

Philippines: BSP opts for prudent pause though inflation is poised to slow

Philippines' central bank has opted to hold interest rates steady even though inflation is expected to decelerate further



BSP keeps rates steady with inflation expected to be benign until 2022

The Bangko Sentral ng Pilipinas (BSP) opted to keep interest rates unchanged at 2.25% even as it lowered its inflation forecasts all the way out to 2022. BSP unveiled its latest expectation for the inflation path with price gains likely to settle at 2.3% in 2020, 2.8% in 2021 and 3.0% in 2022. The central bank believes that price pressures will remain subdued over the policy horizon with risks to the outlook tilted to the downside. Governor Benjamin Diokno signalled previously that he would

pause for “at least 2 quarters” to allow the recent flurry of moves to take root. To date, the BSP estimates it has released up to Php1.5 trillion into the financial system, helping to keep borrowing costs low to aid the recovery.

We do not expect BSP to adjust monetary policy in the near term given that the real policy rate remains negative with headline inflation at 2.4%. Governor Diokno will continue to monitor price developments over the policy horizon to determine if further policy action is required. The central bank, however, did note the key role of fiscal policy in the pandemic response, with the BSP hopeful that the recently passed fiscal stimulus package would complement the string of rate cuts and infusion of liquidity.

BSP approves second cash advance to national government

Investors had priced in a pause from the BSP, as Governor Diokno had signalled that monetary policy would likely be accommodative for at least two years, with the economy currently recovering from the fallout from Covid-19. BSP approved the PPhp540 billion cash advance to the national government via a repurchase agreement to help finance relief efforts. Just recently, BSP closed out a Php300 billion cash advance to the national government, with fiscal authorities promptly securing a more substantial fresh line of credit worth PPhp540 billion. The second tranche of cash advances will have a marginal impact on inflation and the currency but successive rounds of such agreements may eventually call into question the central bank's independence. BSP has justified such arrangements given the urgent need to help finance government outlays to offset the economic downturn, pledging to wind down such extraordinary measures when economic activity normalises.