Philippines—Update

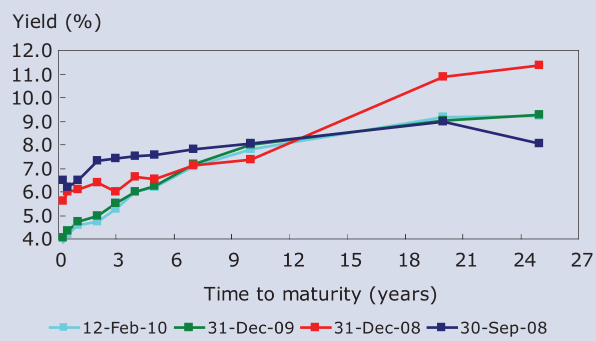
Yield Movements

Philippine government bond yields declined across all tenors between end-2009 and February 2010, except at the very long-end of the curve. Yields on 2-year bonds fell by as much as 275 basis points, while yields on 10-year debt dropped 175 basis points. In the run-up to its foreign bond issue on January 7 of this year, the Bureau of the Treasury (BTr) often declined to accept bids which it felt to be unacceptably high **(Figure 1).**

The Philippines' budget deficit widened to a record PHP298.5 billion in 2009, which was equivalent to 3.9% of gross domestic product (GDP). Increased spending to support the economy amid the global crisis and weak tax collections drove the 2009 deficit above the government's target of PHP250 billion. The government is maintaining its projected budget deficit ceiling at PHP293 billion for 2010, but will monitor the economy's performance in 1Q09 to determine whether the target needs to be adjusted.

Consumer price inflation for the month of February was 4.2% year-on-year (y-o-y), slightly less than January's rate of 4.3%. The rise in consumer prices in January has been attributed to oil and food price hikes. Headline inflation for 2009 averaged 3.2%, which was well within the government's target of 2.5%–4.5%. The inflation target for 2010 has been set by the Development Budget Coordinating Committee (DBCC) at 4.5% ±1.0 percentage point. The key overnight borrowing rate has remained at a record low of 4.0% and the overnight lending (repurchase) facility at 6.0% since July 2009. However, the peso rediscount rate was raised 50 basis points to 4.0% (effective 1 February) as BSP started to unwind its stimulus measures. Prior to this, the peso rediscount rate had been held at 3.5% from March 2009 until January 2010 to ensure the orderly operation of domestic financial markets amid the global crisis. Meanwhile, the economy expanded 1.8% y-o-y in 4Q09, while full year GDP grew at a slower rate of 0.9% after expanding 3.8% in 2008.

Figure 1: Philippines' Benchmark Yield Curve–Local Currency Government Bonds



Source: Bloomberg, LP.

Size and Composition

By the end of 2009, total government local currency (LCY) bonds stood at PHP2.56 trillion. Bonds issued by BTr and agencies owned and controlled by the government rose 12.9% and 18.2% from end-2008, respectively. However, treasury bills decreased 19.2% y-o-y in 2009, which resulted in marginal growth of 3.1% y-o-y for total government LCY bonds. On a quarterly basis, the stock of total government bonds increased 2.3% **(Table 1)**.

The National Food Authority (NFA) raised PHP9 billion worth of 10-year bonds in October for maturing loans, capital expenditures, and rice imports. However, NFA postponed its planned issuance of an additional PHP5 billion–PHP10 billion of long-term bonds from December 2009 to 1Q10, dependent upon local debt market conditions at the planned time of issue.

In November, the National Development Corporation (NDC) sold PHP3.5 billion worth of 5-year bonds, with bids reaching twice the volume offered, indicating robust investor appetite. Funds raised will be used to repair and upgrade

Table 1: Size and Composition of Local Currency Bond Market in the Philippines

	Amount (billion)								Growth Rate (%)						
	Sep-09		Oct-09		Nov-09		Dec-09		Sep-09		Oct-09	Nov-09	Dec-09		
	PHP	USD	PHP	USD	PHP	USD	PHP	USD	y-o-y	q-o-q	m-o-m	m-o-m	y-o-y	q-o-q	m-o-m
Total	2,817	59	2,855	59	2,879	59	2,912	63	7.5	2.3	1.4	0.8	8.1	3.4	1.1
Government	2,504	52	2,538	53	2,545	52	2,560	56	3.0	2.0	1.3	0.3	3.1	2.3	0.6
Treasury Bills	607	13	639	13	620	13	622	13	(20.5)	(10.6)	5.1	(2.9)	(19.2)	2.4	0.3
Treasury Bonds	1,807	38	1,801	38	1,823	37	1,839	40	14.2	7.1	-0.4	1.2	12.9	1.7	0.9
Others	89	2	98	2	102	2	100	2	5.8	0.0	10.1	3.6	18.2	11.8	(2.0)
Corporate	313	7	318	7	335	7	351	8	65.8	5.4	1.6	5.4	66.5	12.4	5.0

m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Note:
1. Calculated using data from national sources.
2. Bloomberg end-of-period LCY—USD rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. "Others" includes government-guaranteed bonds such as Land Bank of the Philippines and National Power Corporation (Napocor).
Source: Bureau of the Treasury and Bloomberg LP.

irrigation facilities. Moreover, President Gloria Macapagal Arroyo signed Executive Order 824-A on 22 October to allow NDC to issue infrastructure bonds of up to PHP50 billion to finance the implementation of infrastructure projects. The National Economic and Development Authority (NEDA) and NDC will select infrastructure projects under NEDA's Medium-Term Public Investment Program (MTPIP) that wil be funded by the proceeds of the bonds.

On 18 November, the Power Sector Assets and Liabilities Management Corporation (PSALM) launched a new 2024 global bond issue of up to USD600 million and re-opened its 2019 USD bonds, inviting investors holding National Power Corporation (Napocor) bonds maturing in 2010 and 2011 to participate in a debt exchange program that allows them to swap their bonds into the new PSALM issue.

The Philippine government sold USD1.5 billion of bonds in a dual-tranche offering in January of this year that was more than six times oversubscribed. The issue comprised a USD650 million re-opening of the 2020 bonds at a yield of 5.67% and a USD850 million re-opening of the 2034 bonds at a yield of 6.66%. The sale was the first international global bond transaction in Asia in 2010, leading other Asian borrowers to tap the offshore market. Furthermore, the government successfully sold JPY100 billion worth of 10-year *samurai* bonds via private placement in late February, with a guarantee from the state-backed Japan Bank for International Cooperation (JBIC). The bonds were priced at par and carried a coupon of 2.32%. The Department of Finance (DOF) said the latest bond sale completes its planned foreign debt market issuance of USD2.5 billion for 2010.

Total LCY corporate bonds outstanding as of end-December 2009 stood at PHP351 billion for a 66.5% y-o-y rise. Of the total amount, PHP127.8 billion, or 36%, were held by local and foreign commercial banks, while the remaining 64% were held by non-financials. More corporates issued bonds in 4Q09, resulting in a 12.4% q-o-q increase in the size of the total corporate bond market.

In October, Unionbank of the Philippines issued lower Tier 2 notes worth PHP3.75 billion, while Allied Bank issued PHP3.5 billion of long-term negotiable certificates of deposit. Real estate companies Megaworld and Filinvest Land each sold PHP5 billion in November to finance their respective projects. Also, JG Summit sold PHP9 billion in 5-year bonds to support capital expenditure requirements.

Meanwhile, the geothermal company Energy Development Corporation (EDC) tapped the local bond market in December and sold PHP12 billion worth of fixed-rate bonds to investors with tenors of 5.5 and 7 years. A portion of the proceeds from the issue will be used to refinance and re-denominate EDC's Miyazawa II loan, which will mature in June 2010. The Miyazawa II loan is under the New Miyazawa Initiative, a financial support mechanism started in 1998 by the Japanese government to assist Asian countries in overcoming their economic difficulties. Also, the Manila Electric Company (Meralco) raised PHP5.5 billion in a December bond offering, which will be used for corporate funding requirements.

San Miguel Brewery remains the largest corporate issuer in the Philippines, with outstanding bonds totaling PHP38.8 billion, followed by Banco de Oro Universal Bank (PHP33.0 billion), and Meralco (PHP20.6 billion). The amount of bonds outstanding among the top 20 corporate issuers comprised 82% of the total corporate bond market at the end of 2009 **(Table 2)**.

The Philippine Dealing and Exchange Corporation (PDEx) reported that the fixed-income trading volume for government and corporate securities reached PHP2.52 trillion as of 9 December. The 2009 year-to-date volume rose by PHP585 billion, or 30%, from last year's volume and PDEx recorded PHP49.4 billion in trades for a 17% y-o-y increase. Corporate bonds issued and listed on PDEx are Ayala Corporation; Ayala Land, Inc.; Globe Telecom, Inc.; Manila Water Company, Inc.; San Miguel Brewery, Inc.; Megaworld Corporation; Energy Development Corporation; Metropolitan Bank and Trust Company; and Rizal Commercial Banking Corporation.

Table 2: Top 20 Corporate Bond Issuers as of December 2009

Rank	Issuer	Amount Outstanding (PHP billion)
1	San Miguel Brewery Inc.	38.80
2	Banco de Oro Unibank Inc.	33.00
3	Manila Electric Company	20.58
4	Metropolitan Bank & Trust	18.50
5	Philippine National Bank	17.75
6	Petron Corporation	16.30
7	Rizal Commercial Banking Corporation	16.00
8	Globe Telecom	15.80
9	Robinsons Land Corporation	15.00
10	JG Summit Holdings Inc.	13.31
11	Energy Development Corporation	12.00
12	SM Prime Holdings Inc.	11.50
13	Bank of Philippine Islands	10.00
14	SM Investments Corporation	9.40
15	Allied Banking Corporation	8.00
16	Ayala Land Inc.	7.00
17	Aboitiz Power Corporation	6.88
18	Megaworld Corporation	6.40
19	Ayala Corporation	6.00
20	Security Bank Corporation	6.00
Top 20 Total		**288.22**
Total Corporate Bonds Outstanding		**351.42**
Top 20/Total Corporate Bonds Outstanding		**82%**

Source: Bloomberg LP.

Rating Changes

In January, three major international rating agencies affirmed their respective outlook and ratings for the Philippines **(Table 3)**.

Table 3: Selected Sovereign Ratings and Outlook for the Philippines

	Moody's	S&P	Fitch
Long-Term LCY Rating	Ba3	BB-	BB+
Outlook	Stable	Stable	Stable

LCY = local currency.
Source: Rating agencies.

Moody's Investors Service has kept its stable outlook and Ba3 long-term LCY rating despite expectations that the Philippines will post the slowest economic growth in Southeast Asia this year.

Standard & Poor's has retained its stable outlook and BB- long-term LCY rating, citing the country's strong external liquidity position and its track record of resilient economic growth.

Fitch Ratings affirmed its stable outlook and BB+ long-term LCY issuer default rating, citing manageable external financing requirements in spite of weaknesses in public finances.

Policy, Institutional, and Regulatory Developments

Monetary Board Aligns Rediscount Rate with Reverse Repurchase Rate

Bangko Sentral ng Pilipinas' (BSP) Monetary Board decided on 28 January to raise the peso rediscount rate by 50 basis points to 4.0% effective 1 February in a sign that the BSP has started to unwind its stimulus measures. The peso rediscount rate was previously held at 3.5% to ensure the orderly operation of domestic financial markets amid the global crisis. The overnight borrowing, or reverse repurchase facility, and the overnight lending, or repurchase facility, remained at 4.0% and 6.0%, respectively.

PSE Tightens Rules on Short-Term Lending

The Philippine Stock Exchange (PSE) released Guidelines on Safeguards Against Securities Borrowing and Lending Program Violations and Expected Minimum Response by Trading Participants on 19 February. PSE identified seven possible violations as follows: (i) the unauthorized lending of a client's securities, (ii) denial of the beneficial owner's right to vote, (iii) failure to share lending fees to beneficial owners of securities, (iv) breach of foreign ownership limits, (v) failure to manage collateral received resulting in loss of possible income, (vi) unreasonably large value of collateral requirements, and (vii) violators failure to properly distribute manufactured dividends. Violators are levied fines of between PHP10,000 and PHP50,000, while grave situations can result in the suspension of the trading participant.

The guidelines will take effect on 5 March.