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Macro Note

Philippines: 2020 Posted The Worst Full-Year GDP Contraction On Record

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- The Philippine economy continued to post a contraction, albeit narrower decline of -8.3% y/y in 4Q20 (3Q20: revised upward slightly to -11.4% from -11.5%), after prolonged movement restrictions, a series of typhoons in Oct-Nov, and lower income weighed on household spending, investment, tourism-related industries, and agriculture & fisheries output. The 4Q20 GDP reading came in line with our estimate (-8.2%) but below Bloomberg consensus (-7.9%), sending the nation's economy into a -9.5% tailspin for the entire year of 2020 (2019: +6.0%).
- The pace of growth recovery may continue to be constrained by a prolonged period of movement restrictions and practising of social distancing given the rise of new coronavirus variant and uncertainty surrounding the inoculation. Both labour market conditions and overseas remittance flows are also likely to remain weak, which will subsequently weaken sentiments and depress household spending and investment, particularly in 1Q21 before showing positive gains from 2Q21 onwards. We maintain our 2021 full-year GDP growth target at 7.0%, partly aided by favourable base effects, further improvement in export sector, and continued policy support.
- An expected uptrend in inflation and a positive growth outlook painted by the central bank in the Dec 2020 monetary policy statement have raised the odds of an extended rate pause this year. The persistence of negative real interest rates and narrowing interest rate differentials with other central banks may also be on the radar of BSP before making any policy rate decision in the near term. Hence, we expect BSP to keep the overnight reverse repurchase rate unchanged at 2.00% until end-2021. The next Monetary Board meeting is scheduled on 11 Feb.

GDP Contraction Narrowed Further In 4Q20

The Philippine economy continued to post a contraction, albeit narrower at -8.3% y/y in 4Q20 (3Q20: revised upward slightly to -11.4% from -11.5%), after prolonged movement restrictions, a series of typhoons in Oct-Nov, and lower income weighed on household spending, investment, tourism-related industries, and agriculture & fisheries output. The 4Q20 GDP reading came in line with our estimate (-8.2%) but below Bloomberg consensus (-7.9%), sending the nation's economy into a -9.5% tailspin for the entire year of 2020 (2019: +6.0%). The 2020 full-year GDP contraction appears to be the steepest drop among ASEAN members and marked the worst recession since data began in 1948. On a seasonally adjusted q/q basis, real GDP increased for the second straight quarter by 5.6% (3Q20: +8.0%), affirming that the economy is on a slow recovery path.

All sectors pencilled in contractions, albeit moderate in 4Q20.

1. The decline in **services** sector narrowed to -8.4% (from -10.5% in 3Q20), with tourism-related sub-sectors (i.e. accommodation & food services activities, wholesales & retail trade, and transport & storage), education, and real estate sub-segments remaining hard-hit by the prolonged COVID-19 containment measures. That said, there were three services sub-sectors shining bright during this health crisis, namely information & communication (4Q20: +3.6%; 3Q20: +2.1%), financial & insurance activities (4Q20: +4.4%; 3Q20: +4.3%), and public administration & defence services (4Q20: +0.6%; 3Q20: +4.7%).
2. The fall in **manufacturing** activities more than halved to -4.3% (from -9.9% in 3Q20), predominantly due to increased demand for electrical & electronics, chemical, and food products. The gradual re-opening of economic activities and increasing global demand particularly related to technology items for e-commerce, work from home, and health safety purposes have also lent a helping hand to the recovery in manufacturing sector.
3. **Construction** sector still posted double digit contraction of -25.3% (3Q20: -39.7%) across all sub-segments. Construction work done by financial & non-financial corporation recorded the steepest fall (4Q20: -48.0%; 3Q20: -39.0%), followed by that of households (4Q20: -32.2%; 3Q20: 58.4%) and general government (4Q20: -15.2%; 3Q20: -28.3%).

4. **Agriculture, hunting, fishery & forestry** sector reversed course and shrank by -2.5% in 4Q20 (3Q20: +1.2%). It was led by a broad-based decline across all farm output such as rough rice (4Q20: -1.1%; 3Q20: +15.4%), livestock (4Q20: -13.0%; 3Q20: -7.7%), and poultry & eggs (4Q20: -4.9%; 3Q20: -3.6%). Activities in fishing & aquaculture sub-sector also witnessed a significant drop of -4.3% (3Q20: +2.1%) as a result of adverse weather during the quarter.
5. **Mining & quarrying** sector posted a deeper fall of -18.8% (3Q20: -14.2%), with all but nickel ore production contracting last quarter.

On the aggregate demand side, the persistent **government spending** albeit moderated (4Q20: +4.4% y/y; 3Q20: +5.8% y/y), marginal **stock replenishment** activities (4Q20: +0.1ppts to GDP; 3Q20: -0.6ppts off GDP), and continued positive **net trade** contribution (4Q20: +4.4ppts to GDP; 320: +4.4ppts to GDP) were the three main pillars supporting the overall economic recovery in 4Q20. These helped to partially offset the sluggishness in **household consumption** (4Q20: -7.2%; 3Q20: -9.2%) and **investment** (4Q20: -28.6%; 3Q20: -37.1%) amid soft labour market conditions and falling capital expansion by businesses outside technology, telecommunication, and agriculture space. Although the nation's unemployment rate had peaked at 17.6% in April and improved to 8.7% in October, it is still high by historical standards and above pre-pandemic level of sub 5.0%.

Gradual And Uneven Growth Recovery Ahead

Given that daily COVID-19 cases at home remain high with a new coronavirus variant emerging and the inoculation is still subject to uncertainty, the Philippines' recovery pace may continue to be constrained by a prolonged period of movement restrictions and practising of social distancing. Both the labour market conditions and overseas remittance flows are also likely to remain weak until the vaccine is proven to be effective and safe as well as further reopening of economic activities back to optimal levels. Weaker sentiment in the near term is likely to depress household expenditure and private investment, particularly in 1Q21 before showing strong and sustain improvement from 2Q21 onwards.

On 25 Jan, President Rodrigo Duterte reinstated an order preventing children aged 10 to 14 years old from going outdoors as a precaution against the spread of the new coronavirus strain. He added that the order will subsist until such time that everybody will be safe by the vaccine. On the same day, Finance Secretary Carlos G. Dominguez said the national government has set aside PHP82.5bn in funds for the vaccination program that would cover doses for 57-60 million Filipinos, while the remaining 10-13 million would be covered by local governments and the private sector. In total, the Philippine government targets to inoculate 70 million people aged 18 and above (or about 63% of population) by end-2021, with the initial vaccine shipments arriving in Feb.

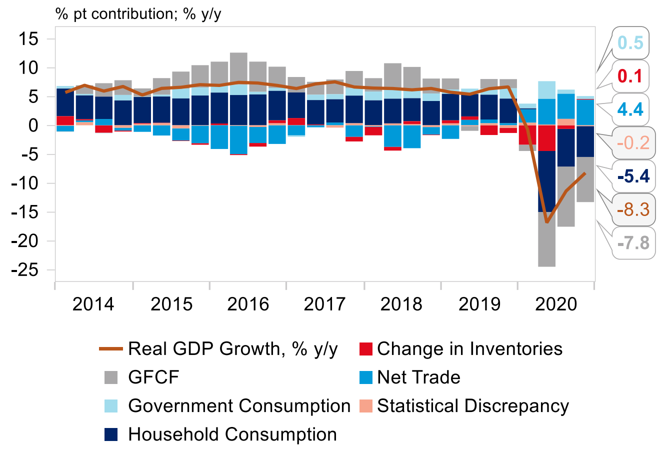
That said, year-ago low base effects, hopes for government expediting infrastructure projects and effectively executing the PHP4.506tr of 2021 national budget (or equivalent to 21.8% of GDP), the continuation of accommodative monetary policy, as well as improving export orders in tandem with recovering global demand are key growth drivers for this year. We maintain our 2021 full-year GDP growth forecast at 7.0% for the Philippines (official forecast: 6.5%-7.5%; 2020: -9.5%).

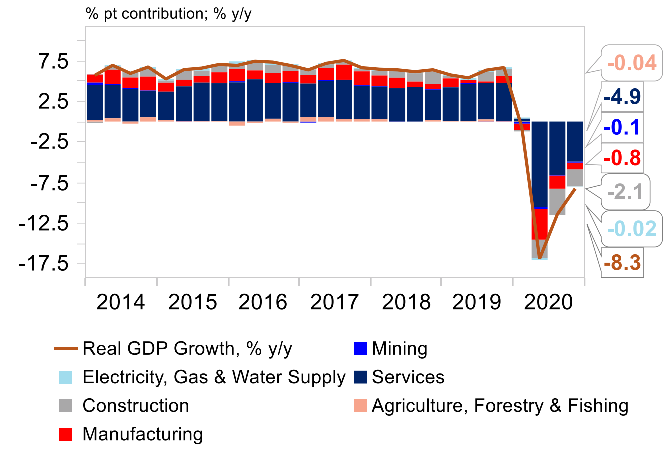
Expecting Policy Rate To Remain Unchanged Until End-2021

An expected uptrend in inflation and a positive growth outlook painted by the central bank in the Dec 2020 monetary policy statement have raised the odds of an extended rate pause this year. The trajectory of inflation is projected to hover above BSP's mid-point of the 2.0%-4.0% target for the greater part of 2021, before easing back to below 3.0% in the later part of the year and towards 2022. This comes on the back of supply-pushed factors including rising global oil prices and the outbreak of African Swine Flu (ASF), as well as base effects. Agriculture Secretary William Dar said the government is considering a cap on the prices of pork at PHP300/kg and dressed chicken at PHP160/kg amid rising costs in the capital region, Manila for 60 days. It also plans to triple pork imports as the ASF cut supplies and drove prices higher.

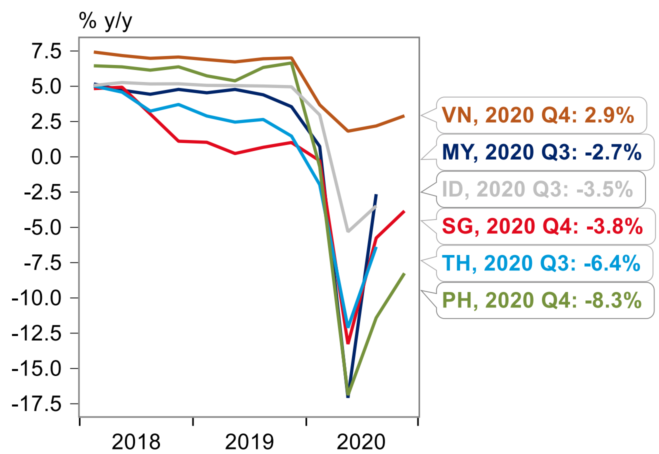
In addition, expectations of a wider distribution of vaccines and effective execution of larger 2021 national budget would further sustain the growth recovery as the year progresses. BSP Governor Benjamin Diokno earlier this month (6 Jan) said the key interest rate will likely remain on hold at least through the first half of 2021 as the economy recovers. The persistence of negative real interest rates and narrowing interest rate differentials with other central banks may also be on the radar of BSP before making any policy rate decision in the near term. Hence, we expect BSP to keep the overnight reverse repurchase rate unchanged at 2.00% until end-2021. The next Monetary Board meeting is scheduled on 11 Feb.

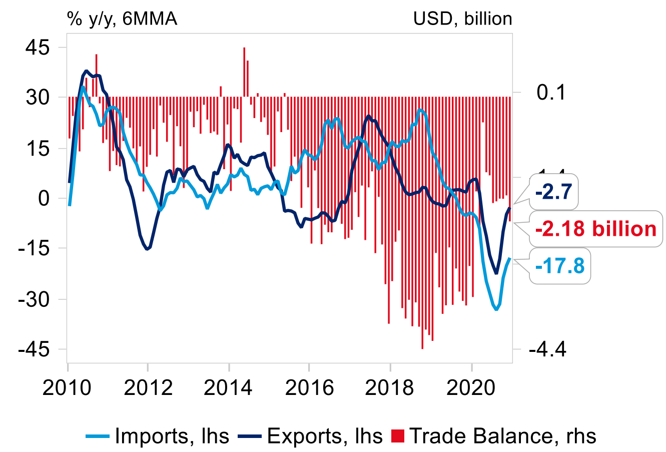
Household Consumption Remained Sluggish In 4Q20	All Sectors Posted Negative Growth In 4Q20
Source: Macrobond, UOB Global Economics & Markets Research	Source: Macrobond, UOB Global Economics & Markets Research



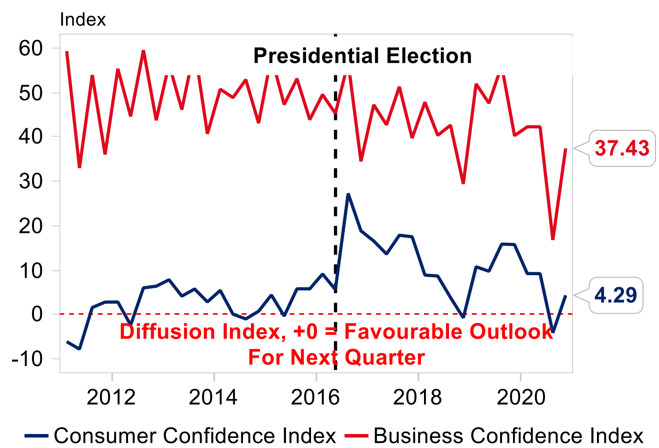


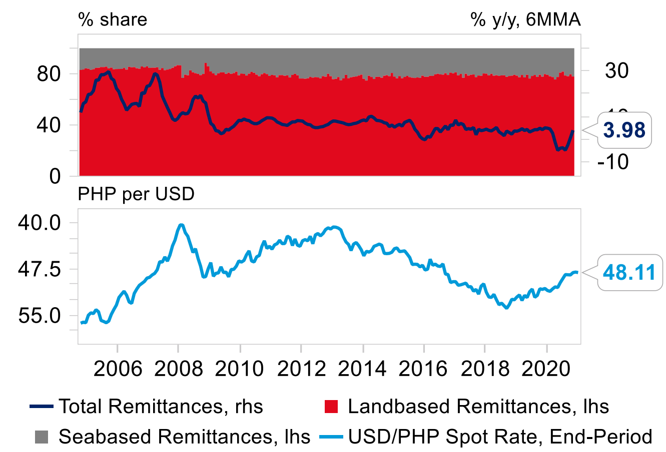
Regional Countries' GDP Performance In 4Q20	Gross Export And Import Performance
Source: Bloomberg, UOB Global Economics & Markets Research	Source: Macrobond, UOB Global Economics & Markets Research





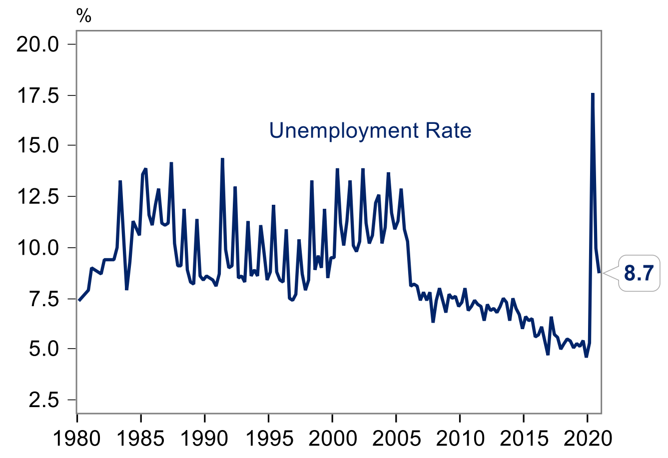
Business And Consumer Sentiment Still Weak	Slow Overseas Remittance Inflows Despite A Stronger Peso
Source: Macrobond, UOB Global Economics & Markets Research	Source: Macrobond, UOB Global Economics & Markets Research





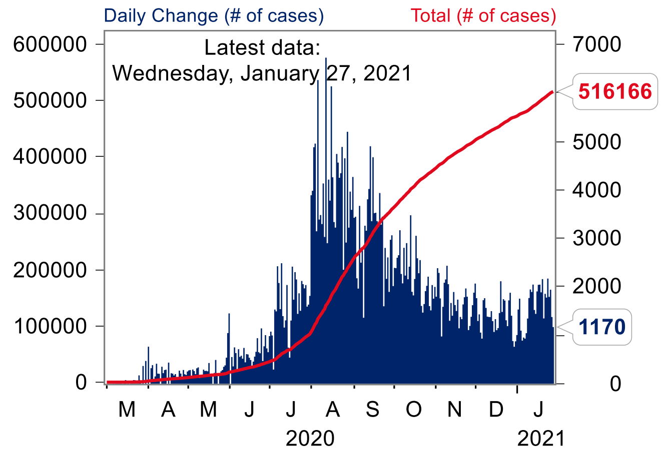
Unemployment Rate Improved Further To 8.7% In 4Q20

Source: CEIC, UOB Global Economics & Markets Research



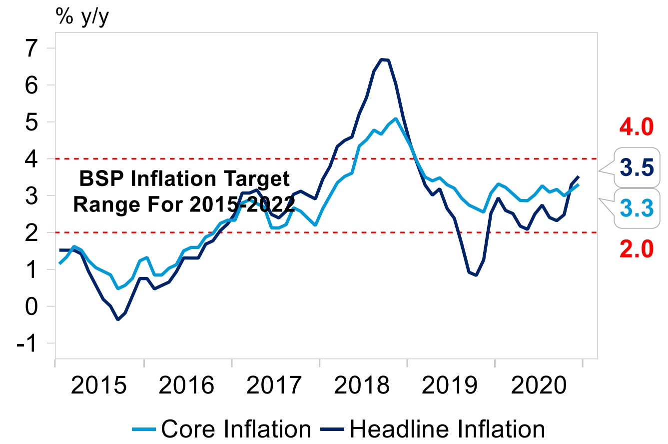
COVID-19 Confirmed Infections In The Philippines

Source: Macrobond, UOB Global Economics & Markets Research



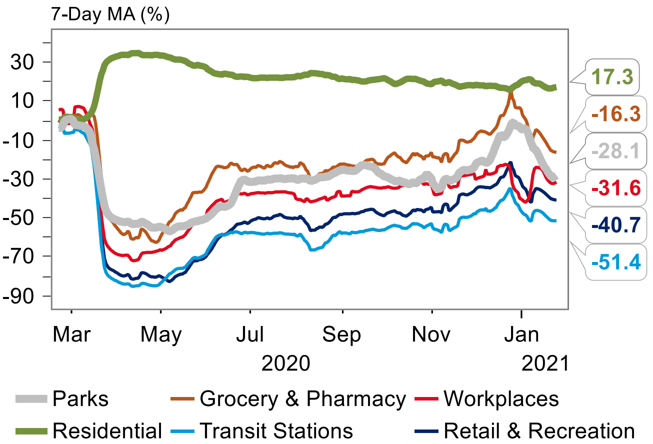
Headline Inflation Stayed Within BSP's Target Range

Source: Macrobond, UOB Global Economics & Markets Research



Philippines' Google Mobility Index

Source: Macrobond, UOB Global Economics & Markets Research



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