A. Philippine Macro-economy

1. The Philippine Economic Miracle (1980 To 2019)

The Philippine economic miracle continues and now spans four decades, from 1980 to 2019.

Through structural economic reforms introduced by seven past and present administrations, Philippine GDP growth has significantly accelerated from 2% in the 80’s, to 2.8% in the 90’s, 4.5% in the 2000’s and 6.3% the past nine years.

The Philippine economy has shown resilience with uninterrupted positive annual and quarterly GDP growth over the last twenty years and over the last 82 quarters, respectively.

In April, S&P Global Ratings upgraded the country’s credit rating to its highest in history: BBB+ or two notches above investment grade, with a stable outlook- a fitting testament to the Philippine economic miracle.

2. Drivers Of Philippine GDP Growth

The main drivers of Philippine GDP growth are investments and private consumption on the demand-side and services on the supply-side.

Fixed investments rose 14% in 2018 and accounted for 27% of GDP, the highest since the mid-1980s.

Foreign direct investments reached $9.5B average from 2016-2018, 2.5x the $3.6B average from 2010-2016.

Private consumption grew 5.6% in 2018, supported by steady Overseas Foreign remittances of $28.9B (+3.1% y-y), or 8.7% of GDP.
By sector, services grew 6.6% in 2018 and accounted for two-thirds of GDP growth, supported by BPO revenues of $21.2B (+2.9% y-y) or 6.4% of GDP and tourism revenues of $6.9B (+4.9% y-y) or 2.1% of GDP.

Inflows from OF remittances, BPOs and tourism helped to cushion the impact of trade deficit on the current account.

The current account deficit widened to $7.9B or 2.4% of GDP in 2018 from $2.1B or 0.7% of GDP in 2017 due primarily to the trade deficit which swelled to $41.4B or 12.5% of GDP in 2018 from $27.4B or 8.7% of GDP in 2017.

Imports rose 13% to $108.9B in 2018, driven mainly by capital goods. It outpaced exports which contracted by 1.8% to $67.5B.


This year, the country’s economic managers are targeting Philippine GDP growth of 6.0% to 7.0% in 2019, from 6.2% in 2018.

Philippine GDP slowed down to 5.5% in the first half of 2019, due mainly to the delayed passage of the 2019 budget and the ban on public works of 45 days before the May 2019 mid-term elections.

The government estimates the Philippine economy needs to grow by an average of at least 6.4 percent in the second half of 2019 to achieve the low-end of the 6% to 7% official target for 2019.

Over the next three years, the present administration is aiming for 6.5% to 7.5% GDP growth in 2020 and 7% to 8% GDP growth in 2021 and 2022, underpinned by its medium-term fiscal stimulus and tax-reform program.

4. Build! Build! Build! Infrastructure Program

The government’s $200-B Build! Build! Build! Infrastructure program is underway.
Out of the 75 flagship projects worth $40B, 62% has been allocated for rail transport and 25% for road transportation.

The National Economic and Development Authority has approved 38 projects, of which 11 are in construction phase.

Under Build! Build! Build!, infrastructure spending will rise from 5.1% of GDP in 2018 to 6.9% in 2022.

5. The Comprehensive Tax Reform Program (Package 1)

Build! Build! Build! is financed by a higher deficit ceiling and Package 1 of the Comprehensive Tax Reform Program (CTRP).

The budget deficit ceiling has been raised to 3.2% of GDP from 2018 to 2022 (from 2.2% of GDP in 2017).

The first tax package of CTRP was implemented at the start of 2018 and imposed higher taxes on sweetened beverages, cigarettes, fuel and automobiles, resulting in additional tax revenues of $2.5B (P134B).

At the same time, it lowered personal income taxes across the board, resulting in an annual $2.1B (P111B) cash salary windfall, to improve consumer spending.

In 2018, Package 1 contributed incremental tax revenues of $1.3B (P68B) or 0.4% of GDP, helping to keep the budget deficit within the 3.2% of GDP target.

This year, Package 1 will make a much bigger contribution of $2.5B (P133B) in tax revenues, double last year’s amount.

6. Inflation And Central Bank Response

Inflation YTD has decelerated to 3%, the midpoint of the government’s official target range of 2% to 4%, from 5.2% in 2018.
Monthly inflation peaked at 6.7% in September and October 2018 and has fallen to 1.7% in August 2019.

Higher inflation was due mainly to supply factors such as delayed importation of rice, higher energy prices and additional excise taxes.

In response, Presidential directives to increase food supply were issued in 2018 and the Rice Liberalization Act was passed in February 2019.

The Bangko Sentral ng Pilipinas (BSP) has taken a proactive monetary stance, shifting policy from aggressive tightening last year to monetary easing this year.

Last year, to control inflation, the BSP raised its policy rate five times by a cumulative 175 basis points from May to November 2018 from 3.0% to 4.75%.

This year, to spur growth and liquidity, the BSP cut its policy rate three times by a cumulative 75 bps, in May, August and September from 4.75% to 4.00%.

In addition, the BSP cut the reserve requirement ratio of universal and commercial banks by 200 bps, from May to July from 18% to 16%.

With inflation expected to remain low at 2.6% in 2019, 2.9% in 2020 and 2021, the BSP governor has signaled another reserve requirement cut of at least 100 bps by the end of this year.

7. **LCY 10-Year Bond Yield, PSEi and Peso Performances**

Inflation peaking in October, coupled with central bank easing have been the main catalysts of the Philippine bond and stock markets and the Peso in the fourth quarter of 2018 and YTD 2019.

The Philippine bond market is Asia’s best-performer.
The Philippine local-currency 10-year bond yield has fallen 228 bps to 4.78% YTD\(^1\) and has fallen 352 bps since the peak of 8.3% in October 2018.

The yield had declined by as much as 405 bps to 4.25% in August 2019.

The PSEi bull market was born again in July when it had rallied as much as 24% to 8419 from 6790 in October 2018.

The PSEi is up 6% YTD\(^2\) and up 14% since the low of 6790 in October 2018.

The Peso is up 0.8% YTD\(^3\) and has appreciated by 3.2% from P54.32 in October 2018.

The Peso had appreciated by as much as 6.5% to P50.81 in July 2019.

B. Capital Markets Outlook

_Incentives_

1. **Tax Reforms: Corporate Income Tax, Stock Transaction Tax and IPO Tax**

On September 13, the House of Representatives voted in favor of Package 2 (Corporate Income Tax and Incentives) and Package 4 (Passive Income and Financial Taxes) of CTRP.

Package 2 proposes to lower corporate income tax by 1 % per year from 30% to 20% by 2029.

It aims to align the corporate income tax rate with the rest of the Asia region, encourage business expansion and create 1.5m jobs per year.

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\(^1\) As of September 18, 2019  
\(^2\) As of September 18, 2019  
\(^3\) As of September 18, 2019
Package 4 proposes to reduce the stock transaction tax by 0.1% per year from the current 0.6% to 0.1% in 2024.

It aims to promote investment in the Philippine stock market and improve value turnover and liquidity.

Package 4 will also eliminate the IPO tax of 1% to 4%, which has been a barrier to entry for potential IPOs.

It aims to encourage IPOs especially of fast-growing small and medium enterprises.

2. **New Product: REIT Revival By Ayala Land**

Ayala Land, the country’s premier property developer, will embark on listing the country’s first Real Estate Investment Trust (REIT) within the year.

Ayala Land plans to infuse $500M of property assets with steady recurring revenues into AyalaLand REIT, Inc. or AREIT, which will have a minimum public ownership of 67%, and will raise around $300m.

3. **PSE EASy: Web-based Local Small Investor IPO Subscription Platform**

The Philippine Stock Exchange (PSE) launched a web-based IPO subscription platform for Local Small Investors (LSI), who may subscribe to as much as $2,000 in an IPO (from $500)

The PSE EASy (PSE Electronic Allocation System) portal ensures the efficient and widespread distribution of the 10% allocation to local small investors for IPOs.

The LSI allocation of Kepwealth Property Philippines Inc. IPO, the first to use PSE Easy, was 96% subscribed, from the historical average of 12%.

**Challenges**

4. **Landmark Ruling On 20% PSE Ownership Limit**
The Court of Appeals ruled in favor of Philippine Association of Securities Brokers and Dealers Inc. (PASBDI) against the Securities and Exchange Commission’s (SEC) imposition on Brokers of 20% ownership limit in the PSE on the following grounds:

1) Ownership of shares are property rights that may only be restricted in the valid exercise of police power; and

2) The harm sought to be avoided has not been established.

The landmark ruling paves the way for PSE-led capital markets reforms.

SEC’s imposition on Brokers of 20% ownership limit in the PSE has been an unnecessary road block to capital markets reforms such as the unification of the equity and debt markets through a planned merger between the Philippine Stock Exchange and the Philippine Fixed Income Exchange (Philippine Dealing and Exchange Corp or PDEEx).

5. **Early Stages Of Green Bond Issuances**

The Philippine capital markets are taking part in achieving UN’s Sustainable Development Goals.

Last year, the SEC issued guidelines for issuance of Green/ Sustainability Bonds in accordance with the ASEAN Green Bonds/ Sustainability Standards.

One of the notable green bond issuances was by AC Energy of the Ayala Group, which raised $410M in February.

AC Energy raised $300M from 5-year green bonds with coupon rate of 4.75% and raised $110M from 10-year green bonds with coupon rate of 5.25%.