





Navigating Risks and Sustaining Growth: Outlook for the Philippines

THE MANILA TIMES ECONOMIC FORUM

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Outline

1. External Environment
2. Recent Developments
3. Outlook
4. Risks and Policies

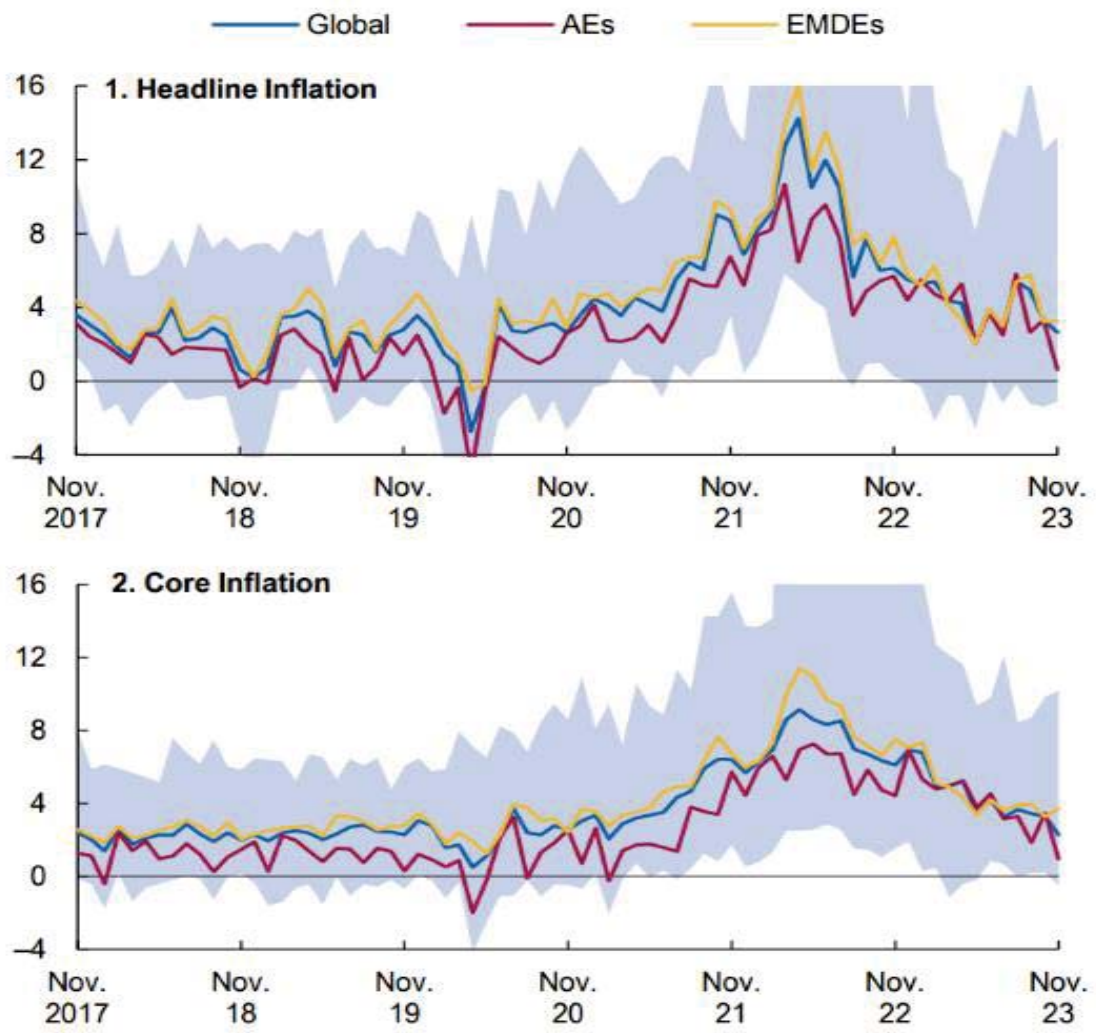
External Environment

Global Outlook

Moderating inflation and steady growth opens a path to soft landing

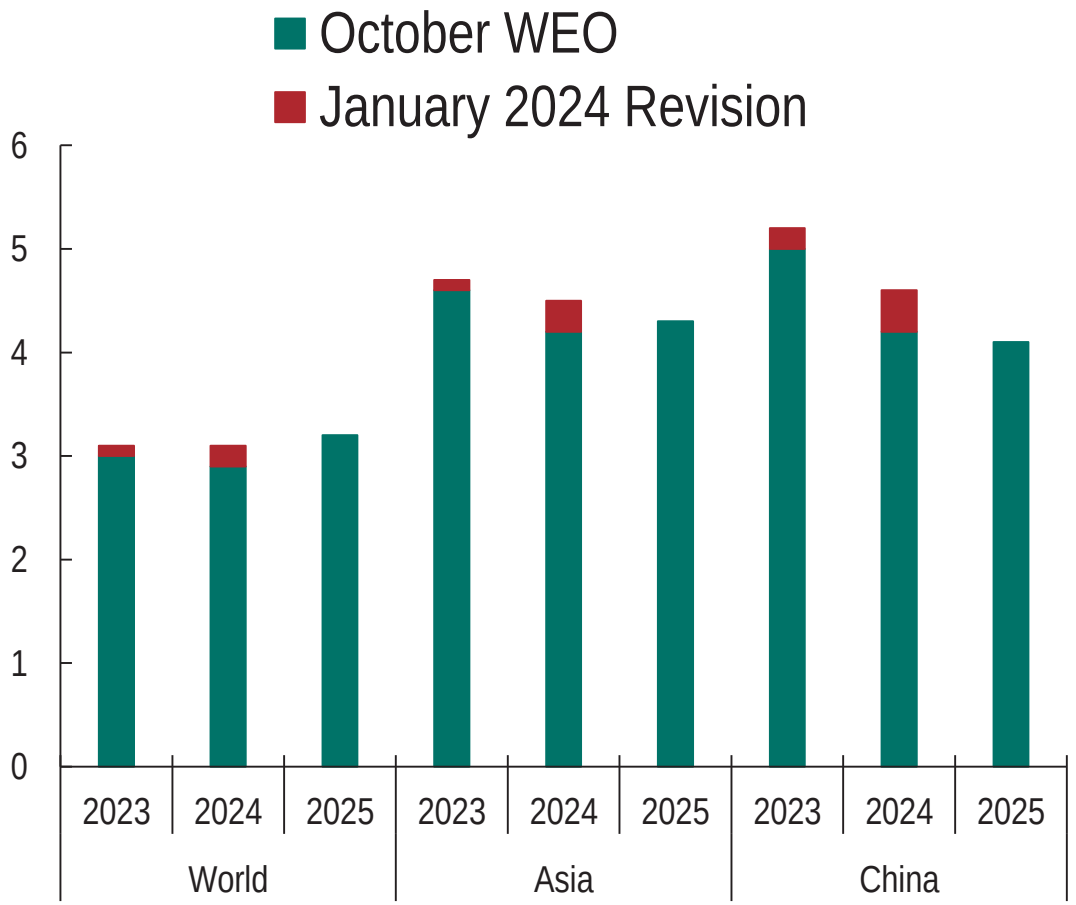
- Growth has proven resilient.
  - *Global growth is projected at 3.1 percent in 2024 and 3.2 percent in 2025*.
- Inflation is falling faster than expected in most regions.
  - *Global headline inflation is expected to fall to 5.8 percent in 2024 and 4.4 percent in 2025.*
- With disinflation and steady growth, the likelihood of a hard landing has receded

Figure 1. Global Inflation: Rise and Fall
(Month-over-month annualized percent change, seasonally adjusted)



Asia Remains The World's Most Dynamic Region

- Asia is on-track to again contribute two-thirds to global growth.
- Asia growth is estimated at 4.7 percent in 2023 and 4.5 percent in 2024
  - carryover effects, supportive external environment, and policy stimulus in some cases.
- For 2025, growth is projected 4.2 percent, largely reflecting China's growth slowdown
- Inflation is on a steady decline (esp. EM Asia) and on course to reach target in 2024.



Source: January 2024 World Economic Outlook

Key Risks and Policies to Strengthen Resilience in the Region

Risks

- **China**: upside and downside risk
- Tighter-than-expected financial conditions and geopolitical fragmentation

Policies

- **Monetary.** Manage the final descent of inflation to target.
- **Fiscal.** A renewed focus on fiscal consolidation to restore buffers and safeguard debt sustainability.
- **Financial Sector.** Strong financial supervision and monitoring of financial sector vulnerabilities.
- **Structural Reforms.** Boost productivity while accelerating the green transition.

Recent Developments

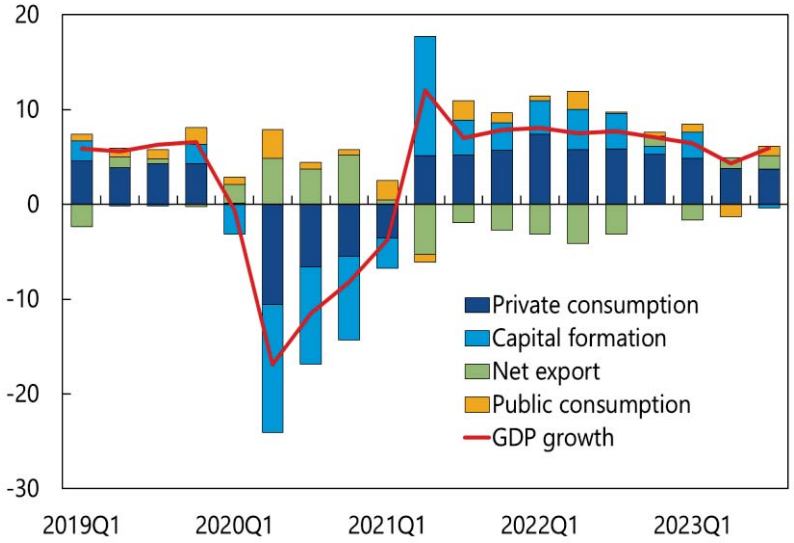
Real Sector

The economy started cooling down with policy tightening in Q2 2023, even though it regained momentum in the second half of the year

Private investment has lagged growth

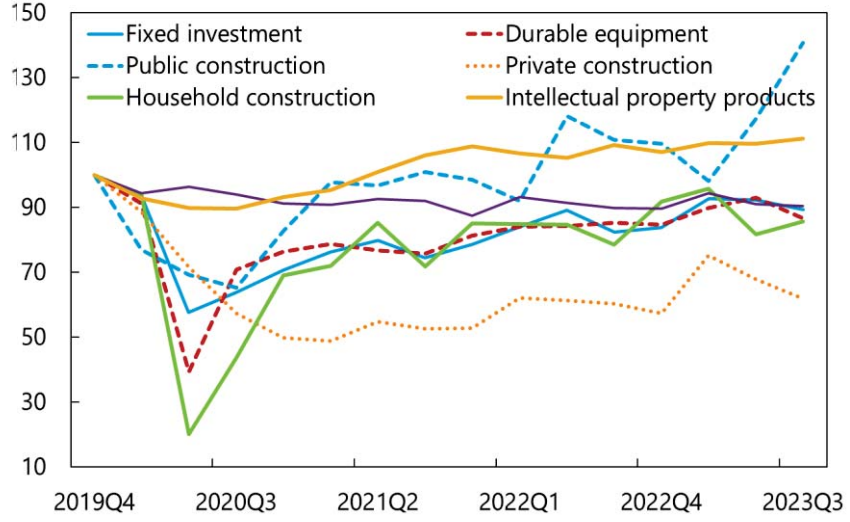
Increased vacancy rates in real estate markets are weighing on the recovery of private construction.

Contribution to Growth
(In percent)



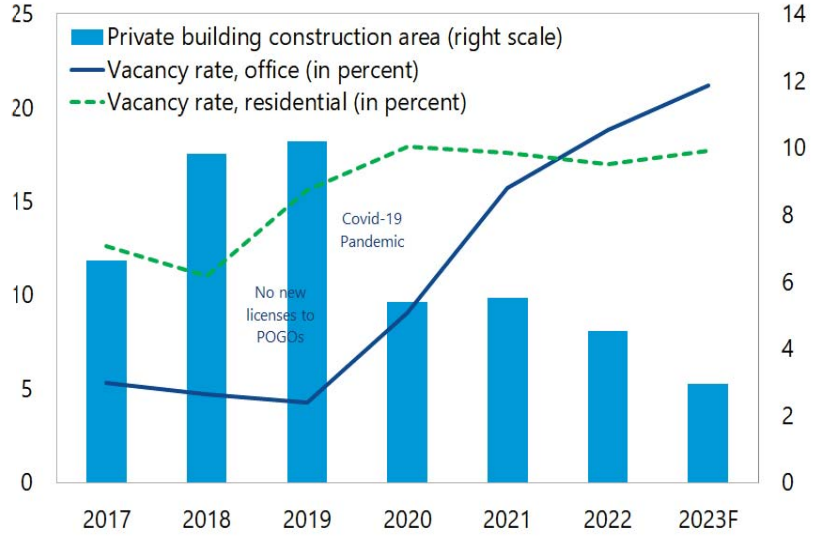
Sources: Haver Analytics; and IMF staff calculations.

Breakdown of Fixed Investment
(2019 Q4=100, seasonally adjusted)



Sources: Haver Analytics; and IMF staff calculations.

Vacancy Rates and Construction Area in Metro Manila
(In million square meter)



Sources: Colliers; CEIC Co. Ltd.; and IMF staff estimates.

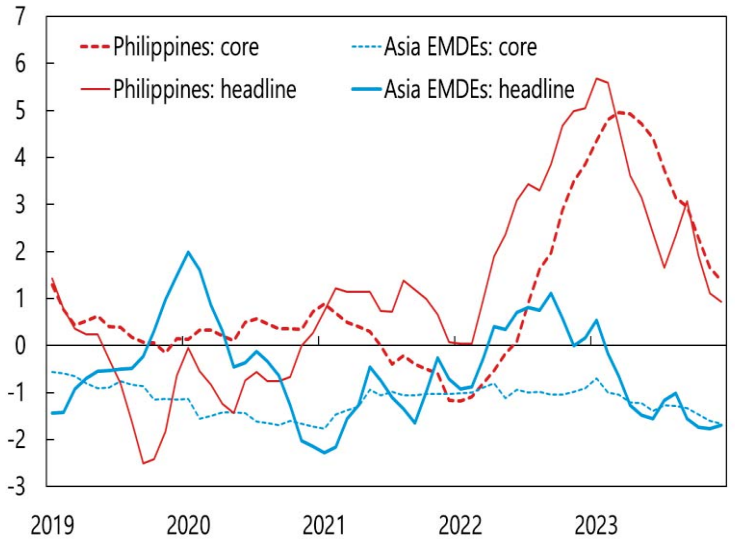
Inflation Developments

Headline inflation has recently decelerated, but pressures subsist.

The tightening of labor market conditions has contributed to the rise in core inflation.

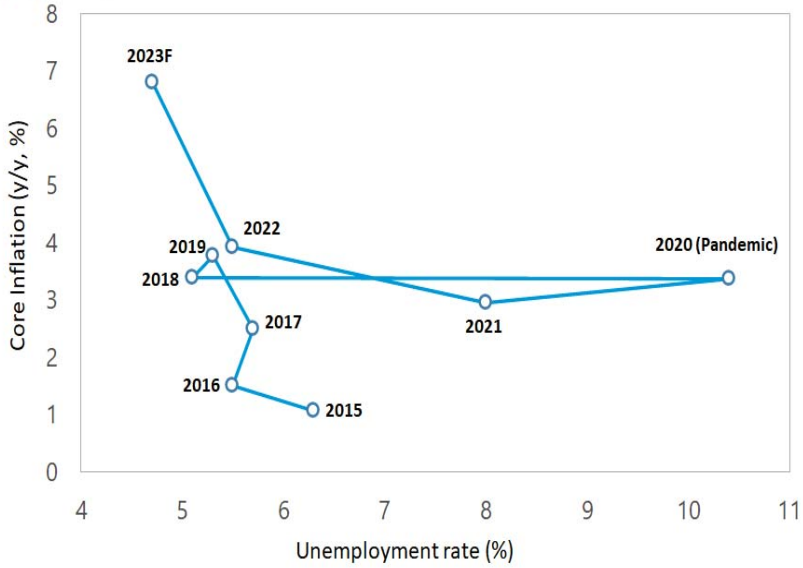
Key food prices, including rice, remain volatile.

Headline and Core Inflation
(In percent, deviation from headline target)



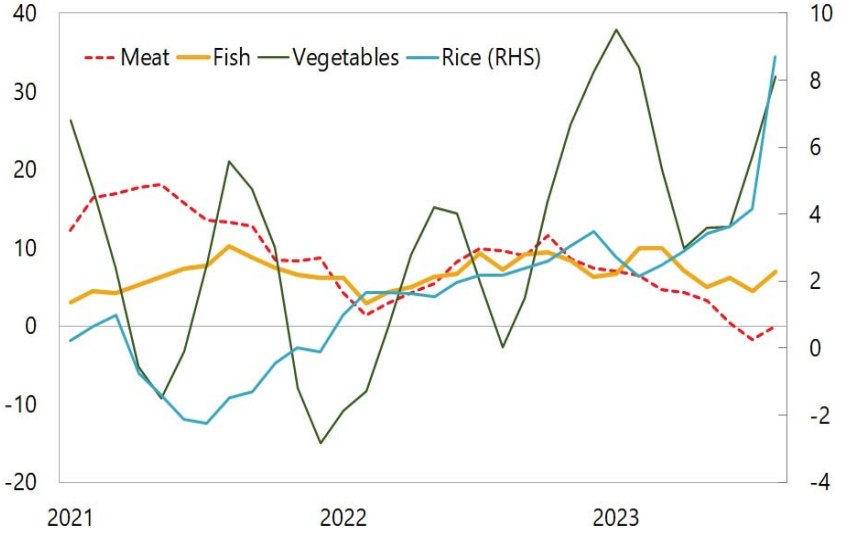
Sources: Haver Analytics; and IMF staff calculation.
Note: Asia EMDEs includes China, India, Indonesia, Malaysia, Philippines, Thailand, and Vietnam.

Core Inflation and Unemployment Rate, 2015-2023
(In percent)



Sources: Haver Analytics; and IMF staff estimates.

Key Food Prices
(Percent change, year-on-year)

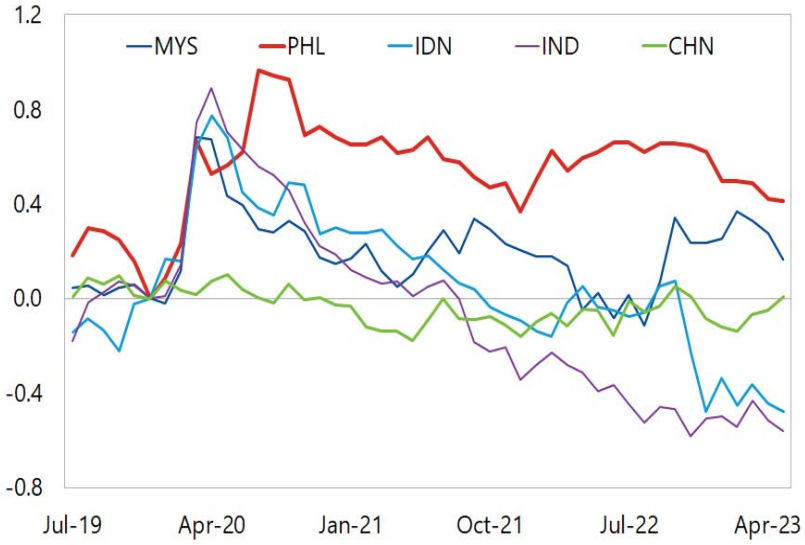


Sources: Haver Analytics; and IMF staff estimates.

Financial Conditions

Conditions in the Philippines tightened by more than in other ASEAN countries.

Selected Asia: Financial Conditions
(Index, December 2019=0, +=tighter)



Source: IMF staff calculations.

...affecting real estate loan growth in particular...

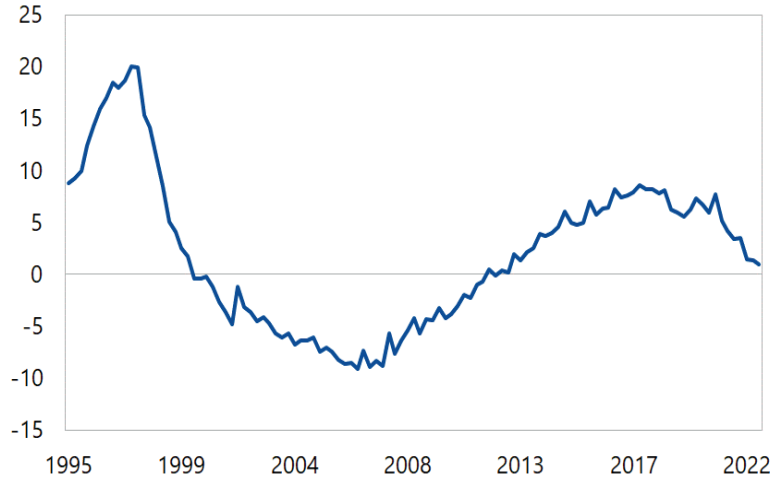
Residential Real Estate: Bank Loan and Price Growth
(Percentage change, year-on-year)



Sources: Bangko Sentral ng Pilipinas; and IMF staff estimates.

...and closing the credit gap.

Credit Gap
(In percent)



Sources: IMF, Systemic Risk Tracker.

Outlook

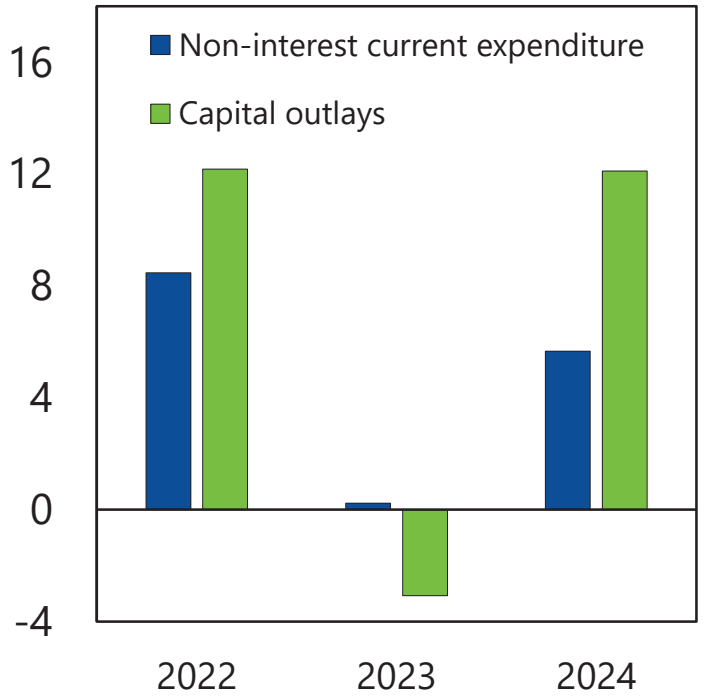
Growth Outlook

GDP growth is expected to pick up in 2024…

	2022	2023	2024
World	3.5	3.1	3.1
USA	2.1	2.5	2.1
Asia	3.9	4.7	4.5
Japan	1.0	1.9	0.9
ASEAN-5	5.5	4.2	4.7
Philippines	7.6	5.6	6.0
China	3.0	5.2	4.6
India	7.2	6.7	6.5

… supported by public spending catching up and expanding infrastructure investment…

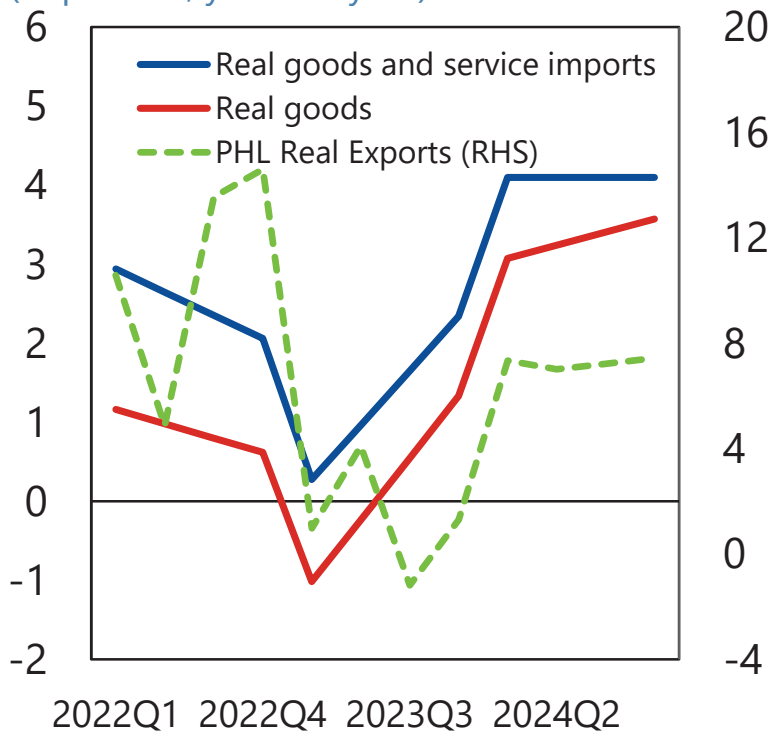
National Government Expenditure
(In percent, yoy)



Sources: Philippine authorities; and IMF staff projections.

…and an improving outlook for external demand.

Real Imports Demand and PHL Exports
(In percent, year-on-year)



Sources: IMF Staff projections.

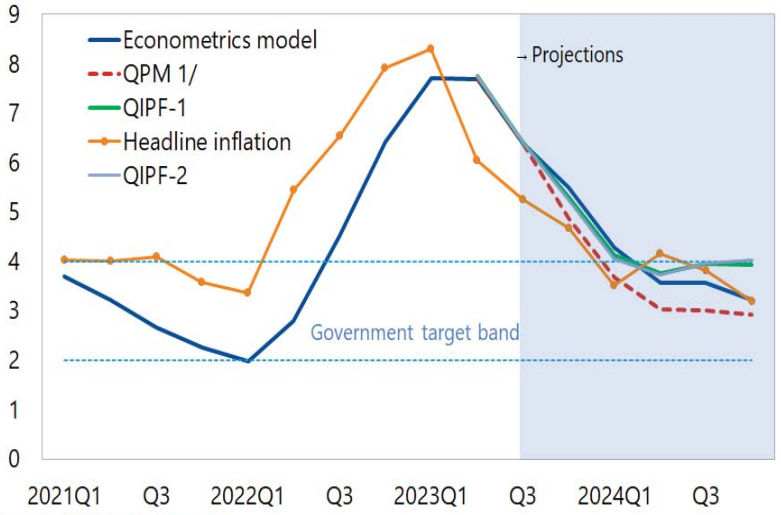
Inflation Outlook

Inflation is projected to remain in line with the target band in early 2024, but with some volatility…

… as commodity price risks are skewed to the upside especially oil…

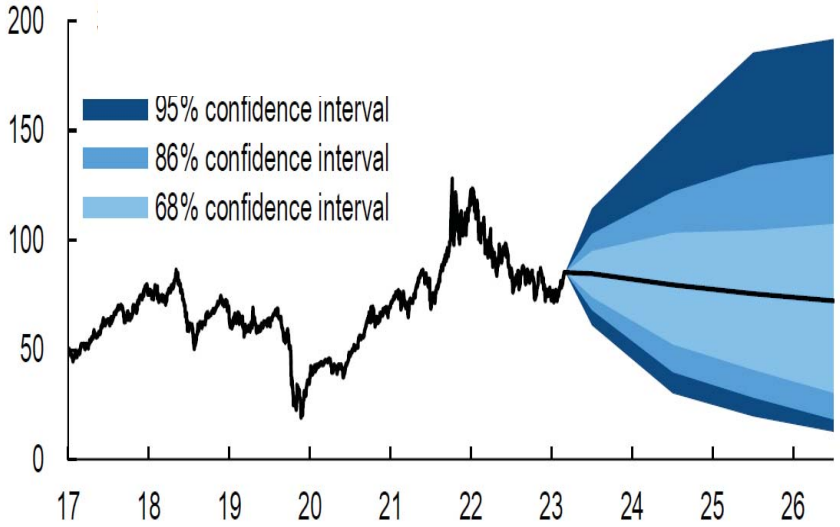
… and rice.

Core Inflation Projections
(In percent)

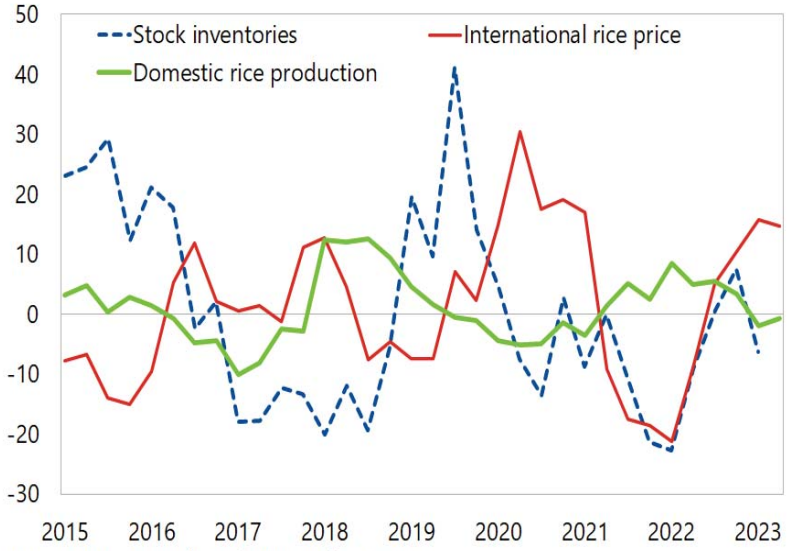


Source: IMF staff estimates.
1/ QPM forecast is based on GAS/WEO-consistent external projection made by ICD's G3MOD with a forthcoming ICD working paper.

Brent Price Medium-term Prospects
(US dollars a barrel, four-year futures)



Risks on Rice
(In percent, year-on-year growth)

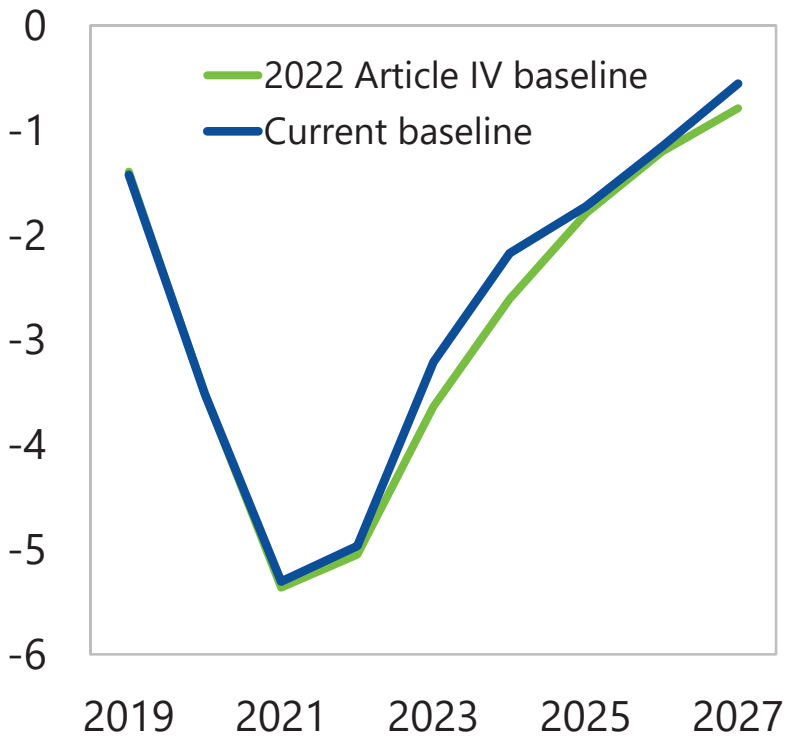


Sources: CEIC Co. Ltd.; and IMF staff estimates.

Fiscal Consolidation will anchor debt sustainability

The pace of fiscal consolidation outlined in the MTFF is appropriate.

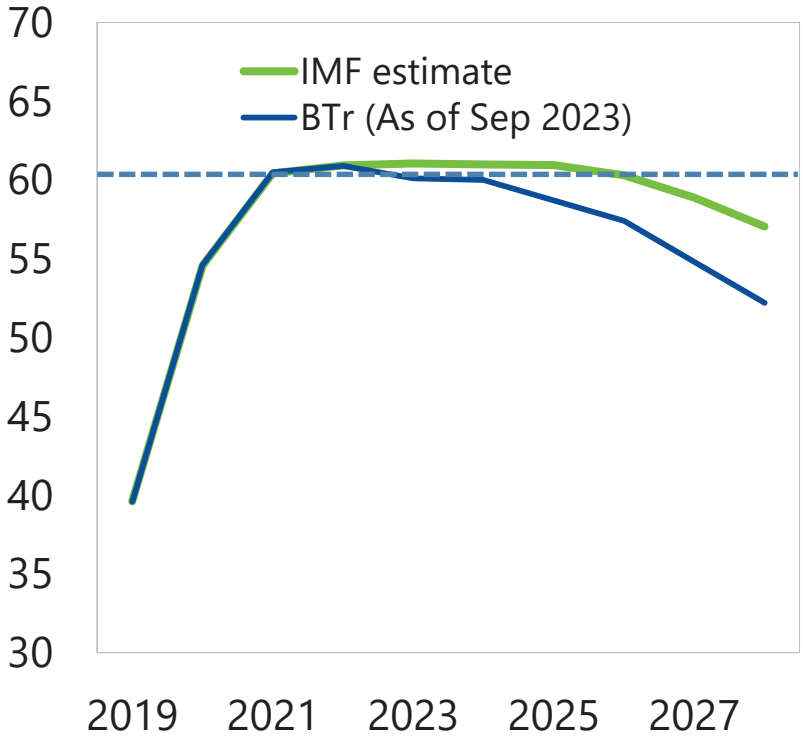
Cyclically Adjusted Primary Balance
(In percent of GDP)



Source: IMF staff estimates.

The consolidation will reduce the national government debt-to-GDP ratio…

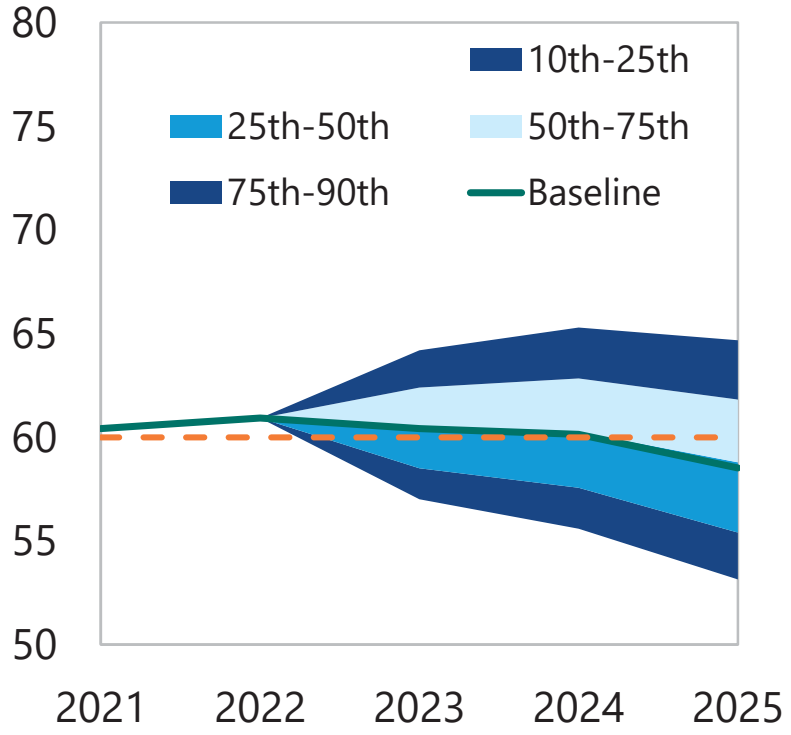
National Government Debt
(in percent of GDP)



Sources: Haver; and IMF staff estimates.

…but with limited safety margin to reach 60 percent by 2025.

National Government Debt
(In percent of GDP, no shocks to primary balance)



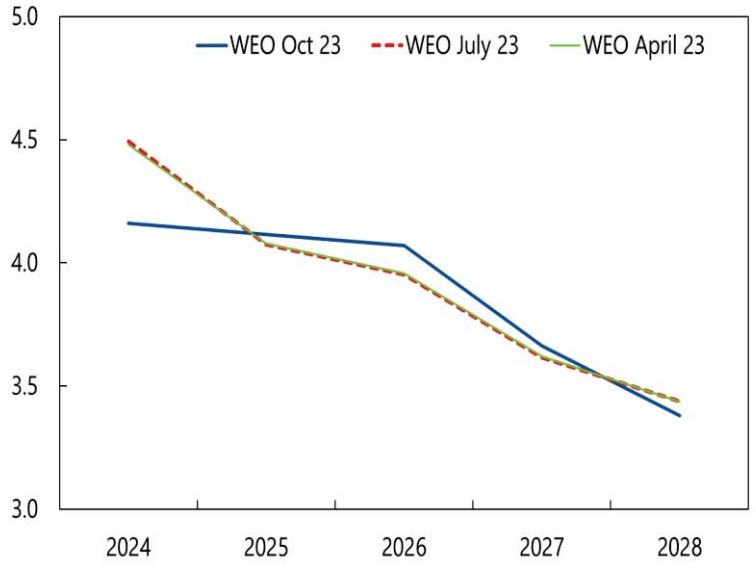
Sources: Philippines authorities; and IMF estimates.

Risks to the Outlook and Policies

Risks to the growth outlook

Growth in China is expected to be slower than earlier projections but could slow further, especially in the near term…

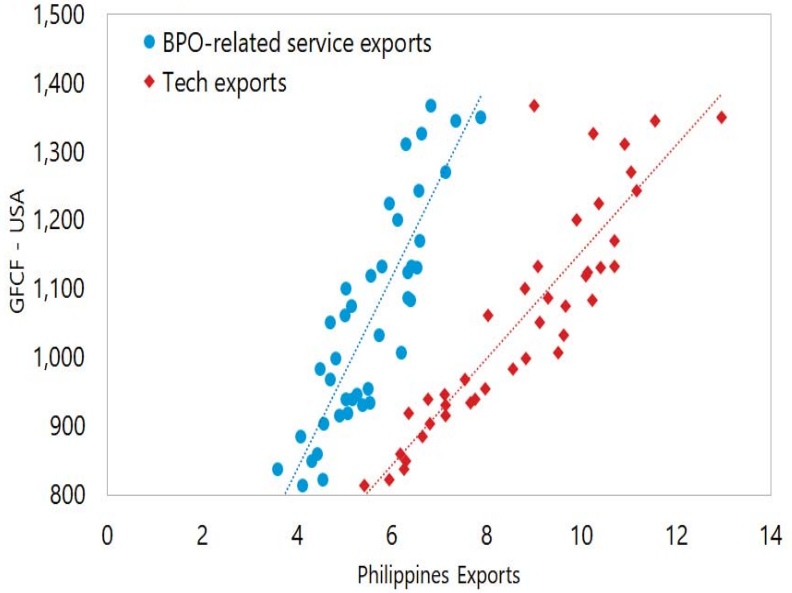
China: Baseline Medium-Term Growth Projection
(In percent)



Source: IMF, World Economic Outlook.

…and the outlook for Philippine exports will depend in large part on investment in the US…

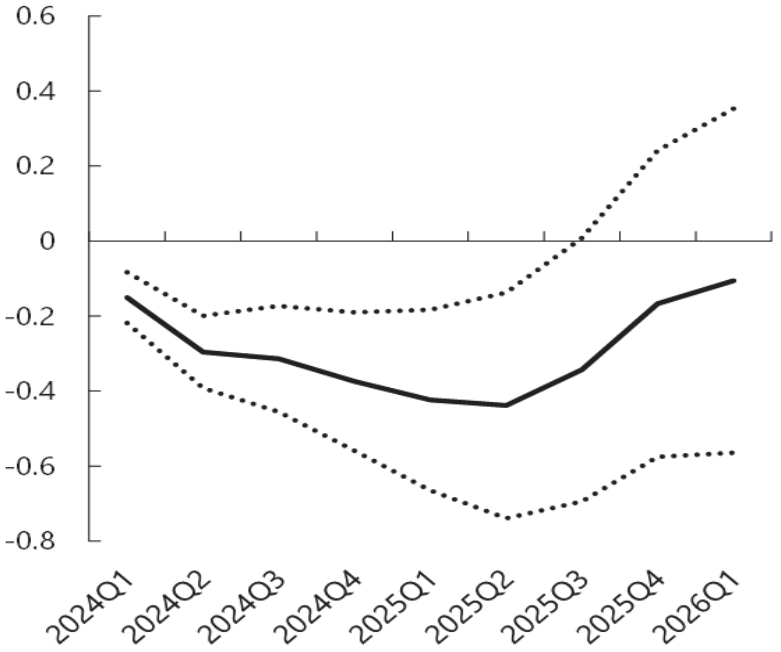
US Capex Cycle and Philippines Key Export Items
(In billions of US$)



Sources: Haver Analytics; CEIC Data Co. Ltd.; and IMF staff calculations.

…which in turn depend on US financial conditions.

Growth Spillovers from Tighter US Financial Conditions
(Percent)



Source: Copestake et al (2023), IMF Staff.
Note: GDP spillovers from 1 standard deviation increase in US Financial Conditions in 2023Q4, similar to the increase between 2021Q3 and 2022Q3. Dotted lines are 90 percent confidence intervals.

Financial Sector

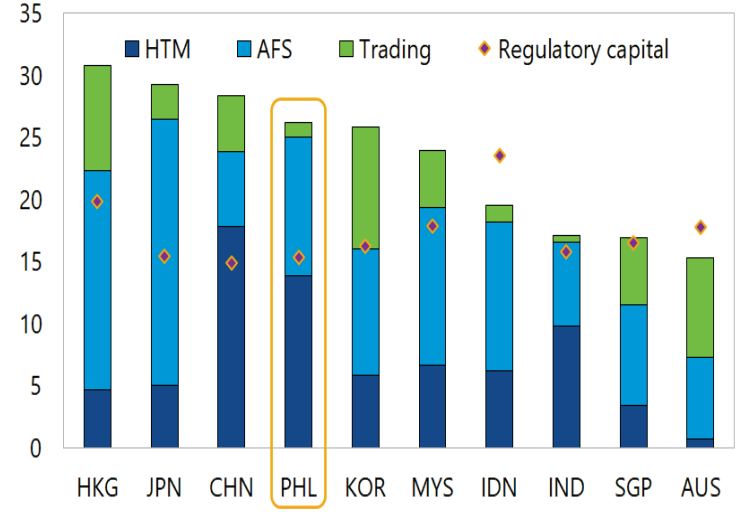
Philippines banks' high HTM share helped withstand the global banking turmoil…

…but pockets of vulnerability remain, particularly in the real estate sector…

…and the higher-for-longer environment may cause trouble for parts of the corporate sector.

Share of Banks' Mark-to-Market Securities Portfolio

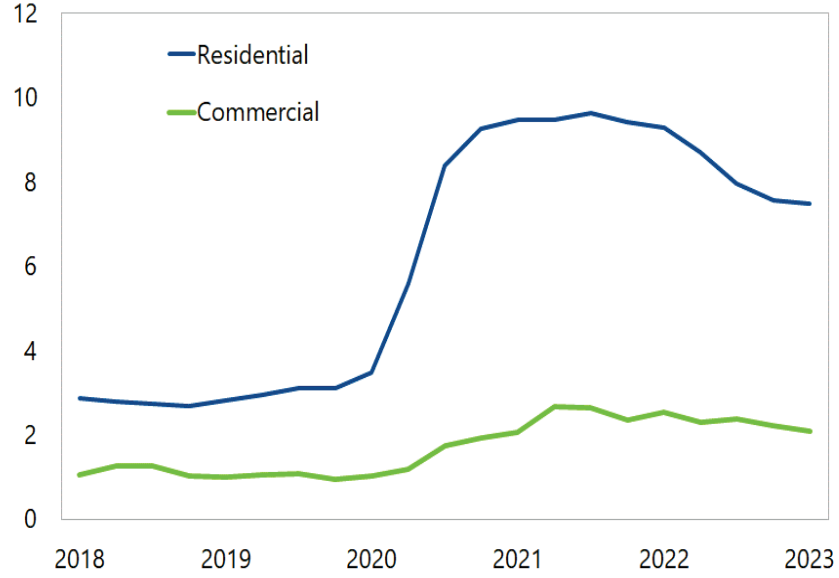
(In percent of total assets; in percent of RWA, right scale)



Sources: Fitch, Bloomberg Finance L.P.; and IMF staff calculations.
Note: MTM portfolios include held-to-maturity (HTM), available for sale (AFS), and trading book securities.
RWA= risk weighted assets.

Non-Performing Real Estate Loans

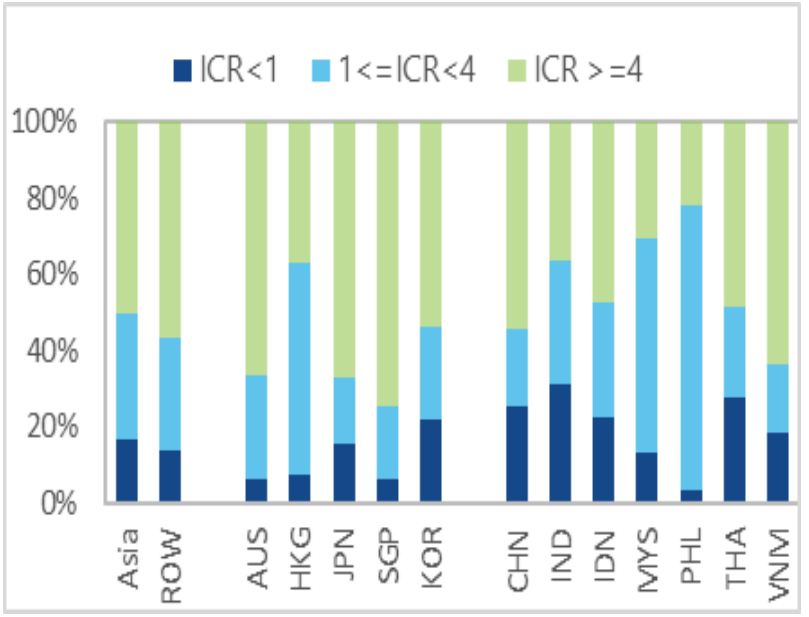
(In percent)



Sources: BSP via Haver Analytics; and IMF staff estimates.

Corporate Debt in Vulnerable Firms

(In percent of all corporate debt)



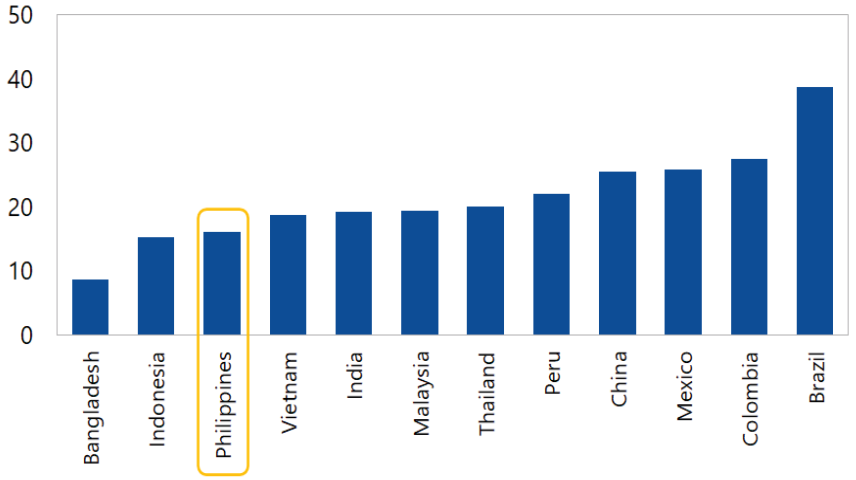
Monetary and Financial Policies

- Maintain a sufficiently restrictive stance until inflation fully returns to target and stand ready to raise interest rates further should upside risks materialize
- Consider raising risk weights or introducing a sectoral systemic risk buffer for real estate exposures
- Strengthen financial supervision and regulation by closing data gaps and expanding stress testing
- Step up efforts to be removed from the FATF grey list by publishing a credible timeline to address outstanding action items

REVENUE POLICIES

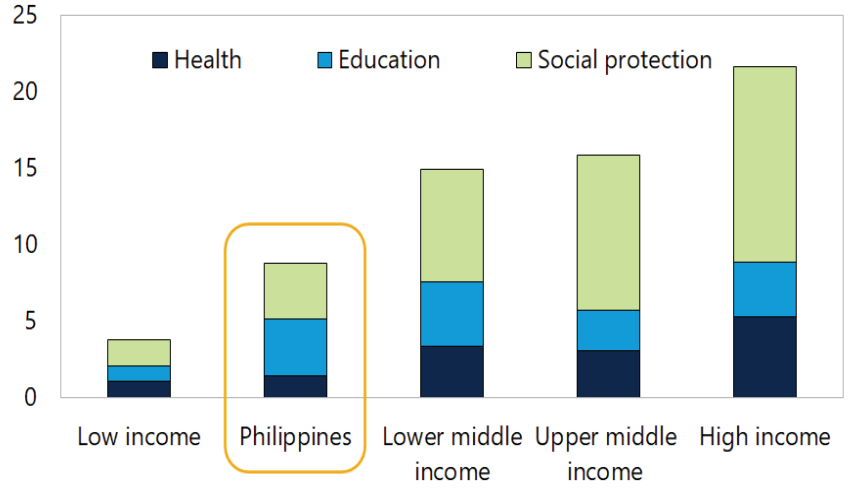
- Introduce a tax policy oriented medium-term revenue strategy to finance more social spending
  - Timely implementation of tax policy measures identified in the 2024 budget
  - Broaden VAT and CIT bases by rationalizing exemptions instead of new B2B zero-rating
  - Incentivize investment through cost-based mechanisms, e.g., expensing of capital spending
  - Step up efforts of tax administration and subsequent reform plans including digitalization plans

Government Revenue, 2022
(In percent of GDP)



Sources: IMF, World Economic Outlook; and IMF staff estimates

Social Spending by Central Government, 2020
(In percent of GDP)



Sources: Philippine authorities; IMF, *GFS database*; and IMF staff estimates.
Note: Average is calculated based on data reported to IMF adherence to the GFSM 2001/2014.

EXPENDITURE AND OTHER POLICIES

- Implement expenditure control measures and improve efficiency
  - Reform the MUP pension to be contributory and delink benefits from wage increases of current personnel
  - Step up capacity building to support fiscal decentralization to the LGUs while developing realistic transition plans
  - Continue reforms in PFM (e.g., Budget Modernization Bill, National Government Rightsizing Bill, cash budgeting, and New Government Procurement Reform Act) and rollout of IFMIS
  - Strengthen the oversight of GOCCs, PPPs, and SSIs

STRUCTURAL REFORMS TO RAISE PRODUCTIVITY AND ADDRESS THE INFRASTRUCTURE GAP

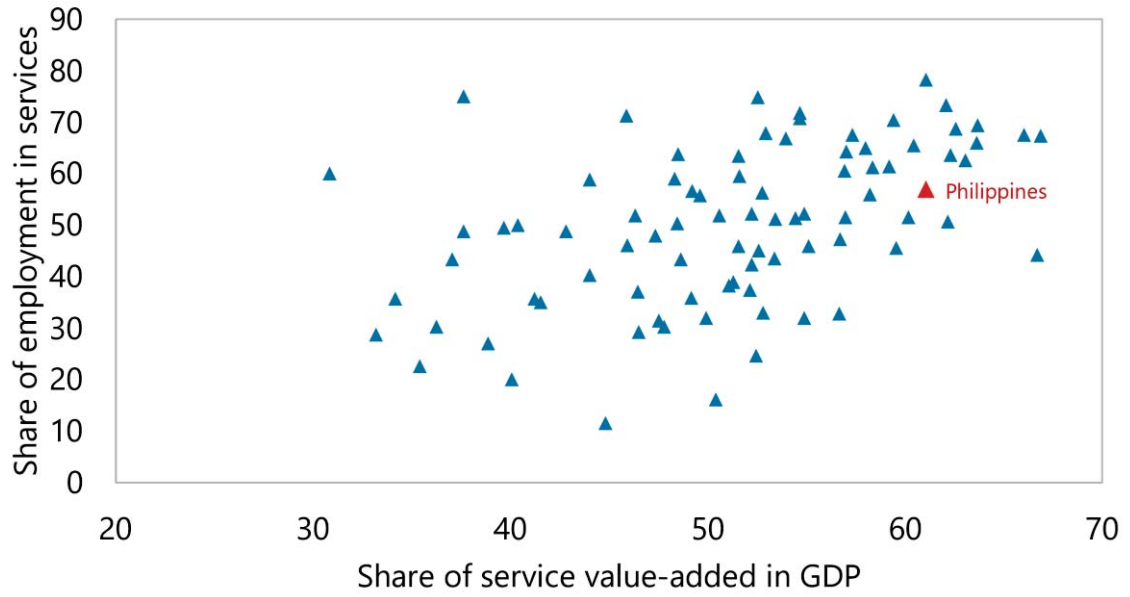
- Maximizing potential benefits of RCEP and opening up to FDI would require reforms to address supply-side issues in the agriculture sector, and removing non-tariff barriers linked to administrative procedures and regulation.
- Restart responsible mining to meet increasing demand for green minerals.
- Reduce the cost of doing business, establishment of green lanes for infrastructure projects welcome.
- Recent passage of the PPP Code will unify the legal framework for PPP projects and institutionalize best practices including fiscal risk assessments at an early stage of the process. This should contribute to closing infrastructure gaps.

STRUCTURAL REFORMS TO HARNESS THE DIGITAL ECONOMY AND FOSTER INCLUSIVE GROWTH

- Digitalization of the economy will be key to supporting the service sector-led growth engine, promoting financial inclusion, and raising the efficiency of government services
- It will require upskilling of the labor force to adapt to the rise of AI as well as efforts to develop the country's digital infrastructure
- Policies should remain focused on targeted support programs to the vulnerable such as the pilot food stamp program and 4Ps while eschewing generalized subsidies.

EMDEs: Service Sector in GDP and Employment, 2021 1/

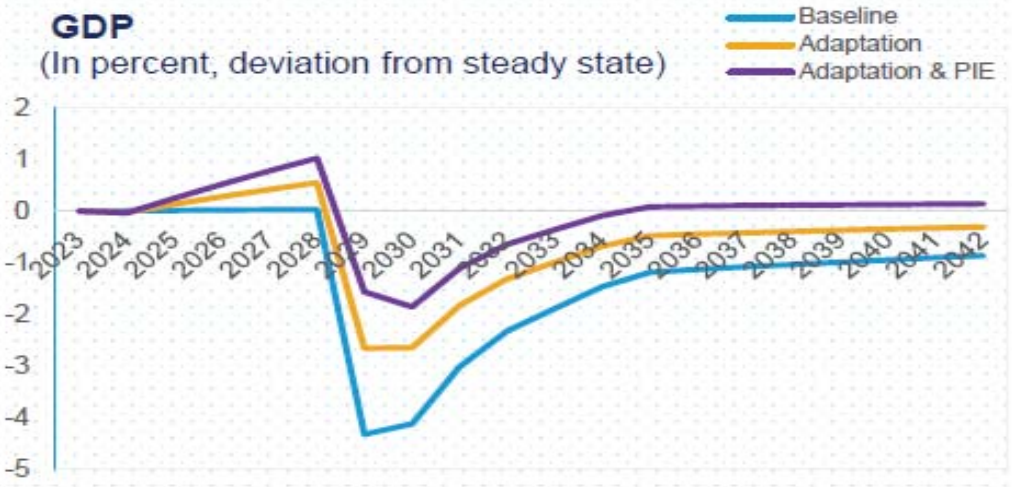
(In percent)

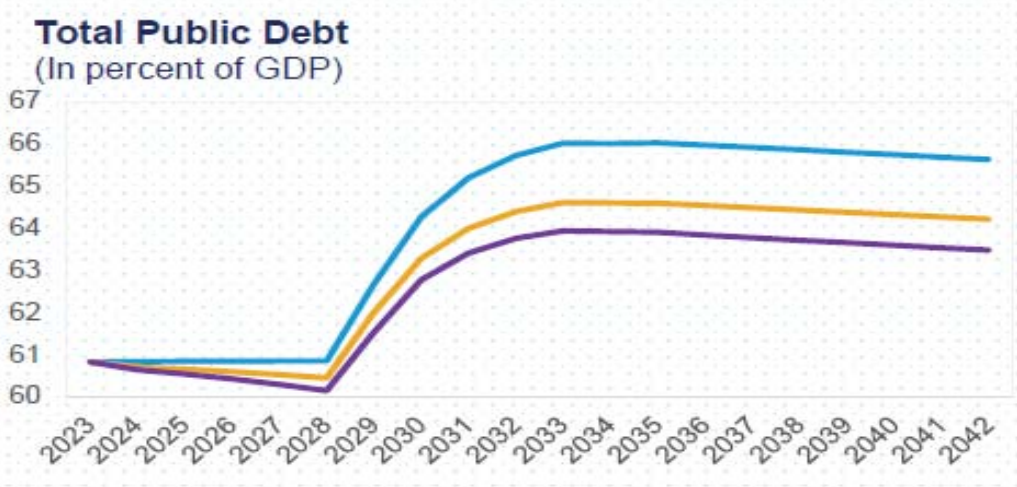


Sources: International Labor Organization, ILO-Statistics; World Bank, World Development Indicators; and IMF staff estimates.

1/ or latest data available for Emerging Market and Developing Economies (EMDEs) excluding small states and tourism dependent economies.

POLICIES TO ADDRESS CLIMATE CHANGE





- Adaptation efforts should notably focus on increasing public investment for resilient infrastructure and supporting the most vulnerable households while paying due regard to debt sustainability.
- Our simulations provide a baseline for climate adaptation needs and assessments in the Philippines.
- Mitigation efforts would benefit from the introduction of carbon pricing mechanisms as envisaged by the current administration.
- The transition to renewable energies should build on a recent measure to facilitate foreign ownership in the renewable energy sector, as well as ongoing efforts of the BSP to stimulate green finance, including through its Sustainable Finance Roadmap.

Thank you!

Salamat!