one of the highest in the region and perhaps the world. This performance was achieved notwithstanding the delay in the approval of the 2019 national budget which held back the implementation of key programs and projects.

Based on the statistics by the National Economic Development Authority (NEDA), the Philippine economy should have grown by at least one percentage point higher, at 6.6 to 7.2 percent in the first quarter, had the 2019 fiscal program been approved on time. Nonetheless, the government has crafted a “catch-up” plan to make up for the lower-than-planned state spending in the first quarter. And the consensus is that we will hit our target of 6-7% growth this year.

On the supply side, economic activity was boosted mainly by the services sectors’ robust performance. Meanwhile, the strong expansion in both investments and consumer spending also supported growth on the demand side. With the sustained 81 consecutive quarters (spanning more than 2 decades from 1999 to 2019) of uninterrupted growth, we remain optimistic that the Philippine economy can sustain its growth momentum over the medium term.

Third-party assessors share the same optimism. Shown in this slide are the growth projections released by the International Monetary Fund (IMF), the World Bank (WB) and the Asian Development Bank (ADB) in their latest surveillance reports.

The World Bank just reaffirmed, they are sticking to 6.4 percent growth this year for our country. These third-party assessments are also not far from the NEDA’s target for 2019. It may be noted that the Development Budget Coordination Committee (DBCC), during its meeting on 13 March 2019, approved a Gross Domestic Product (GDP) growth target range of 6.0 percent – 7.0 percent for 2019, 6.5 percent – 7.5 percent in 2020, and 7.0 percent – 8.0 percent from 2021 to 2022.

In addition, the strength of the Philippine economy was further validated with the upgrade in our sovereign credit rating by Standard & Poor's to BBB+ with a stable outlook. This is the highest letter grade for the foreign currency and an improvement from the BBB grade for the local currency rating. At the same time, Fitch—another rating agency—recently affirmed the Philippines' investment BBB rating, also with a stable outlook.

Recent demand indicators continue to point to overall firm domestic growth prospects in the near term. In fact, results of the Q1 2019 survey-based consumer and business sentiment showed an improved outlook. The consumer outlook index registered an all-time largest quarter-on-quarter increase since the start of the nationwide survey in Q1 2007.

At the same time, the confidence index for business showed marked improvement after declining for four consecutive quarters.

Furthermore, with the end of the 2019 budget impasse, the continued implementation of the government's infrastructure program – which we fondly call "Build, Build, Build" – is envisioned to generate an "impressive multiplier effect" on the economy by increasing its productive capacity, creating jobs, raising incomes, and enhancing the investment climate in the country.

Moving on to inflation dynamics, price pressures have gone down significantly, falling toward the midpoint (at 3.0 percent in April 2019) of the target band. This brought the year-to-date (January – April) average to 3.6 percent year-on-year for 2019. This is firmly within the government's 2-4 percent target range.

This is a stark contrast to last year's rapidly rising inflation figures that was only arrested through the adoption of timely monetary action by the BSP and non-monetary measures by the Executive department.

Looking ahead, we expect inflation to remain on a target-consistent path for 2019 and 2020. The latest baseline forecasts (as of 9 May 2019 MB policy meeting) indicate that inflation is projected to average at 2.9 percent this year while inflation forecast for next year is slightly higher at 3.1 percent. This is due largely to the rebound in global crude oil prices.

Similarly, forecasts of other institutions generally convey the same expectations. Results of the BSP's April 2019 survey of private sector economists showed lower mean inflation forecast for 2019 at 3.1 percent down from 3.3 percent in the previous survey round. The mean inflation forecasts for 2020 and 2021 both declined to 3.3 percent from 3.4 percent. Meanwhile, projections from other institutions also show inflation within target for this year and the next.

Given prevailing conditions, the BSP decided to reduce its policy rate by 25 basis points (bps) to 4.50 percent from 4.75 percent, effective 10 May 2019. The BSP also pre-announced a phased 200-bp reserve requirement reduction for universal and commercial banks, thrift banks (TBs) and non-bank financial institutions with quasi-banking functions (NBQBs); as well as a 100-bp RR reduction on demand deposits and NOW accounts for rural and cooperative banks. Moreover, long-term negotiable certificates of time deposit (LTNCDs) will have uniformed RR ratio of 4.0 percent.

In reducing the BSP's policy rate and reserve requirement ratios, the Monetary Board recognized the progressive decline in domestic inflation. It was further guided by the target-consistent inflation path with inflation expectations converging with the government's target. This is also part of the BSP's ongoing initiative to enhance the effectiveness of monetary policy and deepen domestic money market.

Nevertheless, we recognize the uncertainty in the global economic environment, with the IMF further revising down its global growth prospects due to volatilities in commodity prices, uncertainty over advanced economies' policy normalization, as well as ongoing trade tensions as a result of the US-China [trade] war.

But while the external environment is challenging, I am cautiously optimistic about the current state of the Philippine economy.

“Keeping our house in order” remains the first and best line of defense. We are improving economic openness through liberalization of trade and foreign direct investment, we are enhancing external competitiveness by strengthening domestic industries; we are diversifying products and markets to non-traditional growing economies; and we are sustaining domestic economic resilience by building adequate buffers. These are some of the policy actions and reforms that we can pursue or continue to pursue in order to ward off the potential negative effects of external shocks, especially from rising protectionist measures and heightened policy uncertainty.

Let me talk briefly about the US-China trade dispute. There was no direct imposition against the Philippines in terms of the country’s exposure to the products imposed with tit-for-tat measures between US and China. But the extent of impact would depend on the industries affected. For instance, the Philippines could possibly boost exports of food and agricultural products to the US, taking advantage of the tariffs imposed on Chinese goods of similar nature. The same goes for US agricultural goods imposed with steep tariffs by China.

We see one positive impact that the US-China trade war could have on the Philippine electronics industry. That is if companies on either or both of the countries use the Philippines as an alternative manufacturing site. This scenario, however, would take time and the Philippines would have to compete with other potential relocation sites like Vietnam and Indonesia. The potential upside may not come about for a few years as firms would need to complete the lengthy process of shifting production sites.

We also recognize that the continued trade friction could negatively affect overall investment sentiment and increase caution and uncertainty in the global growth prospects. This could take its toll on the country’s external sector. Nevertheless, given that the economy’s growth is mainly driven by domestic demand, the trade friction would have limited negative impact on Philippine exports.

Before I close, let me emphasize the importance of sustained collaboration between the government and the private sector in pursuing hard yet necessary structural reforms to fuel the Philippine growth engine over the long-term.

Towards the end of the administration of the late president Corazon Aquino, a world class team of economist, headed by no less than Paul Krugman, analyzed the Philippine economy. And they concluded that given the economic conditions at that time, during President Cory Aquino’s time, the long-term growth of the Philippine economy was in the neighborhood of 3 percent. Repeat, 3 percent. We could only grow at 3 percent. That was then. Things are significantly different now.

Over the past 25 years, meaningful reforms have helped build and fortify the institutions that facilitate growth by expanding the role of market forces in key sectors of the economy; encouraging investments and private sector activity; removing bottlenecks for doing business in the country; and strengthening the country’s fiscal position and the financial sector, to name just a few.

No doubt, the Duterte administration is in a strong position to push for reforms by leveraging on its strong political capital as evidenced by the number of laws enacted in less than 3 years of the current administration’s leadership. These include, among others, recent enactment of the tax reforms, amendments to the BSP Charter and Rice Tariffication Law. These reforms, along with the other structural reforms in the pipeline, will continue to play a significant role in propelling the economy on a path of balanced, sustainable, and inclusive growth.

Let me take the chance to talk about Republic Act No. 11211 which was signed on 14 February 2019. This is a monumental milestone for the BSP. Our three pillars of central banking—price stability, financial stability, and an efficient payments and settlements system—were further boosted with the expansion of the BSP's policy toolkit.

- RA 11211 restored the BSP's authority to issue its own debt papers as part of its regular monetary operations, establishes a stronger prudential regulatory framework to promote a safe and sound financial system through the expansion of supervisory coverage and authority to prescribe metrics attuned to international standards and practices.
- The amendment likewise empowers the BSP to oversee the country's payment and settlement systems (PSS) including critical financial market infrastructures that are vital components of the PSS.

Looking ahead, we will continue to monitor domestic and global developments to ensure that the BSP is able to meet its inflation targets. The BSP is also ready to use all appropriate measures as needed to ensure an inflation environment conducive to sustainable growth of the Philippine economy.

Rest assured that the future policy actions of the BSP will continue to be guided by the following principles:

1. Our primary focus will be price stability.
2. We will be pre-emptive rather than reactive and
3. Our policy will be data-driven and evidence-based.

Finally, let me leave you with the assurance that the Philippine economy is sound. It is one of the best performing economies in the world. Its prospects are bright—extremely bright.

And if you have money to invest, and I can see, some people here have money to invest, this is the best time to invest, invest, invest in the Philippines. Do not delay, do not waver. Because if you do, you will regret it.

To wrap up, let me end my presentation with these key take-aways.

- The BSP's monetary policy actions will help ensure that 2019 and 2020 inflation targets are achieved. Nevertheless, the BSP will remain watchful and vigilant, utilizing its analytical and surveillance tools for any potential risks to its monetary and financial stability objectives.
- The Philippine economy has demonstrated uninterrupted economic expansion and has built domestic sources of resilience to help cushion against uncertainty in external environment and emerging domestic challenges
- Strategic policy and structural reforms, addressing infrastructure gaps, and leveraging the country's demographic opportunities have played a significant role and will continue to underpin the economy's path towards balanced, sustainable, and inclusive growth.
- Commitment to pursue infrastructure and reform agenda will help promote globally competitive industries in order to sustain the country's economic growth momentum.

Lastly, on behalf of the Bangko Sentral ng Pilipinas, I congratulate all the energetic and irrepressible members of the Rotary Club of Manila, both young and old, for reaching 100 years!

Mabuhay ang Rotary Club of Manila! Mabuhay ang Pilipinas! Mabuhay po tayong lahat!