

Philippines Business Forecast Report Q4 2014

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Abstracts

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Core Views

The Philippines' decision to seek international arbitration in its maritime dispute with China will raise tensions between the two countries, and could accelerate US efforts to 'pivot' towards Asia. The dispute also increases the risk of Beijing imposing economic sanctions on the Philippines, which would pose downside risks for our 6.3% real GDP growth forecast in 2014. We continue to hold a positive outlook for the economy, and maintain our forecast for real GDP growth of 6.3% in 2014, as investment is likely to pick up and the export sector should see a modest rebound this year.

Rising inflationary pressures have narrowed the scope for continued accommodative monetary policy in the Philippines. As such, we maintain that the Bangko Sentral ng Pilipinas (BSP) will raise its benchmark interest rate by a total of 50 basis points to 4.00% by end-2014.

Effective fiscal reforms by the Philippine government will lead to a continued improvement in the country's debt metrics and allow for fiscally funded infrastructure projects. We are forecasting the budget deficit to narrow to 0.8% of GDP in 2014, while public debt as a share of GDP to decline to 46.9%.

Major Forecast Changes

We have upgraded our 2014 budget deficit forecast from 1.4% of GDP to 0.8% of GDP, owing to improving tax revenue collection and prudent expenditure management.

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CHAPTER 1: POLITICAL OUTLOOK

SWOT Analysis

BMI Political Risk Ratings

Domestic Politics

Sino-Philippine Maritime Dispute: Geopolitical And Economic Implications

The Philippines' decision to seek international arbitration in its maritime dispute with China will raise tensions between the two countries, and could accelerate US efforts to 'pivot' towards Asia. The dispute also increases the risk of Beijing imposing economic sanctions on the Philippines, which would pose downside risks for our 6.3% real GDP growth forecast in 2014.

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 Ratings

Economic Activity

Still Positive Despite Disappointing Q114 GDP Print

The Philippines' real GDP growth fell to 5.7% year-on-year in Q114, missing Bloomberg consensus estimates of 6.4% as investment faltered. We nevertheless maintain a positive outlook on the economy, and maintain our forecast for real GDP growth of 6.3% in

2014, AS INVESTMENT IS LIKELY TO PICK UP, DOMESTIC DEMAND WILL REMAIN STRONG, AND THE EXPORT SECTOR SHOULD SEE A MODEST

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year.

Table: Economic Activity

Fiscal Policy

Fiscal Position To Remain On A Sound Footing

The Philippine government's fiscal reforms to bolster their tax revenues and keep expenditures in check have been effective, which will in turn lead to a continued improvement in the country's debt metrics and allow for fiscally funded projects. We forecast the fiscal deficit to narrow to 0.8% of GDP in 2014, while public debt as a share of GDP to decline to 46.9%, from 49.2% in 2013.

Table: Fiscal Policy

Monetary Policy

Rate Hikes In Sight Amid Rising Inflation

Rising inflationary pressures have narrowed the scope for continued accommodative monetary policy in the Philippines. As such, we maintain that the Bangko Sentral ng Pilipinas will raise its benchmark interest rate by a total of 50 basis points to 4.00% by end-2014.

The country's positive growth outlook will also provide room for rate hikes.

Table: Monetary Policy

Exchange Rate Policy

Peso To Retain Recent Gains

We are neutral towards the Philippine peso over the coming months, and expect the currency to retain its recent gains against the dollar, owing to the country's still-positive growth outlook, declining external debt and returning net portfolio inflows. Any currency weakness will also likely be limited by the strong reserves that the central bank has. As such, we maintain our end-2014 and 2014 average forecasts of PHP43.50/USD and PHP44.00/USD respectively. That said, further weakness in the Chinese yuan poses a downside risk to our outlook.

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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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