Philippine economy decelerating amid global turmoil

Dante Pastrana
19 September 2011

The Philippine economy has continued to slow sharply, as part of a broader reversal throughout Asia amid worsening international economic turmoil. The second quarter figures, released in late August, registered just 3.4 percent growth, year-on-year—the fourth consecutive quarterly decline in growth.

The Philippines was one of the countries that did not slide into recession in the wake of the 2008-09 global financial crisis. Analysts were trumpeting a "new normal" of high growth for the country. President Benigno Aquino pledged to boost growth by as much as 8 percent annually. Now these forecasts and plans are in tatters.

The slump began from the second quarter last year, when growth hit an annualised rate of 8.9 percent. The figure dropped to 7.3 percent in the third quarter of 2010, then 6.1 percent in the fourth quarter. In the first quarter, the result was just 4.6 percent—substantially less than the overall growth figure of 7.9 percent for 2010.

The government reacted by blaming international factors—high oil prices, the earthquake in Japan, a poorly performing US economy and the European debt crisis—and pledging to boost public spending on infrastructure to encourage growth. Any extra spending, however, will immediately come under scrutiny from international finance capital, which has been pressuring the Aquino administration to cut the budget deficit.

The World Bank's *Philippines Quarterly Update*, issued in June, forecast 5 percent growth for 2011 and a 5.4 percent expansion in 2012. The Asian Development Bank's Outlook 2011 predicted 5.3 percent for 2012. Almost certainly these figures will have to be revised downward following the worse-than-expected second quarter outcome.

The World Bank update was upbeat on the Philippine economy, declaring that the country could look forward to "more robust and less variable growth". The deceleration, it implied, was largely temporary, resulting from the government's efforts to cut the budget deficit and the broader slowdown in international trade.

The World Bank was optimistic for the coming year, pointing to the first quarter expansion in investment of 42.3 percent and a growth of 5.3 percent in consumer spending. With the Aquino administration expected to push ahead with plans for public-private partnerships, investment was expected to continue to expand.

The international credit rating agencies—Moody's and Fitch Rating—were also upbeat. In June Moody's raised the country's sovereign debt rating to two notches below investment grade and Fitch, in an unprecedented move, lifted it to one notch below investment grade.

Fitch analyst Andrew Colquhoun spoke enthusiastically about the Aquino administration's "progress on fiscal consolidation"—that is, increased taxes and the slashing of public spending. The country, he said, now had "a track record of macro stability, broadly favourable economic prospects and strengthening external finances."

The Philippines, however, is being buffeted by the same global economic forces that are affecting the entire region. China, South Korea, Hong Kong, Malaysia, Singapore and Taiwan have all recorded slowdowns in recent months. The decline in China is particularly significant as its demand for parts and raw materials, as well as investment and aid, has acted as an economic buffer for countries throughout the region.

Philippine exports, which account for 30 percent of gross domestic product, fell in June by 9.4 percent year-on-year. The latest export figures for July, released last week, showed a further fall of 1.7 percent from a year earlier. Electronics exports, which account for about half of Philippine products sold overseas, plunged by 21 percent in July from a year earlier. Singapore-based Forecast Pte economist Radhika Rao predicted that exports would "remain weak" for the rest of the year and be the "main drag" on economic growth.

Like other Asian economies, the Philippines has faced a strengthening peso and rising prices. A major factor has been the policy of quantitative easing by the US Federal Reserve to deliberately weaken the US dollar. The result has been a surge of speculative capital around the world that has produced higher prices and strengthening currencies against the American dollar.

According to the Bangko Sentral ng Pilipinas, foreign purchases of equities in the first quarter surged to $US2.14 billion, more than 65 percent up from the same period last year. Debt securities bought by non-residents also increased to $2.38 billion—over 46 percent higher than a year earlier. The Philippine Stock Exchange Composite Index reached a new high in April of 4319.5 before easing—its highest point for seven years.

The incoming surge of speculative capital, coupled with the $4.6 billion in remittances from Filipinos working overseas, has put enormous upward pressure on the Philippine peso. Bangko Sentral has already increased the benchmark interest rate twice this year to 4.5 percent and in July bought nearly $200 million in a bid to prevent the peso from climbing further.

The high value of the peso has impacted on many working people. Some 23 percent of Filipino families receive remittances from an estimated 8 million Filipinos working overseas. According to the World Bank, the level of remittances, in real peso terms, between March 2010 and March 2011 declined by an average of 2.1 percent. As a result, personal consumption decreased quarter-on-quarter by 13.4 percent in the first quarter, then increased by 6.0 percent in the second quarter after an increase in remittances.

A recent survey by the Bangko Sentral found that consumer expectation was increasingly negative, particularly among households relying on remittances. Its index for the third quarter fell to -18.7 percent compared to -14 percent for the same period last year. A negative index indicates a majority of respondents are pessimistic about their income and the prospects for the economy.

Inflation hit a 26-month high of 5.2 percent (annualised) in June before slowing to 4.6 percent in July and 4.3 percent in August, reflecting higher interest rates and a decelerating economy.

Unemployment figures are on the rise. The jobless rate for July, released last week, was 7.1 percent, up marginally from 7.0 percent in June. The underemployment rate was 19.1 percent, lower than 19.4 percent for April but significantly higher than the 17.9 percent in the same period last year. This means more than one in four working-age Filipinos are either unemployed or looking for more work.

The economic slowdown will only widen the gulf between rich and poor. As the World Bank report acknowledged, economic expansion over the past decade has worsened inequality and the incidence of poverty in the Philippines.

The government's 2009 Family Income and Expenses Survey (FIES) indicates that the number of poor families—with an annual income less than $1,800 for a family of five—increased from 3.29 million to 3.86 million between 2003 to 2009. The poverty rate rose from 24.9 percent of the population in 2003 to 26.5 percent in 2009.

Social inequality also deepened. From 2002 to 2010, the combined net worth of the five richest Filipinos increased by 72.5 percent, from just $5.3 billion to over $9.1 billion. By contrast, a worker in the national capital on the legal minimum daily wage of PHP382 pesos earned just over $2,200 annually.

The World Bank report found that the richest 20 percent of the Philippine population outspend the poorest 20 percent by more than eight times.

A report by the Stratbase Research Institute issued in July found that the Philippines was the most unequal among Southeast Asian countries. In 2010, it had the highest GINI coefficient of 0.44, compared to 0.425 for Thailand, 0.394 Indonesia, 0.379 for Malaysia and 0.378 for Vietnam. The GINI coefficient measures social inequality on a scale from 0 to 1, with 1 indicating complete inequality.

Stratbase warned of "social tension and even political instability" if the income gap was not addressed. Similarly, the World Bank report declared: "The huge disparity in expenditures can cause problems such as the lack of legitimacy, the weakening of social cohesion and the outbreak of social strikes," exacerbating "the existing differences and conflict between the poor and non-poor."