



**HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON  
MONETARY POLICY ISSUES HELD ON 19 APRIL 2007\***

The Advisory Committee<sup>1</sup> submitted the following recommendations for the consideration of the Monetary Board:

- Maintain the current monetary policy settings as follows:
  - a. Maintain the BSP's policy interest rates at 7.5 percent for the overnight RRP (borrowing) rate and 9.75 percent for the overnight RP (lending) rate;
  - b. Maintain the tiering scheme;
  - c. Maintain the current interest rates on term RRPs, RPs, and SDAs; and
  - d. Maintain the current reserve requirement ratios.
- Introduce the following schemes for absorbing liquidity:
  - a. Encourage GSIS, SSS, and other GOCCs to deposit funds with the BSP;
  - b. Allow trust entities supervised by the BSP to deposit at the BSP; and
  - c. Allow SDA placements of banks to be deemed as alternative compliance by banks to BSP requirements on liquidity floor for government deposits.

The Monetary Board then proceeded to review the recent developments and the key considerations in the formulation of the BSP's monetary policy stance.

---

\* The discussion presented herein reflects the assessment made by the Monetary Board based on the information available at the time of the policy meeting. The highlights of the discussions of the 19 April 2007 meeting were approved by the Monetary Board during its regular meeting held on 17 May 2007.

<sup>1</sup> The Advisory Committee is composed of the Governor of the BSP as Chairman and five members, namely: the Deputy Governor for the Monetary Stability Sector, the Deputy Governor for Supervision and Examination Sector, the Managing Director of the Treasury Department, the Managing Director of the Monetary Policy Sub-sector, and the Acting Director of the Department of Economic Research.



## **I. Review of Recent Developments**

### **Prices**

- Headline inflation slowed to 2.2 percent in March from 2.6 percent in February. This level was last recorded in January 2000 and has been the lowest inflation outturn since April 1987. All commodity groups in the Consumer Price Index (CPI) basket, with the exception of clothing, registered slower price increases during the month.
- Similarly, core inflation decelerated in March. The official core inflation measure eased to 2.6 percent from 3.0 percent in February. Alternative measures of core inflation estimated by the BSP also displayed a similar decelerating trend.
- International spot and futures oil prices were higher in March and early April due to continued tensions over Iran's nuclear program and lower US gasoline inventories. Similarly, domestic pump prices were higher during the period.
- Preliminary results of the BSP's Q1 2007 survey on inflation forecasts showed continued easing in inflation expectations. The mean inflation forecast for 2007 fell to 3.8 percent from 4.5 percent in the last quarter's survey. For 2008, the BSP's survey showed a mean inflation forecast of 4.6 percent from 5.1 percent in the last quarter's survey.

### **Demand**

- Latest data generally showed a continuing improvement in demand conditions.
  - Latest available data from Colliers International Research showed that property values sustained their uptrend in Q4 2006. Office rents are nearing their early 1996 levels and are forecast to increase by 20 percent in the course of 2007.
  - The year-on-year growth in passenger car sales accelerated to 34.9 percent in March from 25.6 percent in February due to the introduction of new models. Sales of trucks and buses rose at a robust albeit slower pace of 45.8 percent year-on-year in March compared to 66.0 percent in February.
  - Energy sales by Meralco grew at a faster pace of 5.0 percent year-on-year in January compared to 3.6 percent in the previous month.



## *Bangko Sentral ng Pilipinas*

---

- Appliance sales slid slightly by 0.7 percent year-on-year in February after declining by 12.0 percent in January. Year-to-date sales declined at a slower pace of 6.6 percent compared to 21.2 percent in the first two months of 2006.
- Average capacity utilization in manufacturing was slightly lower at 80.1 percent in January compared to 80.3 percent in the previous month based on the NSO's Monthly Integrated Survey of Selected Industries (MISSI).
- Production indices in the MISSI showed a modest expansion in manufacturing activity in January 2007. The Value of Production Index (VAPI) rose by 1.8 percent year-on-year in January after four consecutive months of decline. The Volume of Production Index (VOPI) also increased slightly by 2.0 percent in January after year-round decreases in 2006.
- Growth in merchandise exports decelerated to 7.0 percent year-on-year in February from a revised rate of 21.8 percent in January. The year-to-date growth in merchandise exports was 14.2 percent, more than double the 6.8 percent growth in same period last year.
- Merchandise import payments increased slightly by 1.0 percent year-on-year in January, an improvement from the previous month when they slid by the same amount. This can be attributed largely to higher growth in imports of electronic products.
- The latest BES for Q1 2007 showed continued bullish business confidence in the economy in 2007. The survey also showed continuing confidence in the next (i.e. second) quarter with the business confidence index hitting its highest level since the start of the survey in Q2 2001.
- Based on the preliminary results of the January 2007 Labor Force Survey (LFS), the unemployment rate declined to 7.8 percent in January 2007 from 8.1 percent in January 2006.

### **Domestic Liquidity**

- Domestic liquidity or M3 growth was largely unchanged at 22.4 percent year-on-year in February compared to 22.8 percent in the previous month based on the data from the BSP's Depository Corporations



# *Bangko Sentral ng Pilipinas*

Survey (DCS).<sup>2</sup> The expansion in liquidity was driven by strong foreign exchange inflows from OFW remittances, export earnings and foreign investments. The expansion in domestic credit also contributed to the strong growth in domestic liquidity.

- Bank lending continued to grow in February albeit at a slower pace relative to the previous month. Based on the new data series, bank lending in February continued to grow, although at a slower pace of 7.7 percent compared to the 9.4 percent growth registered in January<sup>3</sup>. Lending to all sectors posted positive growth rates, with the exception of mining and quarrying, electricity, gas and water, and manufacturing. The growth in lending was driven mainly by loans granted to financial institutions, real estate and business services (FIREBS), and community, social and personal services sectors.
- Consumer credit surged in Q4 2006 compared to the previous quarter as the seasonal increase in consumer spending during the Christmas holiday pushed up demand for credit card loans.

## **Other Domestic Developments**

- Data from the January 2007 Rice and Corn Production Survey of the Bureau of Agricultural Statistics (BAS) suggest that rice and corn output are expected to decline slightly in Q2 2007 due to earlier concerns about El Niño.
- The peso weakened in early March along with other regional currencies, triggered by the heavy sell-off in China's stock market and fears of a US economic slowdown. Subsequently, the peso was supported by reports of lower inflation and higher gross international reserves, coupled with sustained inflows of OFW remittances, export earnings and foreign investments. The peso was also buoyed by the country's sustained economic growth and improving fiscal position.
- The National Government (NG)'s fiscal deficit for January-February 2007 reached P18.6 billion, about ₱27.2 billion or 40.6 percent below the Q1 program of ₱45.8 billion. The favorable fiscal performance can be attributed to the continued double-digit growth of revenue collections and modest government spending.

<sup>2</sup> The DCS, which replaced the Monetary Survey as the basis for measuring domestic liquidity, features an expanded list of surveyed institutions that includes the BSP, commercial banks, thrift banks, rural banks, non-stock savings and loan associations and non-banks with quasi-banking functions.

<sup>3</sup> The new data series covers not only commercial banks but also thrift banks and rural banks, with initial available series starting from January 2005 to February 2007.



- Relative to the 9 March 2007 auction, T-bill rates during the 16 April auction increased slightly.

## **External Developments**

- The global economic momentum was sustained in 2006 with a gradual rebalancing in the composition of global growth. The pace of growth in Japan and emerging Asia continued to pick up while the upturn in the Euro Area had become more broad-based. Likewise, the US economy recovered late in the year as the impact of the ongoing correction in the housing market on consumption remained limited.
- Firm domestic demand, buoyant labor market conditions and benign financial conditions supported the global expansion. However, a number of risks remain, notably a sharper-than-expected slowdown in the US economy, a disorderly unwinding of global imbalances, and a potential increase in market volatility.
- Global inflation pressures have eased slightly compared to a few months ago but risk from the declining spare capacity remains.
- Emerging debt markets rallied in March as growth prospects for emerging economies, particularly Asia, remained intact following the recent sell-off in the global equities market.
- Major central banks decided to maintain their policy rates but noted that inflation risks remain. The federal funds rate was kept at 5.25 percent for the sixth consecutive time at the 20-21 March 2007 US FOMC policy meeting on indications of ongoing adjustments in the housing market coupled with the likelihood that the high level of resource utilization in the country could sustain inflation pressures. Similarly, the Bank of England's (BOE's) Monetary Policy Committee voted to maintain the official bank rate paid on commercial bank reserves at 5.25 percent during its 4-5 April 2007 meeting given evidence of a more subdued inflation profile. The Bank of Japan (BOJ), likewise, voted to keep its uncollateralized overnight call rate steady at 0.5 percent during its 9-10 April 2007 monetary policy meeting, on the premise that the monetary environment will be kept accommodative to ensure price stability while achieving sustainable growth in the medium to long term. The European Central Bank (ECB) Governing Council decided to leave its key interest rates unchanged during its 12 April 2007 policy meeting following the 25.0 basis-points increase in its 8 March 2007 meeting.



## **II. Key Considerations in the Formulation of the Monetary Policy Stance**

- The Monetary Board noted that the benign inflation outlook and manageable demand conditions suggested that there may be some room for accommodation. However, there continue to be risks to the inflation outlook coming mainly from the continuing strong growth in domestic liquidity, renewed volatility in world oil prices, and steady improvements in demand including public sector wage adjustments and higher public spending.
- On balance, however, the Monetary Board believed that the liquidity surge, the emerging risks to the inflation outlook, and the need to assess further the effects of the tiering scheme on credit activity supported keeping policy settings unchanged.
- The Monetary Board also noted that it was important to address the strong foreign inflows and liquidity expansion in the financial system by developing alternative monetary policy instruments that would absorb liquidity from the market. The development of alternative monetary policy instruments will help the BSP to not only address the robust expansion in foreign assets but also to deepen the BSP's range of monetary policy tools in better managing liquidity.
- The Monetary Board reiterated its firm commitment to address the risks to future inflation and to continue to monitor closely the evolving conditions for consumer prices, aggregate demand, domestic liquidity and other factors in order to determine the appropriate stance of monetary policy.

## **III. Monetary Policy Decision**

- After considering the risks to inflation and the evidence that has become available since its previous meeting on monetary policy, the Monetary Board approved the recommendations of the Advisory Committee.

The next meeting of the Monetary Board on the monetary policy stance is scheduled on 31 May 2007.