

Philippine's central bank announces phased RRR redux

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16%

BSP Reserve Requirement Ratio

by end July

Central bank trims RRR with a twist, the 1st under Diokno

The Philippine's central bank followed through its recent policy rate cut with a reduction to its reserve requirement ratio (RRR) at a non-policy meeting on 16 May 2019, with a twist.

With inflation gliding back within target and expected to remain benign well into 2020, this was the perfect opportunity for the central bank to cut both the policy rate and reduce RRR more so with GDP dropping to 5.6%. In 2018, BSP announced the policy stance would be signalled by changes to the RRP, thereby removing RRR from the official statement and relegating it to an operational tool.

The BSP will carry out a cumulative 200 basis point cut to the RRR, 100 bps at the end of May, 50 by the end of June and another 50 by the end of July. The gradual reduction in RRR will definitely help alleviate the current tight liquidity conditions and complements its recent policy rate cut.

The right tool for the right problem

After slamming hard on the proverbial brakes in 3Q18 by jacking up rates by 175 basis points, the central bank believed it was time to give the economy a much-needed breather especially with the inflation objective well in hand. Meanwhile, with liquidity conditions tight, as evidenced by seven months of single-digit M3 growth and multi-year high time deposit rates, BSP looked to finally address the lack of funds circulating in the system. Deploying the appropriate tool to address specific ailments was key in this round of decisions despite being tempted to deploy one tool to address all concerns.

BSP to monitor price developments moving forward

We believe the central bank will remain data-dependent and forward-looking as they look to safeguard price stability to achieve an environment conducive for economic growth.

Moving forward, growth prospects appear to point north post-budget passage and all the more with slowing inflation and the recent BSP easing seen to drive both consumption and capital formation. But for now, after priming its “pacemaker” for growth, the BSP’s move for a “transfusion” was welcome as it complements its previous policy rate cut. Growth will likely fall within the government’s 6-7% target while inflation remains benign, all the while continuing BSP’s reform agenda.