BANGKO SENTRAL NG PILIPINAS

HIGHLIGHTS OF THE MEETING OF THE MONETARY BOARD ON THE MONETARY POLICY STANCE HELD ON 26 MARCH 2015[1]

I. Monetary Policy Decision

The Monetary Board (MB) decided to:

a) Maintain the BSP's key policy interest rates at 4.00 percent for the overnight RRP (borrowing) facility and 6.00 percent for the overnight RP (lending) facility;

b) Maintain the current interest rates on term RRPs, RPs and SDAs; and

c) Maintain the current reserve requirement ratios.

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

- The MB's decision was based on its assessment that the inflation environment continues to be manageable. Latest baseline forecasts indicate that inflation is likely to settle within the lower half of the target range of 3.0 percent ± 1 percentage point for 2015 and 2016. The forecasts are also supported by well-anchored inflation expectations, which remain within the target band over the policy horizon.

- The Monetary Board likewise noted that the risks to the inflation outlook continue to be broadly balanced, with upside risks emanating from pending petitions for adjustments in utility rates and possible power shortages. Meanwhile, global economic prospects have turned slightly more positive but continue to be uneven, which could further mitigate upward pressures on commodity prices.

- At the same time, the Monetary Board observed that domestic demand conditions remain robust, owing to solid private demand, adequate domestic liquidity, and buoyant business sentiment. Higher public spending is also expected to support economic activity.

- Given these considerations, the Monetary Board is of the view that current monetary policy settings remain appropriate. Going forward, the BSP will continue to monitor domestic and external developments affecting the inflation outlook to ensure that the monetary policy stance remains consistent with its price and financial stability objectives.

[1] The discussions presented reflect the assessment made by the Monetary Board based on the information available at the time of the policy meeting. A comprehensive set of economic information was provided by the Technical Secretariat of the Advisory Committee (AC). The AC is composed of the Governor of the BSP as Chairman and four members, namely: the Deputy Governor of the Monetary Stability Sector, the Deputy Governor of the Supervision and Examination Sector, the Assistant Governor of the Treasury Department, and the Officer-in-Charge of the Monetary Policy Sub-Sector. The highlights of the discussions on the 26 March 2015 meeting were approved by the Monetary Board during its regular meeting held on 16 April 2015. The next meeting of the Monetary Board on monetary policy issues is scheduled on 14 May 2015.

III. Recent Developments and Inflation Outlook

The MB considered the following developments in deciding on the monetary policy stance:

A. Domestic price conditions

- Year-on-year headline inflation rose slightly in February. Other indicators also increased such as the official core inflation rate and the trend of seasonally-adjusted annualized headline inflation.

- The higher February inflation reading was driven largely by the higher prices of selected non-food items. In particular, non-food inflation increased as a result of upward adjustments in electricity rates as well as higher prices for transport services. In contrast, food inflation decelerated on ample domestic supply of key food items such as rice, corn, meat, fruits, vegetables, and sugar.

- By geographical location, inflation in the National Capital Region (NCR) rose to 2.2 percent in February from 1.5 percent in January. By contrast, inflation in areas outside NCR declined slightly to 2.6 percent from 2.7 percent a month ago.

B. Inflation expectations

- Inflation expectations depicted in forecast surveys of private sector economists by the BSP and by Consensus Economics are well within the target band over the policy horizon. Results of the BSP's February 2015 survey of private sector economists yielded lower mean inflation forecast for 2015 at 2.8 percent (from 3.1 percent in January 2015). Meanwhile, inflation forecasts for 2016 and 2017 were both unchanged at 3.4 percent. Similarly, results of the March 2015 Consensus Economics inflation forecast survey for the country showed a lower mean inflation forecast for 2015 at 2.7 percent (from 2.8 percent) and steady inflation forecast for 2016 at 3.5 percent.

C. Inflation outlook

- The latest outlook for inflation remained within the target range of 3.0 percent ± 1.0 percentage point for 2015-2016. The latest baseline inflation forecasts continued to indicate that inflation will likely settle in the lower half of the 2-4 percent target range for both 2015 and 2016. The slight increase in oil prices and higher-than-projected inflation for February 2015 were offset by the lower-than-assumed actual minimum wage increase and by the possible delay in the likely implementation of NFA rice price adjustments as well as the approved reduction in taxi fares.

- The distribution of risks to the baseline inflation forecast continues to be broadly balanced. Pending petitions for utility rate adjustments and the potential power shortages are seen to pose upside risks to the baseline inflation forecasts. Meanwhile, downside risks are linked mainly to possible slower-than-expected global economic activity (which could further drive international oil prices downward) and pending petitions for transport fare reductions.

D. Demand conditions

- Indicators of domestic demand remain firm. The latest business cycle analysis of the BSP and various leading economic indicators monitored by the BSP point to a continued economic upturn in Q1 2015. This is consistent with the results of the Q1 2015 business expectations survey showing positive confidence in the first half of 2015. Likewise, the purchasing managers' index (PMI) suggests that the Philippine economy was still in an expansion phase. Based on the January 2015 Labor Force Survey of the Philippine Statistics Authority (PSA), the unemployment rate declined to 6.6 percent from 7.5 percent a year ago, but was higher compared to the preceding quarter's 6.0 percent.

E. Supply-side indicators

Developments in Agriculture

- The retail prices of rice decreased in February 2015 partly due to the completion of the main harvest season. During the fourth week of February, the average prices of well-milled rice and regular-milled rice both declined, compared to month-ago levels.

- The Food and Agriculture Organization (FAO) Food Price Index was lower in January as prices of almost all commodities, particularly cereals and oil fell year-on-year amid ample supplies. Only the prices of sugar and dairy products remained broadly unchanged.

- The Philippine Atmospheric, Geophysical and Astronomical Services (PAGASA) latest climate monitoring and analyses indicated that the Philippines is in the midst of a weak El Niño episode. Weak El Niño is likely to result in a lower than normal rainfall pattern in different parts of the country in the coming months.

Oil Price Developments

- International oil prices recovered in February amid reports of declining oil drilling, investment, and exploration activities in the US. However, oil prices retreated in March on reports of record-high US crude oil inventories, adding to concerns of excess global supply. Tracking the movements of international oil prices, the domestic prices of petroleum products, except LPG, were reduced on 17 March.

Developments in the Utilities Sector

- Electricity rates declined in March due to lower generation costs. According to Meralco, generation rates decreased mainly on account of higher dispatch of the power plants under Power Supply Agreements. Meanwhile, according to the Department of Energy (DOE), the summer months of 2015 (i.e., April and May) could be a critical period characterized by tight power supply conditions.

F. Financial market developments

- The equities market continued to be buoyant in March. Early reports of strong corporate earnings and low inflation numbers supported buying momentum. However, the market subsequently retreated as investors cashed in on gains on the possibility of an earlier-than-expected interest rate hike by the US Federal Reserve following positive jobs data in February.

- The peso strengthened further in March as the still dovish testimony of US Fed Chairman Janet Yellen to the US Congress continued to drive demand for emerging market assets, while expectations of sustained low domestic inflation also helped lift market sentiment. The sustained inflows of foreign exchange from overseas Filipino remittances, BPO and tourism receipts, foreign portfolio and direct investments, as well as the ample level of the country's gross international reserves likewise provided support to the peso.

- Meanwhile, debt spreads inched up in March, following favorable reports on US non-farm payrolls in February, which bolstered the case for the Fed to raise policy rates beginning June. Renewed market concerns over the prospects for Greece likewise contributed to the widening pressures in emerging market debt spreads. However, debt spreads remained low as market participants continued to expect a gradual rise in US interest rates.

G. Domestic liquidity and credit conditions

- Preliminary data showed that M3 grew by 7.7 percent in January 2015 to ₱7.5 trillion. This was slower than the 11.3-percent expansion recorded in December 2014. On a month-on-month seasonally-adjusted basis, M3 increased by 1.4 percent, following the 0.5-percent increase in the previous month.

- The outstanding loans of commercial banks, net of reverse repurchase (RRP) placements with the BSP, grew at a slower rate of 17.3 percent in January 2015 from 19.9 percent in December 2014. On a month-on-month seasonally-adjusted basis, commercial bank lending decreased for both loans net of RRPs and loans inclusive of RRPs.

H. Fiscal developments

- The fiscal deficit for 2014 was ₱73.1 billion, 55.4 percent lower than the deficit incurred in 2013. This represented 27.5 percent of the ₱266.2 billion programmed deficit for 2014. Meanwhile, after excluding interest payments from total expenditures, the resulting primary surplus amounted to ₱248.1 billion, ₱88.7 billion or 55.7 percent higher than the level recorded in the previous year.

I. External developments

- Global economic prospects since the previous meeting have turned slightly more positive, albeit still uneven. Growth in the US remains firm while unemployment rate eased to 5.5 percent in February from 5.7 percent in January. Economic activity in the euro area and Japan appears to have improved but growth in major emerging markets, particularly in China and India, continues to be modest. Deflation also remains a concern, primarily in the euro area and Japan.