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FOREIGN AFFAIRS & TRADE
Manatū Aorere

Philippines Economy

Market Report

MARCH 2022

Prepared by the New Zealand Embassy in Manila and based on Philippine government official statistics, briefings from economists from ANZ, HSBC, and other local banks (Banco de Oro, Bank of Philippine Islands, and Chinabank).

Summary

- Strong performance for the last quarter of 2021 raised the Philippines' annual growth, demonstrating the economy's potential given less restrictions and better COVID-19 management.
- There is general optimism for the Philippine economy in 2022, which will likely be buoyed by election spending, increased income and household expenditure, and continued government disbursement to fund infrastructure.
- The passage of the Public Service Amendment Act and the Foreign Investments Act should further liberalise the Philippine economy and open up opportunities for New Zealand to explore. This also paves the way for the Philippines' proposed accession to the CPTPP.
- New Zealand companies remain challenged by shipping delays while others look to the Philippines as a possible outsourcing solution. Reopening of Philippine borders also see Kiwis returning to the Philippines for their in-country operations.

Report

<u>Philippine Economic Performance</u>

- The Philippines posted a better-than-expected GDP growth of 7.7% in the fourth quarter of 2021, thereby raising annual growth for the year to 5.6%. This beats the government's adjusted target of 5% to 5.5% for the year. The robust performance was mainly due to higher household consumption as mobility restrictions were lifted coming out of the Delta variant surge. The high figures were despite the the destruction brought by Typhoon Rai (known as Odette in the Philippines) in December.

<u>Prospects for 2022</u>

- Analysts remain optimistic about the growth target for 2022. Mean projection is at 7.1% (Fitch ratings – 6.6%, JP Morgan – 11.1%, ADB 6%, World Bank 5.9%, among others). Optimism is due to several factors. 2022 is an election year in the Philippines, which historically meant larger household income due to campaign spending on paraphernalia, campaign rallies, media push which in turn create jobs both formally and informally (i.e. printing of materials, employment to boost grassroots organisations). Household expenditures, which remain a key factor for the Philippines GDP will increase with "revenge spending", where people will spend more generously after experiencing the constraints of COVID-19 and lockdown measures.
- Another factor would be the increased vaccination rate and seemingly quick recovery from the Omicron variant, which resulted in fewer deaths, increased spending, improved business confidence and less restrictions on mobility. Government spending is also expected to increase as infrastructure projects continue despite the elections in May.
- Remittances from overseas Filipinos are expected to continue to grow strongly this year, which will also help drive

up household spending including property investment. Ease in entry restrictions abroad resulted in more deployment for Overseas Filipino Workers last year and is expected to continue this year. New COVID variant outbreaks could dampen this outlook.

- In addition, risks for inflation remain as supply constraints plus closed businesses mean remaining businesses can increase prices, e.g. meat importation in the wake of swine flu fever. Continued increase in gas prices worldwide will also contribute to inflation. Additional emerging variants of COVID-19 challenging Philippines' pandemic management will continue uncertainty. The biggest risk for 2022 would involve the absence of a peaceful transition of power following the 2022 elections.

Public Service Act and Foreign Investment Acts

- The Public Service Amendment Act has been ratified by Congress and submitted to Duterte for signature. It is expected to be signed as this has been marked as priority legislation under this administration. The bill identifies an increased number of industries, including telecommunications, domestic shipping, airlines, and airports, as public utilities and would now permit up to 100% foreign ownership (from a previous maximum of 40%). Business groups and various foreign chambers were pleased with the development, given the years it took to pass the bill. A copy of the congress bicameral report said this was "one of the most significant liberalisations of the foreign investment climate in the Philippines since the country gained independence."
- The Foreign Investment Act Amendments was also submitted to the President for signature. This would lower the minimum employment and capital investment (for select technology) for small and medium sized businesses required for foreign investment.
- The enactment of both bills into law is expected to generate more foreign direct investment into the Philippines, modernise major sectors and increase competition for impacted industries. The Public Service Amendment Act in particular has been crucial in the Philippines' interest in acceding to the CPTPP and would remove one of the bigger legislative barriers to their membership.

Bilateral Trade

- In the September 2021 quarter, New Zealand exported NZD178.84 million of total goods and services to Philippines and imported $53.3 million, with a total trade value of NZD232.15 million. This is a slight increase from NZD157.29 million and NZD49.75 million respectively in the same period of 2020, but still way below pre-pandemic levels.

Long-term effect of COVID-19 on productivity

- Last year, the National Economic Development Authority (NEDA) released a report estimating the long-term economic cost of the pandemic will amount to losses of over PHP40 trillion (NZD1.17 trillion) and would be felt for the next 40 years. Lower consumption and investment over the past two years will continue to result in lower revenues, incomes wages and future streams of tax revenues.
- Closure of schools since 2020 is expected to have lasting effects on future income, productivity and competitiveness. An immediate impact was the reduction of the labour force, and thus household wages, as parents chose to stay home to facilitate distance learning. A World Bank study, prior to the pandemic, assessed 12 years of schooling in the Philippines was only equivalent to 8 years of learning against OECD averages. This is likely to worsen as a result of ongoing school closures. The ability of parents to stay home to supervise learning depends on the affluence of the parents, exacerbating the already unequal access and variable quality of education in the country. The UN estimates 2 million children have been permanently lost to education due to school closures, and high school students are poorly prepared to move on to tertiary learning. This is expected to constrain the availability of skilled workers in the future.
- Longer-term, NEDA expects workers' productivity to remain below its pre-pandemic potential as death, illness, and losses in education are not reversible.

Regional trade and economic integration agenda

- The Philippines is actively engaged in a raft of international trade policy discussions, ranging from new free trade agreement negotiations through to reviews of existing arrangements and exploring entry into new ones.
- This international work agenda is supported by changes to domestic legislation that would support continued opening and liberalising of the Philippines' market. The recent amendment to the Philippines' Retail Trade Liberalization Act and the current effort to reform its Foreign Investments Act – both have the intention of further opening and liberalising its market. The digital economy remains a priority for the Philippines.

Climate change and renewable energy

- The opportunities and challenges facing the Philippines' transition to renewable energy include current state of power consumption, power sources and industry dynamics. There is a shift away from local coal production towards renewable energy production – although the Philippines continues to import huge quantities of coal from Indonesia. Leading power generating companies are partnering with international players to develop a range of renewable energy options such as solar, hydro but also hydrogen and battery storage.
- Climate change is a growing part of ADB's strategy, and is being mainstreamed throughout the Bank's operations. Ahead of COP26, ADB's climate finance target had been raised from US$80B to 100B of ADB's own resources by 2030, with one third of that financing intended to support adaptation actions and a greater emphasis on mobilising private finance.

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