Philippines: Economy grows by 6.1 % in 4Q

Slowing growth leaves door wide open for BSP to ease policy in 2019

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6.1% 4Q 2018 GDP

Lower than expected

We got your back: Government spending helps lift overall growth

With other sectors of the economy facing headwinds, government spending helped offset the slight deceleration in traditional growth sources to push overall growth to settle at 6.1%. Government expenditures expanded by 11.9% as the administration chased its target deficit-to-GDP ratio of 3%.

Capital formation hampered by base effects

Capital formation, a key component in the economy's recent run, sustained growth at 5.5%. This was likely on strong construction efforts as durable equipment took a back seat on base effects. Car sales contracted sharply in 4Q 2018. This can be traced directly to the one-off car buying spree seen in 2017 - these forced car sales in 2018 into steep contraction but auto dealers are confident that sales will rebound in the coming year. Economic prospects remain bright and the introduction of new model lineups should entice demand.

Net exports continue to pose a drag

With exports struggling despite the Peso's depreciation, the trade deficit has continued to test historical wides as imports surge on a mixture of strong capital infusion from corporates, raw materials for infrastructure spending, bloated fuel costs and still solid consumer goods purchases. Given the ambitious targets set by the national government, we can expect raw material and capital goods purchases to continue. The trade deficit may see some relief as oil prices appear, at least for the time being to be more well-behaved.

The return of household consumption

Consumption remains the main cog in the Philippine growth engine and the sector managed to post decent 5.4% growth - after it dipped to 5.2% in 3Q 2018 with inflation hitting multi-year highs. With inflation finally coming off the peak in 4Q and forecasted to slide back within the BSP's 2-4% target, we can expect household consumption to resume its strong performance to lead the economy into 2019. Inflation has slowed to 5.1% as of December 2018.

Outlook

2019 will likely remain a tale of two halves with the first 6 months of the year to see relatively subdued growth. The government budget delay is seen to handicap one crucial leg of Philippine growth, with government expenditures likely put off to the latter half of the year. Furthermore, knock-on effects from the BSP's aggressive 175 bps rate hike in 2018 are expected to continue to feed into the economy and sap investment momentum. Meanwhile, household consumption will likely be revived as inflation decelerates further and slides back within target as early as 2Q 2019.

With the inflation specter curtailed for the time being, the BSP will likely unload a string of easing measures to help buttress growth closer to the administration's growth target of 7-8%. With liquidity conditions still relatively tight and the Governor's pledge to slash reserve requirements (RRR) to single digits by the end of his term, we can see the BSP slashing RRR further in 1Q followed by a possible policy rate cut in 2Q to help bolster growth for the second half of the year.