The Philippines

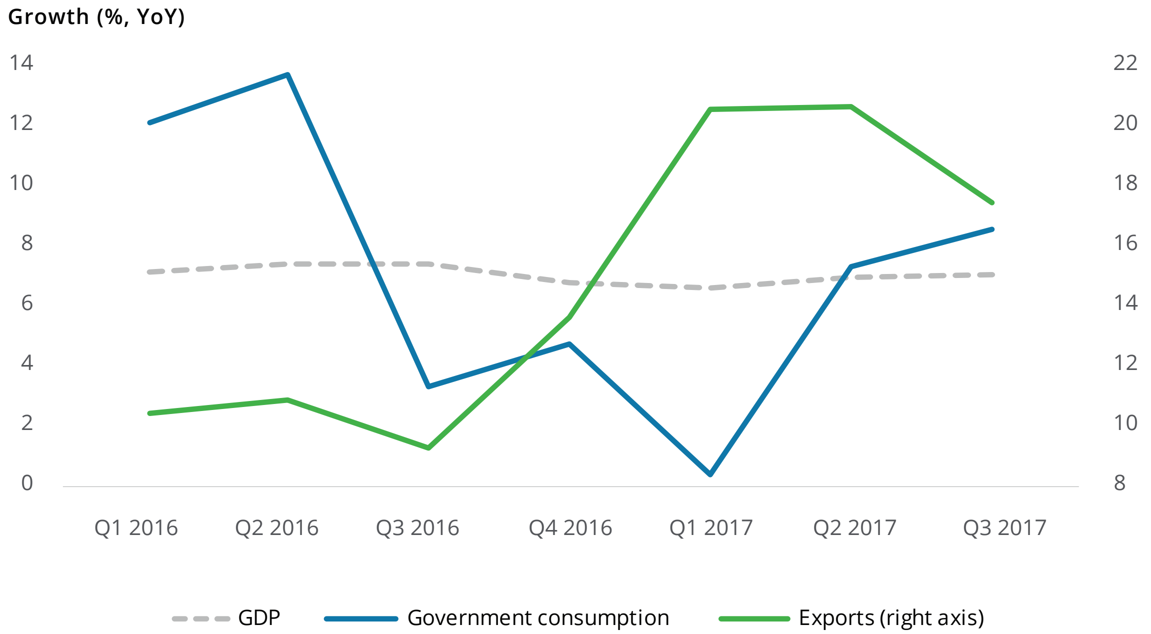
It just keeps getting better

By: Akrur Barua

Economy watchers in Asia now can't take their eyes off the Philippines—and why not? With GDP growth picking up in Q3, the economy is set for a strong annual expansion (likely 6.5–6.8 percent) this year as well. The distribution of growth among key expenditure categories is also noteworthy. Trade has been stealing the show so far this year with strong double-digit expansion in exports.

Government consumption has also picked up due to a continued focus on infrastructure development and attracting foreign capital. This has aided fixed investments as well, with businesses upbeat.[1] And although slowing remittances and an uptick in inflation dented private consumption growth in Q3, this is likely a temporary blip. Policy makers will be keen to continue this momentum through 2018, while keeping inflation in check.

Figure 1. Exports and government consumption were key contributors to growth in Q3



Source: Haver Analytics; Deloitte Services LP economic analysis.

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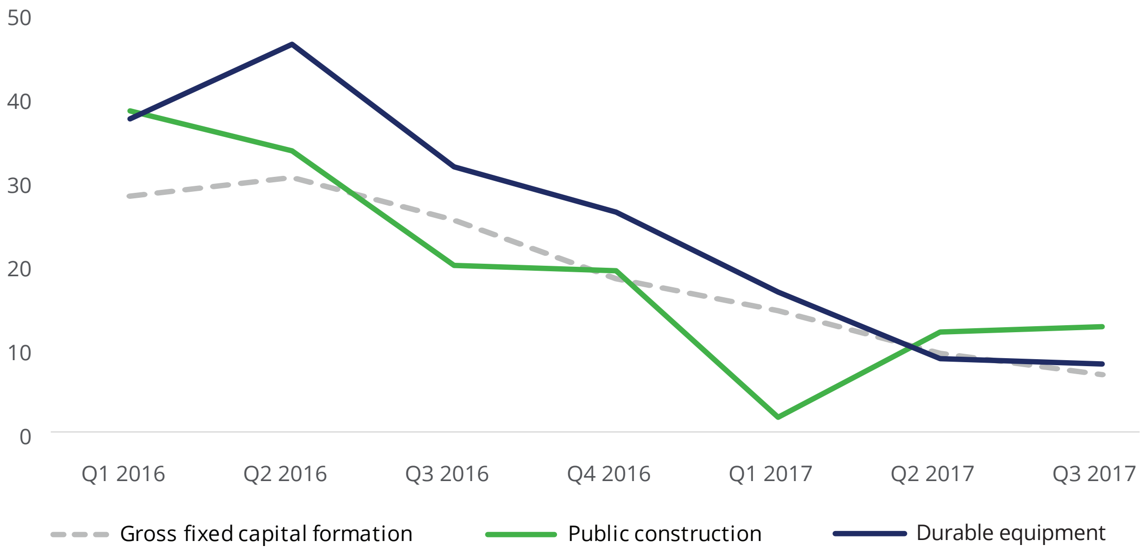
Up's the word for GDP growth

Real GDP expanded by 6.9 percent year over year in Q3 2017, up from a 6.7 percent rise in the previous quarter.[2] Exports continued to boost the economy with a 17.2 percent expansion during the quarter, although they lagged the above-20 percent growth in Q1 and Q2. With imports growth slowing a bit during the quarter, the contribution of net exports to GDP growth picked up in Q3. The momentum of exports is also visible from monthly data, although growth in exports value in US dollars slowed slightly in Q3, likely due to slowing exports to China and Japan.[3] However, rising exports to the Association of South East Asian Nations and to the United States made up for any slowdown elsewhere. The other key contributor to growth in Q3 was government consumption, which picked up pace during the quarter (figure 1).

Investments too did not disappoint despite some moderation. Durable equipment investment growth held steady at 8.3 percent in Q3, close to the previous quarter's number, while public construction—a key indicator of infrastructure development—grew by 12.6 percent. Investments are expected to remain strong in the near to medium term as the government focuses on infrastructure development and businesses thrive on strong economic momentum. However, expansion will likely be less than the heydays of 2016, given the high base over 2016–2017 (figure 2). The only minor blemish in Q3 growth numbers was private consumption, where growth slipped to 4.5 percent from 5.9 percent in the previous quarter. This was the slowest pace of expansion since Q3 2010.

Figure 2. Investments have slowed since 2016, but remain healthy



Source: Haver Analytics; Deloitte Services LP economic analysis.

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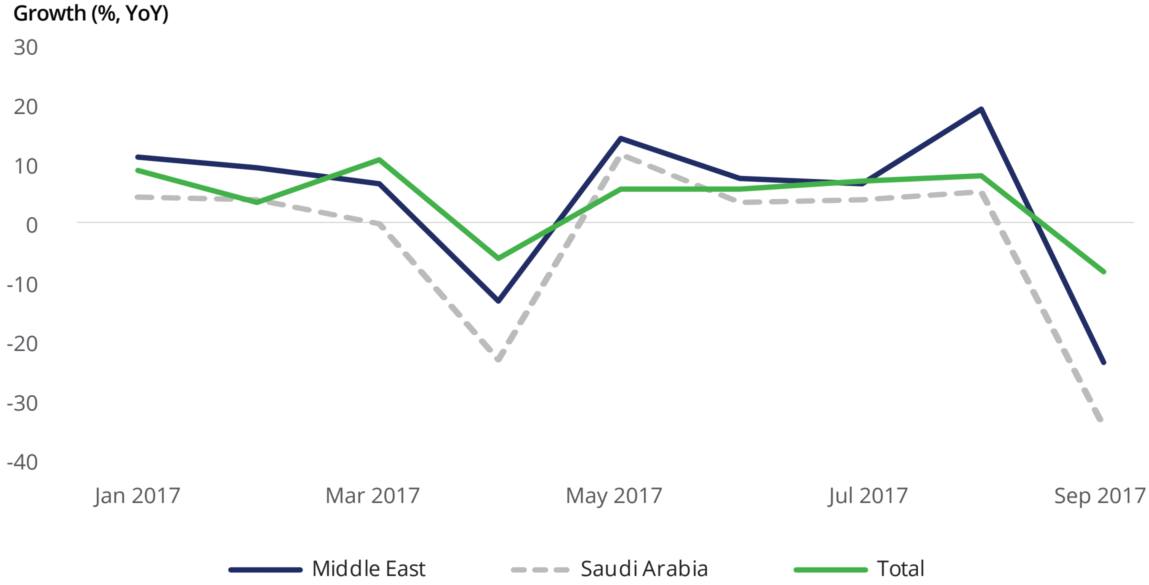
What led to the drop in private consumption growth?

The decline in private consumption growth in Q3 was despite a strong labor market, with the unemployment rate (non-seasonally adjusted) declining marginally to 5.6 percent during the quarter. There are likely two reasons that impacted private consumption growth last quarter. First, inflation has been picking up and cut into real earnings of households. In Q3, headline inflation averaged 3.1 percent year over year, marginally higher than the previous quarter and much higher than the 2.0 percent recorded a year back. Second, slowing remittances have also impacted household spending. Remittances grew by just 2.0 percent year over year on average in Q3; they fell by 8.3 percent in September. A key factor behind this trend is slowing remittances from the Middle East (figure 3), a region that accounts for the second-largest share in total remittances by overseas Filipino workers (OFWs) (figure 4). The drop in inflows from the Middle East is primarily due to the repatriation of undocumented Filipino workers from Saudi Arabia under the kingdom's amnesty program.[4] What has also weighed on remittances is the withdrawal of banking relationships with local banks by global counterparts to comply with anti-money laundering regulations.[5]

Figure 3. Remittances from Saudi Arabia fell by 34.4 percent in September



Source: Haver Analytics; Deloitte Services LP economic analysis.

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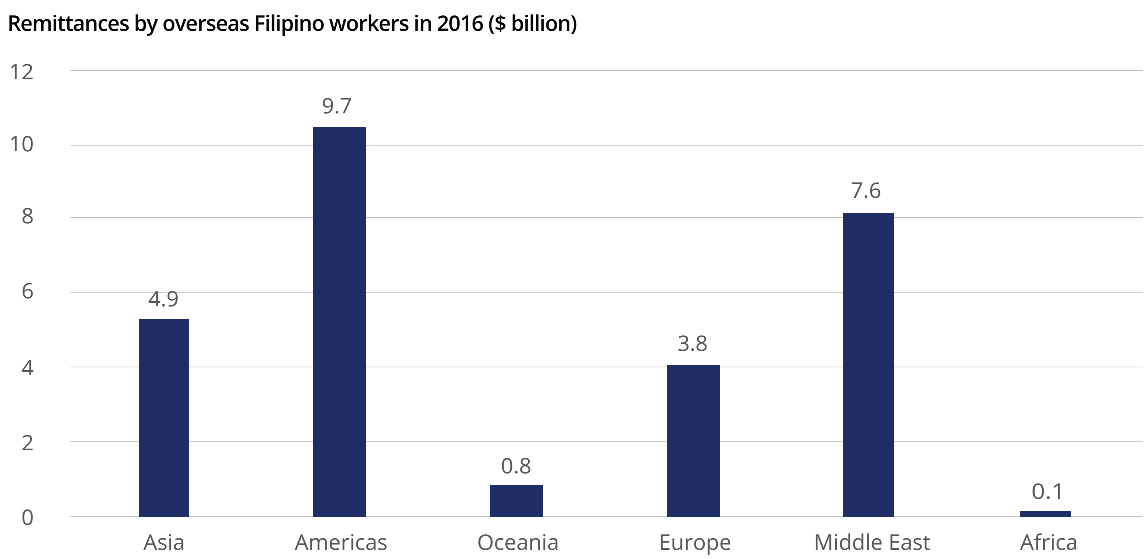
Figure 4. The Middle East accounts for 28.1 percent of total remittances by overseas Filipino workers



Source: Haver Analytics; Deloitte Services LP economic analysis.

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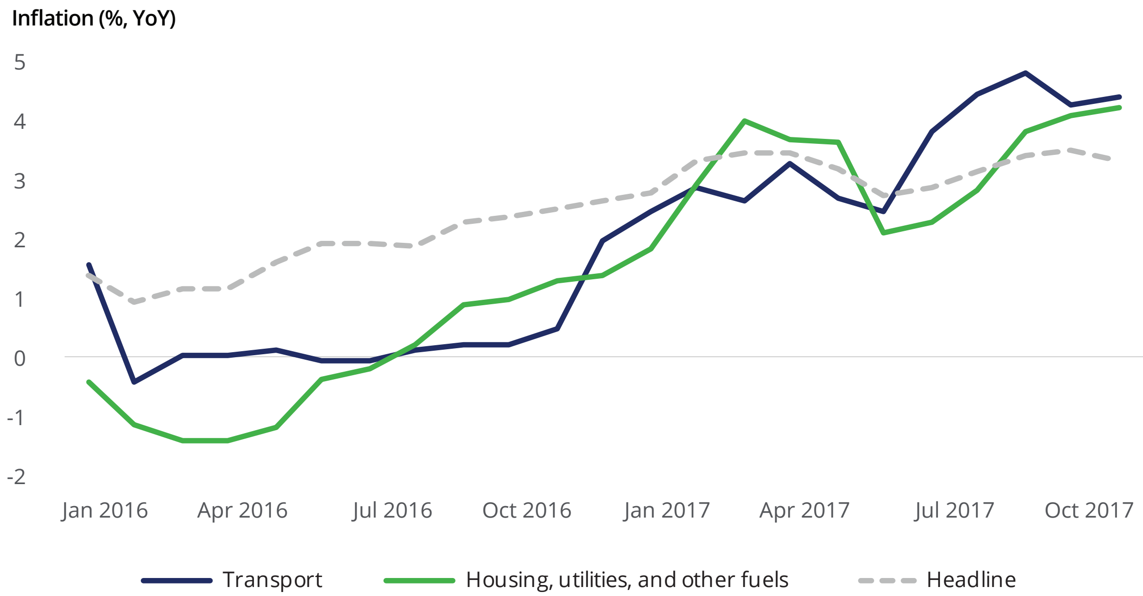
A single drop is not the whole story

The decline in private consumption growth in Q3 is, however, not a cause for concern. First, the uptick in inflation in recent quarters is likely to abate by the end of 2018 as the base effect comes into play. Headline inflation came down in November (3.3 percent) from October's nearly three-year high of 3.5 percent (figure 5). Higher fuel prices (and hence, transport prices) are likely to dissipate as global crude prices stabilize in 2018. For example, according to forecasts by the US Energy Information Administration, Brent crude price growth is expected to slow to 4.9 percent in 2018 from an estimated 21.2 percent this year; prices had fallen by 16.4 percent in 2016.[6] Most importantly, inflation is still within the central bank's target range of 2.0–4.0 percent and is hovering just above the midpoint. With policy rates still at a low of 3.0 percent, there is ample room for any monetary tightening, should the need arise.

Second, although pressure on remittances from Saudi Arabia is likely to remain in the near term, inflows are likely to stabilize in the medium term. Moreover, despite the upheaval in September, total remittances in the first nine months of the year was still up by 3.9 percent with inflows from Asia and the Americas continuing to rise at a steady pace.[7] Also, a weaker peso compared to 2016 is likely to make up some ground in terms of the peso value of remittances.[8] Finally, as economic activity continues to remain strong, domestic gains are likely to intensify, keeping private consumption healthy in the near to medium term. No wonder then that consumers appear upbeat in the consumer composite index, reflecting even greater optimism for the next three months and the next twelve months compared to the current quarter.[9] Households can thus look forward to a happy new year.

Figure 5. Inflation is still within the central bank's target range of 2.0–4.0 percent



Source: Haver Analytics; Deloitte Services LP economic analysis.

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ENDNOTES

1. Bangko Sentral ng Pilipinas, "Business expectations survey," sourced from Haver Analytics on December 11, 2017.
2. Unless mentioned otherwise, all data in this article has been taken from Haver Analytics.
3. Haver Analytics, December 11, 2017.
4. Lawrence Agcaoili, "Remittances shrink in September," *Philippine Star*, November 16, 2017.
5. Ibid.
6. US Energy Information Administration, *Short-term energy outlook*, November 7, 2017.
7. Haver Analytics, December 11, 2017.
8. Ibid.
9. Bangko Sentral ng Pilipinas, "Consumer expectations survey," sourced from Haver Analytics on December 11, 2017.

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