Philippines: Rates unchanged but a cut in reserve requirements may be in the offing

The Philippines' central bank (BSP) kept policy rates unchanged as expected but a reduction in the reserve requirement ratio could be in the works

4.75% Overnight reverse repurchase rate

As expected

'Dovish' Diokno keep rates unchanged

The BSP kept policy rates steady, leaving its overnight reverse repurchase rate at 4.75%, as expected by the market. Official forecasts by the BSP continue to show inflation remaining within target for the year, with the latest readings showing inflation at 3.0% in 2019 (from 3.08%) and 3.0% (from 2.98%) in 2020. This was the first meeting for new central bank Governor Benjamin Diokno who is perceived to be dovish, having flagged threats to the growth outlook, such as the budget impasse, during the press conference.

RRR now a policy tool again?

ING continues to expect a cut in the reserve requirement ratio (RRR) in the near term given that it was omitted from the official policy statement on Thursday. Deputy Governor Diwa Guinigundo continued to maintain that the RRR and adjustments to it must move in line with the bank's monetary policy stance. But with domestic liquidity growth in the single digits and time deposit rates elevated, we foresee a reduction in this rate to 17% from 18% at an off cycle policy meeting in the next few weeks. We predicted the RRR cut in February, as inflation finally fell within target, and all indications suggest that price gains will remain within target for the balance of the year.

Policy reversal in May a possibility?

The BSP continues to preach “data dependency” and may await further validation that inflation is settling within target. But forecasts show a gradual deceleration, with price gains even expected to dip to the 2% handle in 3Q. Given the supply-side nature of 2018’s inflation spike, we can expect price pressures to dissipate further now that the rice tarrification bill is in effect. On the other hand, BSP will also likely be monitoring oil price movements and the possible inflationary impact of El Niño, as risks to the inflation outlook.

On the external front, the Fed’s abrupt turnaround on rate guidance will also give the BSP added leeway to finally consider reversing its tightening cycle, particularly because 1H growth is seen to be challenging due to the protracted budget delay and the ill effects of the current dry spell. BSP’s inflation forecasts validate that the BSP is likely done with its tightening cycle, with a policy reversal in sight given slowing growth momentum, a dovish Fed and inflation back within target.

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