Philippines: election year to deliver 7-9% growth? Curb your enthusiasm

Philippine GDP grew 5.6% in 2021, but can the economy sustain this momentum?

We remain optimistic about the growth outlook for the Philippines

Recent economic performance

The Philippines managed to string together a decent run of three-quarters of gross domestic product (GDP) growth in 2021. Aided by a favourable base and helped along by the gradual easing of mobility restrictions, full-year GDP growth settled at 5.6%, better than the official growth target of 5-5.5%. Despite the better-than-expected performance, it has become clear that growth momentum was held back during Covid-19 waves induced by new variants. During these periods, the national government was forced to reinstate mobility restrictions, weighing on momentum.

Strong growth in 2022? Curb your enthusiasm

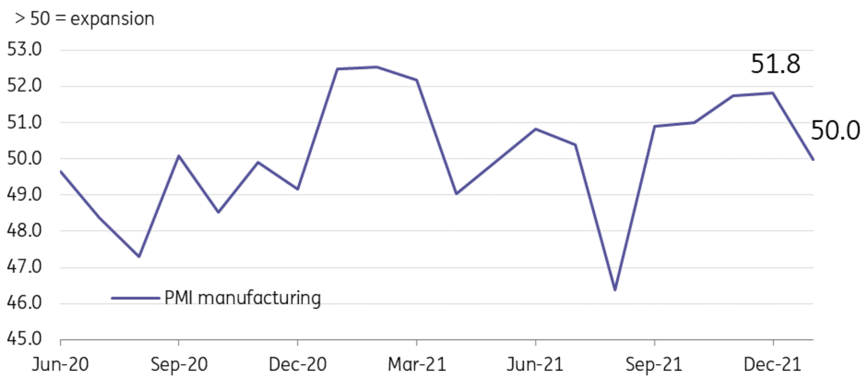
Philippine economic managers remain optimistic about economic prospects in 2022. The official forecast for 2022 GDP was pegged at 7-9% with growth expected to get a boost from national elections scheduled in May. And although recent history shows us that election-related spending tends to bolster growth momentum, we highlight certain developments that could force us to tone down expectations for this year.

Omicron disruption

This year got off to a less-than-ideal start with daily Covid-19 infections surging with the arrival and spread of the Omicron variant. The surge in infections resulted in yet another round of mobility curbs in the capital region and surrounding provinces.

And although early data points to a less burdensome impact on the healthcare sector, the disruption caused by restrictions will likely reverse positive trends in consumer and business sentiment. The impact of Omicron also appears to have filtered through to the manufacturing sector with the latest manufacturing purchasing managers' index (PMI) reading showing a stagnation in activity. This highlights that growth momentum will likely take its queue from virus containment, and growth momentum could be hampered should the country experience additional Covid-19 waves in the coming months.

Manufacturing activity stalls during Omicron shutdown



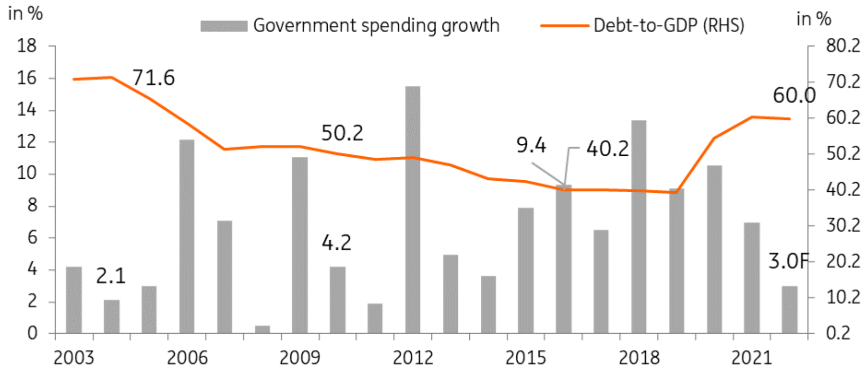
Source: IHS Markit

Fiscal handicap for incoming administration

The fiscal situation in the Philippines deteriorated substantially during the pandemic. The government was forced to roll out support measures during lockdowns while also dealing with a steep drop in revenue collection due to weaker economic output. As a result, the debt-to-GDP ratio rose sharply to 60.5% by end-2021 and is expected to remain above 60% until 2023. The incoming administration will inherit a substantial debt pile which could constrain the ability of the next president to support the economy.

Previous election years showed a noticeable slowdown in government expenditures in the quarters after the May elections. A new economic team will likely struggle to hit the ground running, all the more so with the current fiscal state. We therefore expect a slowdown in government outlays by the second half of the year, which could weigh on the overall growth outlook.

High debt-to-GDP to handicap incoming president



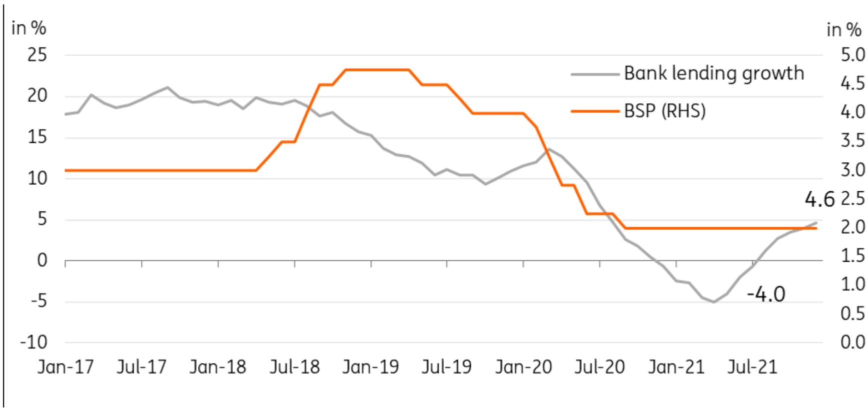
Source: Bureau of the Treasury Philippines and Philippine Statistics Authority

Et tu Ben?

Bangko Sentral ng Pilipinas (BSP) Governor Ben Diokno has never shied away from being tagged as a “pro-growth” central bank governor. Throughout the pandemic, he vowed to maintain an accommodative stance “for as long as necessary” to ensure a sustainable growth trajectory. Diokno has remained dovish even in the face of imminent rate hikes from the Federal Reserve and other central banks, ruling out rate hikes for at least the first half of the year. Despite these dovish undertones from Diokno, we have pencilled in a salvo of rate hikes from the BSP with the first adjustment as early as 2Q. The deterioration in the external position by the end of 2021 suggests that the Philippine peso (PHP) will continue to come under pressure ahead of the projected March Fed rate hike. This, alongside a decent 1Q GDP report, could be enough to convince Diokno to join the rate hike chorus.

A reversal from the Philippine monetary authorities will likely nip the recent rebound in bank lending in the bud. Bank loans had managed to revert to growth recently, due in part to economic reopening. Demand for credit has been sensitive to rate hikes in the past and we expect BSP’s rate hike salvo to cap the recovery in bank lending and weigh on overall capital formation.

Bank lending rebound to be capped by BSP rate reversal



Source: Bangko Sentral ng Pilipinas

Growth momentum intact but may fall short of target

Despite these speed bumps, we expect the Philippine economy to post a respectable expansion in 2022. The gradual economic reopening has helped revive household consumption which has resulted in a rekindling of business sentiment. Election-related spending may indeed support economic activity in the first half of the year as the campaign season peaks in April.

Growth may fall short of current aspirations, however, with momentum disrupted by the surge in cases linked to the Omicron variant. Meanwhile, a likely slowdown in government outlays will be felt in the second half given the fiscal handicap passed on to the new administration. Lastly, the potential reversal in stance by the BSP is expected to cap the recent bounce in bank lending activity which in turn could limit capital formation. We remain optimistic about the growth outlook for the Philippines, but we believe GDP growth may ultimately fall below expectations and settle at 5.3% for the year.

Author

Nicholas Mapa
Senior Economist, Philippines
nicholas.antonio.mapa@asia.ing.com