

Philippines Business Forecast Report Q1 2015

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Abstracts

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Core Views

We hold a positive outlook for the Philippine economy, and forecast real GDP growth to come in at 6.3% in 2014. However, tighter monetary policy in 2015 is likely to cause real GDP growth to ease to 6.0%.

We continue to see the Bangko Sentral ng Pilipinas raise its benchmark interest rate by another 50 basis points to 4.50% in 2015, owing to continued price pressures emanating from a potential electricity shortage in Luzon and likely interest rate normalisation in the US in the coming year. Ongoing fiscal consolidation efforts by the Philippine government will ensure a sustainable budgetary trajectory over the coming years.

We forecast for the country's budget deficit to narrow to 0.8% of GDP in 2014 and 0.6% in 2015, from 1.4% in 2013. However, the lacklustre fiscal spending will be a drag on growth. The Philippine peso should stay largely resilient despite USD strength. We forecast the unit to average PHP44.50/USD in 2014 and PHP43.71/USD in 2015. A combination of still-positive economic growth outlook, strong foreign inflows and an improving external position should provide structural support to the peso.

Major Forecast Changes

We have revised our 2015 benchmark interest rate forecast to 4.50%, from our previous estimate of 4.00%. We have revised our forecast for the Philippine peso to average PHP44.50/USD in 2014, from our earlier estimate of PHP44.00/USD.

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We believe the Philippines will receive continued political support from European leaders for its international arbitration case against China, and strengthen its economic relations with Europe over the coming years.

Table: Political Overview

Long-Term Political Outlook

Prospects For Improving Governance

The Philippines faces a number of political challenges over the coming years that, if handled successfully, could improve governance.

However, given low income levels and high levels of inequality, we expect the political scene to remain vulnerable to intermittent instances of turmoil.

CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis

BMI Economic Risk Index

Economic Activity

Q214 Rebound Presages Continued Growth Momentum

We believe that the Philippines will sustain relatively robust growth momentum over the coming quarters, as we expect stronger

investment performance, while private consumption and net export growth should remain robust. We maintain our forecast for real GDP

to grow 6.3% in 2014 and 6.0% in 2015.

Table: Economic Activity

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Lacklustre Fiscal Spending To Drag On Growth

Ongoing fiscal consolidation efforts by the government will ensure a sustainable budgetary trajectory over the coming years. We forecast for the country's budget deficit to narrow to 0.8% of GDP in 2014 and 0.6% in 2015, from 1.4% in 2013. That said, the lack of momentum in fiscal spending to boost infrastructure development will weigh on the country's economic output amid tighter monetary policy in 2015.

Table: Fiscal Policy

Monetary Policy

Additional Rate Hikes In 2015 On The Cards

In order to meet the Philippine government's real GDP growth target of 6.5-7.5% in 2014, we believe the Bangko Sentral ng Pilipinas (BSP) will hold its benchmark interest rate at the current 4.00% through 2014, following the two 25bps rate hikes to temper rising price pressures. However, we continue to see another 50bps rate hike in 2015, owing to price pressures emanating from a potential electricity deficit in Luzon and likely interest rate normalisation in the US.

Table: Monetary Policy

Exchange Rate Policy

Peso To Stay Largely Resilient Despite Headwinds

While the Philippine peso has come under pressure amid recent broad USD strength, we maintain our neutral outlook for the unit. A combination of a still-positive economic growth outlook for the Philippines, strong foreign inflows and an improving external position will provide structural support for the peso. We also see scope for the central bank to use its foreign reserves to defend against extensive peso weakness.

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The Philippines holds significant economic growth potential and has begun to come into the investment spotlight as a result. Although the country has in the past been hampered by political instability and poor investor perception, we believe President Benigno Aquino III has been able to make progress on both fronts. Moreover, consumerism is expected

to pick up in a big way towards the end of the decade as income levels rise.

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