Metrobank

Research and Market Strategy Department

MONTHLY ECONOMIC UPDATE: First look at 2026

125 bps Interest Rate Differential: BSP and Fed in it for the long-run

"With policy meetings scheduled in October and December, 25-25 (two cuts of 25 basis points each) is possible in principle." – BSP Governor Eli Remolona Jr.

METROBANK RESEARCH FORECASTS

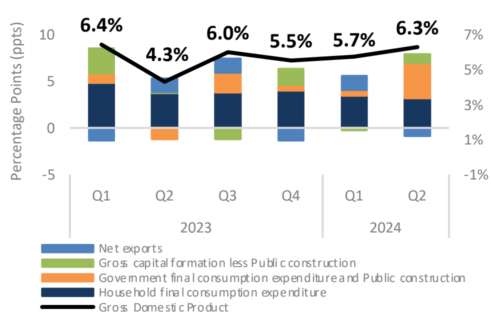
	Actual		Forecasts		
	2022	2023	2024	2025	2026
Real GDP (2018=100) average of period	7.60%	5.60%	5.70%	6.20%	6.20%
Inflation (2018=100) average of period	5.80%	6.00%	3.30%	3.00%	3.00%
BSP Target RRP Rate end of period	5.50%	6.50%	5.75%	4.75%	4.25%
Target Fed Funds Rate end of period	4.50%	5.50%	4.50%	3.50%	3.00%
USDPHP end of period	56.12	55.57	55.30	54.50	53.70

OUTLOOK

Real Economy: Sustained growth momentum

- Following its consultation visit to the Philippines on August 27 to September 6, the ASEAN+3 Macro Economic Research Office (AMRO) maintained its 6.1% and 6.3% GDP growth forecasts for the Philippines in 2024 and 2025, respectively, the same as published in AMRO's July publication. These favorable forecasts are anchored on AMRO's positive outlook on government spending, external and domestic demand, and private consumption.
- Meanwhile, the Asian Development Bank (ADB) and the World Bank (WB) forecast a lower GDP growth at 6.0% and 5.8%, respectively, for 2024; and 6.2% and 5.9%, respectively, for 2025.
- However, in a recent interview, WB Lead Economist for the Philippines Gonzalo Varela said that the multilateral organization's latest GDP growth forecast for the Philippines has been slightly updated to 6.0%, taking into account expectations of monetary easing by the Bangko Sentral ng Pilipinas (BSP).
- Metrobank Research slightly revised its full-year forecast downward to 5.7% from 5.8% for 2024, as we expect lagged effects of the high interest rates to weigh on growth. However, we expect consumption and investments to gradually pick up next year following the start of the BSP's easing cycle. Metrobank Research expects this growth momentum to continue until 2026, with GDP growth projected at 6.2% annually for both 2025 and 2026.
- Related Articles: 1) Philippines eyes return to emerging market bond index
  2) BSP's rate cuts promise relief amid economic challenges

PH GDP Growth (in %)
2018=100

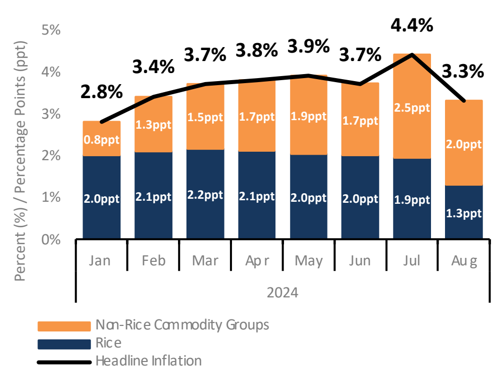


Source: Philippine Statistics Authority (PSA)

Inflation: Settling within target

- August headline inflation slowed down to 3.3% year-on-year (YoY) from the 4.4% YoY in July, slightly above the 3.2% Metrobank Research estimate for the month. This brings the year-to-date inflation down to 3.6%, which is within the BSP's 2%-4% target for the full-year.
- On a month-on-month (MoM) basis, inflation accelerated by 0.1% in August, slower than the 0.7% in the preceding month.
- Core inflation, which excludes selected food and energy items, continues its downtrend at 2.6% YoY in August from the 2.9% in July.
- While rice prices remain the main contributor to headline inflation with a 1.3-percentage-point (ppt) contribution for the month, this is a significant drop from the 1.9 ppt contribution in July as rice inflation slowed to 14.7% YoY in August from 20.9% in the prior month.
- We expect the impact of the lower rice tariffs to continue to pull down inflation in the coming months. Considering high base effects, rice inflation may be seen in single digits starting September.
- There were still upside risks to inflation this month as the risk of African Swine Fever affected the local supply of pork and the heavy rains brought flooding to agricultural lands, which we expect to partially offset the decline in rice and oil prices. We estimate inflation in September at 2.3% YoY.
- Metrobank Research retains its FY2024 inflation forecast of 3.3%, owing to the continued impact of lower rice tariffs and the within-target year-to-date inflation. Meanwhile, full-year inflation is forecast at 3.0% for both 2025 and 2026.
- Related Articles: 1) August Inflation Update: Philippine inflation set to continue downward trend
  2) September inflation preview: Will inflation finally slide to the 2% level?

PH Inflation Rate (in %)
2018=100



Source: Philippine Statistics Authority (PSA)

OUTLOOK

BSP RRP: Cutting ahead of the Fed

- The Bangko Sentral ng Pilipinas (BSP) began its monetary easing cycle with a 25-basis-point (bp) policy rate cut ahead of the US Federal Reserve (Fed) which its lowered Reverse Repurchase (RRP) Rate to 6.25% and narrowed the RRP and Fed Funds Rate differential to 75 bps.
- However, when the Fed reduced its policy rate to 4.75% - 5.00% in September 17-18, the interest rate differential (IRD) widened to 125 bps.
- On September 20, the BSP doubled down on its more dovish stance by announcing a 250-bp reduction in the reserve requirement ratio (RRR) from 9.50% to 7.00%, effective October 25.
- On September 26, BSP Governor Eli Remolona Jr. also signaled 25 bps worth of cuts each in the October 17 and December 19 Monetary Board (MB) meetings, supporting our call for a total of 75 bps worth of cuts for FY2024.
- Metrobank Research maintains its baseline forecast of a total of 75 bps worth of cuts for the year, with the recent 25-bp cut in August to be followed by two more 25-bp cuts each during the remaining MB meetings. This will bring the upper-end of the target RRP to 5.75% by year-end.
- Related Articles: 1) So it Begins: BSP starts monetary easing
  2) Philippines: Can Remolona forge ahead of the Fed again?
  3) After lowering policy rates, the central bank will soon reduce banks' cash requirements

Fed Funds Rate: Cutting deeper than the BSP

- The US Federal Reserve (Fed) reduced the Federal Funds Target Rate (FFR) by 50 bps to 4.75% - 5.00% in its Federal Open Market Committee (FOMC) meeting last September 17-18, widening the interest rate differential (IRD) to 125 bps.
- The FOMC has shifted its focus away from inflation, noting that although it remains elevated, it has already made further progress toward its 2% target. Officials are now more concerned with the labor market, recognizing that job gains have slowed.
- Based on the September Summary of Economic Projections (SEP), the Fed's inflation has been revised downwards, indicating a faster pace towards the 2% target. Meanwhile, the Fed's unemployment rate projections have been revised upward. Additionally, the Fed's September dot plot is pointing at lowering the policy rate *at* a faster pace than earlier signaled, with the terminal rate potentially at 3.00% by 2026.
- Metrobank Research has revised its forecast for the target FFR and is now expecting 100 bps worth of cuts for FY2024, which should bring the upper end of the target FFR to 4.50%. Moreover, we project a cumulative total of 150 bps worth of cuts in FY2025 and FY2026, which should bring the upper range of the target FFR by end-2025 and end-2026 to 3.50% and 3.00%, respectively.
- Related Articles: 1) Policy Rate Views: More rate cuts ahead for US and the Philippines

Foreign Exchange: Wider differential meets trade deficit

- In his August 23 speech at the Jackson Hole Symposium, Fed Chair Jerome Powell claimed that "The time has come for policy to adjust," signaling a cut in interest rates. However, the size of the policy rate cut was left to speculation, causing volatility in the market. This has led to the peso trading as high as 56.610 on September 3, and as low as 55.695 on September 17, leading up to the FOMC meeting on September 17-18.
- Following the 50-bp cut delivered by the Fed in its September policy meeting, the dollar appreciated against the peso despite the Fed projecting another 50 bps to be cut from interest rates before the end of the year. On September 27, the USD/PHP closed at 56.076.
- Given the recent market movements and the forecasted BSP policy rate adjustments by the Fed and the BSP, Metrobank Research projects the USD/PHP spot rate to continue along a downtrend, approaching 55.3 by end-2024, down to 54.5 by end-2025, and 53.7 by end-2026.

LOCAL NEWS

PH Balance of Payments: Shrinking deeper

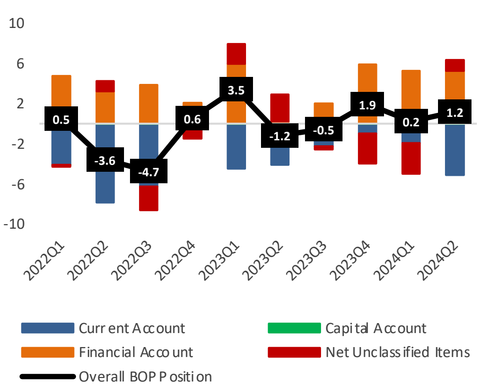
Q2 BOP reverses to surplus

- The Philippines' overall balance of payments (BOP) position reversed to a USD 1.4-billion surplus in Q2 from the USD 1.2-billion deficit in the same quarter last year.
- The reversal in the Q2 BOP position is mainly attributed to the higher net inflow in the financial account, which was offset by an increase in the current account deficit.
- The country's current account deficit expanded by 24.4% YoY in Q2 to USD 5.1 billion from the USD 4.1 billion posted in the same quarter in 2023. This comes as the trade in goods deficit grew by 13.6% YoY and the trade in services surplus slightly dropped by 13.6% YoY.
- Meanwhile, the capital account grew by 15.4% YoY to USD 17.6 billion from the USD 15.2 billion in Q2 2023, owing to higher net receipts in the government's capital transfers.
- Finally, the net inflows to the financial account swelled to USD 5.3 billion, a staggering 2,490.3% YoY growth from the USD 203.7 million net inflows recorded in the same quarter last year. This is mainly due to higher net receipts in the government's capital transfers.

BOP surplus shrinks year-to-date

- Despite the reversal of the BOP position in Q2, the country's BOP surplus for the first six months of 2024 still dropped by 36.2% YoY to USD 1.4 billion from the USD 2.3 billion recorded in the same period last year.
- The year-to-date BOP surplus reflects a strong 70.3% increase in the net inflows in the financial account, a 17.8% drop in the account deficit and a 13.5% expansion in the capital account surplus.

PH BOP
In PHP billion



Source: Philippine Statistics Authority (PSA)

BSP projects higher BOP surplus

- This September, the BSP adjusted its BOP projections higher relative to its last projection in June, expecting a higher surplus in 2024 and 2025 at USD 2.3 billion and USD 1.7 billion, respectively.
- Latest BSP numbers also show a wider current account deficit projection in 2024 and 2025 to USD 6.8 billion and USD 5.5 billion, respectively.