Media and Research - Speeches

The Philippines: Gearing up for Greater Heights

Date: May 29, 2022
Occasion: BBVA Investor Roundtable Discussion
Speaker: BSP Governor Benjamin E. Diokno

Good day, everyone. Thank you to BBVA for giving us the opportunity to update you on the Philippine economy.

Allow me to highlight our connection with Spain. Over the years, Spain has been an important ally, contributing to our trade growth. Spain and the rest of the European Union support our initiatives, particularly the Build, Build, Build program, which I will be talking in detail.

The Philippines has successfully managed the COVID-19 health crisis on the back of strong fundamentals built through decades of structural reforms and sound macroeconomic management.

After the pandemic-driven recession in 2020, the economy grew by 5.7 percent last year and 8.3 percent in the first quarter this year. We attribute this to much-relaxed mobility and activity restrictions as the country was able to manage the spread of COVID-19.

Growth in the first quarter was broad-based.

On the supply side, all sectors expanded, driven by industry at 10.4 percent, followed by services at 8.6 percent.

On the expenditure side, growth was driven by 10.1-percent increase in private consumption, a stark reversal of 4.8-percent contraction in the same quarter a year ago.

Investments and external trade performed well, too.

Its latest robust performance has made the Philippines the fastest growing economy in the region.

The employment picture is close to pre-pandemic level.

From a peak of 17.6 percent in April 2020, unemployment rate was down to just 5.8 percent in March this year.

Foreign direct investments reached an all-time high last year. In the first two months of the y
FDIs grew by 8.0 percent to USD1.7 billion.

Manufacturing activity has strongly rebounded, with the purchasing managers' index at 54.3 in April, the highest in four years.

All these came on the back of a whole-of-government approach to pandemic recovery.

In tandem with the national government's efforts, the Bangko Sentral ng Pilipinas implemented its own array of COVID-response measures.

In sum, the central bank has injected over PhP2.2 trillion, or approximately US$ 41.9 billion into the financial system. This is equivalent to about 11.3 percent of GDP.

Even as the country transitions from one administration to another - and this will take place on July 1st - the Bangko Sentral ng Pilipinas will continue to fulfill its mandate of ensuring sound macroeconomic management.

On the whole, there are clear signs that the new administration will continue the key reforms and programs of the outgoing administration.

As the economy recovers, the central bank recognizes the need to scale back its extraordinary measures.

The timing and conditions of the BSP's exit strategy will continue to be guided by the inflation and growth outlook over the medium term, the state of public health, and domestic and global risks to the economy.

Earlier, the BSP provided provisional advances to the national government of P540 billion – or approximately USD10.3 billion - in 2020 and 2021. It was down to P300 billion as of January 2022. And to date, the national government has fully paid the central bank's advances to the national government.

Unwinding the extraordinary measures was one of the messages highlighted during the IMF-Word Bank Spring Meetings held last April. Balancing the need to safeguard economic recovery and controlling inflation would be a key challenge for policymakers going forward.

The balancing act requires a well-planned, well-calibrated, and well-communicated exit strategy to avoid causing substantial market volatility, reduce potential spillovers, and continue the recovery momentum.

For the Philippines, economic recovery came sooner than expected. The economy grew by 8.3 percent in the first quarter of this year. We expect the economy to grow much faster in Q2, making the growth target for this year of 7.0-8.0 percent doable.

Moreover, employment is nearing its pre-pandemic rate.

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In response to these developments, we have started the normalization process. We recently raised the policy rate by 25 basis points to 2.25 percent last May 19.

The government's fiscal space allowed it to spend massively on COVID-19 response without incurring unmanageable debts.

We reformed the tax system. We simplified the tax structure, rationalized fiscal incentives, reduced personal and commercial income tax rates, increased excise taxes on oil, cigarettes, and sweetened beverages.

With the new tax system, the incoming administration will be in a better position to face the challenges of the post-COVID economy.

The Philippines also enjoys healthy external accounts, with hefty gross international reserves that served as buffer during this pandemic.

Meanwhile, the peso depreciated by 2.43 percent to ₱52.27 as of May 23 from its end-2021 level. This mirrors the market sentiment affecting all emerging markets across the globe amid the Russia-Ukraine conflict. The movement of the peso is within the range of the National Government's macroeconomic assumptions for the year.

We keep our market-determined exchange-rate policy and we intervene only to ensure orderly market conditions and to prevent excessive short-term volatility in the exchange rate.

The stable banking system—which benefitted from regulatory reforms over the years—remains able to provide credit to consumers and businesses. Loan growth is steadily picking up.

Prudent lending standards of banks also help keep the rise in bad debts within manageable levels while ample capitalization enables them to absorb shocks.

On digital transformation, the central bank's policy agenda includes digitalization of the country's payments system.

By 2023 or next year, we aim to digitalize at least half of all financial transactions and onboard at least 70 percent of all Filipino adults into the formal financial system.

Complementing our digitalization agenda is the new Financial Consumer Protection Act. The law improves the resolution mechanisms for financial consumer complaints including those involving cybercrimes.

The BSP has also issued six digital banking licenses, in line with our Digital Payments Transformation Roadmap.

On sustainability, the central bank is at the forefront of promoting sustainability principles in the financial sector.

We have issued regulations requiring banks to incorporate such principles into their operations.

We are also among the early investors in the Bank of International Settlements' Green Bond Fund and the Asian Green Bond Fund.

The Philippine government did not let this unprecedented crisis go to waste. It did not sit idly by and wait for the coronavirus to subside. Instead, it continued to pursue game-changing reforms that help make the Philippines a preferred investment destination.

The government sustained the reform momentum in consonance with its pandemic response.

For instance, it pursued the passage of the Corporate Recovery and Tax Incentives for Enterprises or CREATE Act, which cut corporate income tax to make it competitive with our ASEAN neighbors and we rationalized the fiscal incentives system.

In addition, three landmark laws further opened the Philippines to foreign investors: the amended Retail Trade Liberalization Act, the Foreign Investments Act, and the Public Services Act.

These game-changing reforms will help stimulate the economy, generate more jobs, improve basic services to Filipino consumers and allow for the exchange of skills and technology with the country's foreign partners.

Over the last six years, the Philippines invested massively in infrastructure under the "Build, Build, Build" program, which I originally called the Golden Age of Infrastructure in the Philippines.

The goal is to make up for past neglect which earned the Philippines the distinction of having one of the poorest public infrastructures in the ASEAN region.

From 2016 to 2020, infrastructure spending as percent of GDP averaged 4.6 percent. In 2021, actual infrastructure spending reached PHP1.1 trillion or 5.8 percent of GDP.

One thing is certain: the incoming administration will inherit a better state of infrastructure to help in its socioeconomic agenda. The next administration will inherit a robust pipeline of implementation-ready infrastructure projects. A total of 88 infrastructure flagship projects for completion next year and beyond will be up to the next administration to continue.

Taking all these into consideration, we are optimistic about the Philippine economy. We expect the economy to grow by 7.0 to 8.0 percent this year, and by 6.0 to 7.0 percent next year and beyond.

That said, like the rest of the world, the Philippines faces risks to its growth outlook. Among
are deterioration in the COVID situation and a prolonged Russia-Ukraine conflict.

While the IMF has cut its global economic growth forecast in its April 2022 World Economic Outlook or WEO, it raised its GDP growth projection for the Philippines from 6.3 percent to 6.5 percent this year.

On COVID-19, the Philippines is managing risks of potentially new variants emerging through sentinel surveillance and protecting the vulnerable population through accelerated vaccination.

As of May 17, 68.8 million out of the target 90 million Filipino population have already been fully vaccinated.

Now on the Russia-Ukraine conflict, the channel through which we see the most material impact is on domestic prices, but even here, we expect this to be manageable.

Based on the most recent BSP forecast, inflation this year could average 4.6 percent – much lower than what you see in the developing world, but that is slightly above our target range of 2.0 to 4.0 percent. And by next year, we expect inflation to average 3.9 percent, which is within our target band.

The BSP supports timely implementation of targeted non-monetary measures by the national government to prevent price pressures from broadening. These include direct financial transfers to vulnerable sectors, and efforts to boost domestic production and importation of certain food commodities.

For its part, the central bank is prepared to take preemptive action when there are stronger indications of possible disanchoring of inflation expectations.

Before the pandemic hit, we were on our way to A-level credit rating.

While the virus set us back, the Philippine economy was strong and the Duterte administration carried on its game-changing reforms. Not surprisingly, all the international and regional rating agencies unanimously affirmed the Philippines' investment-grade ratings throughout the pandemic despite a wave of ratings downgrades for many advanced and emerging economies.

Now, the next administration has to continue the country's pursuit of A-level rating. This can be done by crafting, among others, a well-thought-out fiscal consolidation framework, which has been prepared by the Executive Department and ratified by Congress.

So why take interest in the Philippines?

The Philippines is currently in a demographic sweet spot. It has a younger population compared with the rest of the world. It has a rich talent pool, having an annual average of 750,000 graduates across disciplines, forming a deep manpower pool of 45 million well-educated and hard-working workforce. In an ageing world, having a population with a median age of 25.7 is an asset.

Moreover, the Philippines' location is favorable for key markets as it is situated at the heart c
trading routes.

At the height of the pandemic, as I said earlier, we didn't sit idly by and wait for the virus to recede. Instead, we pushed for game-changing reforms. We continued to invest in physical infrastructure and human capital. All these are meant to improve the Philippines' competitiveness, boost its productive capacity, and make the Philippines an even more attractive investment destination.

In closing, we invite you to continue engaging with us. We thank our partners in Spain who have played significant roles in the Philippine economic narrative.

And for those who have yet to do business with the Philippines, we urge you to take a look at our promising economy as we soar to new heights.

Thank you and good morning.