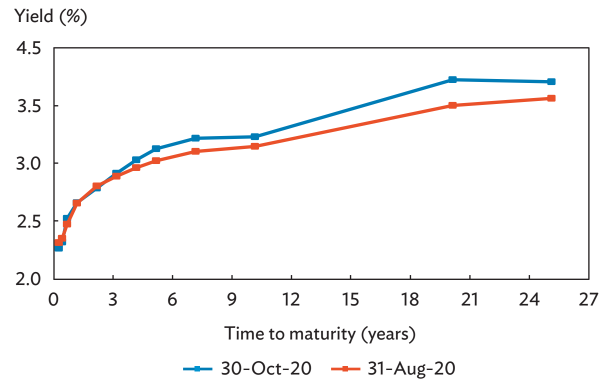
Philippines

Yield Movements

The yield curve of local currency (LCY) government bonds in the Philippines steepened between 31 August and 30 October (**Figure 1**). Yields on bonds with 1-month, 3-month, and 2-year maturities dropped on an average of 7 basis points (bps). The remaining tenors all saw increases in their yields. Bond yield for 1-year tenor increased the least at 0.6 bps, while those for 6-month and 3-year to 10-year tenors increased an average of 15 bps. Larger yield increases were seen in 20-year and 25-year maturities at 45 bps and 29 bps, respectively. This steepening led to a widening of the yield spread between 2-year and 10-year tenors during the review period from 69 bps to 89 bps.

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



Source: Based on data from Bloomberg LP.

The decline in government bond yields at the shorter-end of the curve was due largely to the accommodative monetary policy stance of the Bangko Sentral ng Pilipinas (BSP) and the inflation rate remaining subdued.

The reverse repurchase rate was held steady at 2.25% for the second consecutive time during the BSP's monetary policy meeting on 1 October, citing easing inflation and encouraging signs of domestic economic recovery. Since the start of the year through October 2020, the central bank had slashed 175 bps from the policy rate, placing it to a historically low level. The BSP maintained the view that the pause will allow it to evaluate previous easing measures' effect in the economy. The BSP is expected to reassess its policy actions based on the third quarter (Q3) economic performance which remained sluggish. The slower-than-expected gross domestic product (GDP) growth provides room for a rate cut, while excess liquidity and negative real interest rates will likely restrain the central bank's policy space.

Consumer price inflation picked up to 2.5% y-o-y in October after easing in September (2.3% y-o-y) and August (2.4% y-o-y). The acceleration mainly came on the back of higher prices of heavily-weighted food and non-alcoholic beverages. Inflation rate averaged 2.5% for the first 10 months of the year and is within the government target of 2.0%–4.0% for full-year 2020. With domestic demand remaining weak due to the coronavirus disease (COVID-19) pandemic, the BSP has forecast inflation to average 2.3% in 2020, 2.8% in 2021, and 3.0% in 2022.[8]

High liquidity in the financial system, along with a sustained preference for liquid assets, has also kept bond yields grounded at the shorter-end of the curve. The uncertainty and risks surrounding the pandemic have made investors position their funds in the more liquid portion of the curve as they await fresh developments.

On the other hand, yield increases at the longer-end of the curve stem from expectations that inflation may pick up with the further reopening of the economy and easing of quarantine restrictions that will spur economic activities. Gloomy economic growth forecasts may have also weighed on investor sentiment, leading some to trim their demand for long-term investments to avoid looming risks.

The Philippine economy remained in a recession after recording a GDP contraction of 11.5% y-o-y in Q3 2020; however, it was an improvement from the revised 16.9% y-o-y decline in Q2 2020. The double-digit decline in growth rate can be attributed to the 2-week reimposition of stricter quarantine measures in August in some areas, including the country's economic center of Metro Manila, after daily cases of COVID-19

[8] BSP forecast as of October 2020.

had escalated. Only government consumption on the expenditure side and agriculture sector on the income side saw y-o-y increases. The government expects the economy to contract between 4.5% y-o-y and 6.6% y-o-y in 2020, but will review its projections to account for the Q3 2020 figure.

The Philippine peso sustained its strength against the United States (US) dollar despite the recession and the extended community quarantine resulting from the Philippines having the highest number of COVID-19 cases in emerging East Asia.[9] The strength of the peso is generally traced to low domestic demand that reflects low imports and thus weak demand for US dollars. In October, the exchange rate movement was range-bound, prompted by the passage of the 2021 Philippine national budget, continued reopening of the economy, decline in daily COVID-19 cases, easing of some community quarantine restrictions, and ongoing negotiations over a COVID-19 pandemic stimulus package as well as elections in the US. The peso traded at PHP48.41 to the US dollar on 30 October, reflecting a year-to-date gain of 4.6%.

Size and Composition

Total LCY bond outstanding in the Philippines reached PHP8,136.4 billion (USD167.8 billion) at the end of September on growth of 8.8% quarter-on-quarter (q-o-q) and 21.5% y-o-y (**Table 1**). The rate of expansion in Q3 2020 was faster than in Q2 2020 and was supported by both the government and corporate segments on the back of higher issuance volumes. At the end of Q3 2020, government bonds comprised 79.9% of the LCY bond market, and corporate bonds accounted for the remaining 21.1%.

Government bonds. LCY government bonds outstanding amounted PHP6,503.0 billion at the end of Q3 2020, increasing 10.1% q-o-q. The increase in market size was supported by Treasury bills and, in particular, Treasury bonds. The Bureau of the Treasury (BTr) issued another tranche of Retail Treasury Bonds (RTBs) to raise more funds for the government's pandemic responses. At the same time, the BSP started issuing its own securities as additional instrument for its monetary policy implementation and liquidity management operations, adding to the government's debt.

Government bond issuance in Q3 2020 strongly rebounded on growth of 65.4% q-o-q, following a decline of 6.9% q-o-q in Q2 2020. It totaled PHP1,105.8 billion, lifted by Treasury bonds and the maiden issuances of central bank securities.

Treasury bonds issued in the quarter reached PHP651.3 billion, more than triple the amount issued in Q2 2020. The high debt sales volume was due to the issuance of RTBs in August when the BTr raised a record PHP516.3 billion. The timing has been conducive for

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q3 2019		Q2 2020		Q3 2020		Q3 2019		Q3 2020	
	PHP	USD	PHP	USD	PHP	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**6,699**	**129**	**7,477**	**150**	**8,136**	**168**	**(0.1)**	**15.7**	**8.8**	**21.5**
Government	5,253	101	5,904	119	6,503	134	(0.7)	14.4	10.1	23.8
Treasury Bills	553	11	797	16	876	18	(15.3)	25.9	10.0	58.5
Treasury Bonds	4,678	90	5,068	102	5,537	114	1.3	13.5	9.3	18.4
Central Bank Securities	0	0	0	0	50	1	–	–	–	–
Others	22	0.4	40	0.8	40	0.8	(0.03)	(35.5)	(0.02)	83.3
Corporate	1,447	28	1,573	32	1,633	34	2.1	20.7	3.8	12.9

( ) = negative, – = not applicable, PHP = Philippine peso, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third quarter, USD = United States dollar, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg end-of-period local currency–USD rates are used.
3. Growth rates are calculated from local currency base and do not include currency effects.
4. "Others" comprise bonds issued by government agencies, entities, and corporations for which repayment is guaranteed by the Government of the Philippines. This includes bonds issued by Power Sector Assets and Liabilities Management and the National Food Authority, among others.
5. Peso Global Bonds (PHP-denominated bonds payable in USD) are not included.
Sources: Bloomberg LP and Bureau of the Treasury.

[9] This covers the period from 6 August to 15 October. 2020. COVID-19 in Charts: Where Does PH Stand in ASEAN, World? 16 October. https://www.rappler.com/newsbreak/data-documents/coronavirus-charts-where-philippines-stands-asean-world.

the government to secure a good portion of funds for its spending needs amid the COVID-19 pandemic as interest rates remain low while high liquidity in the market drew in strong demand from investors. The 5-year security is the Treasury's second RTB issuance in 2020, following its PHP310.8 billion sale in February. During the quarter, the BTr rejected bids for 10-year and 20-year Treasury bonds at two auctions subsequent to the RTB sale as investors sought higher yields and, to some extent, the government had already secured sufficient financing.

The BSP issued central bank securities totaling PHP50.0 billion in Q3 2020. The initial offerings were small in volume with short maturities, but they will be adjusted depending on market response as well as the market liquidity forecast.

Issuance of Treasury bills, on the other hand, amounted to PHP488.6 billion on a decline of 17.2% q-o-q in contrast to the double-digit growth posted in Q2 2020. The drop in debt sales was traced to lower offer volumes during the quarter. The BTr also rejected bids for 365-day Treasury bills in one of the auctions as investors demanded higher rates.

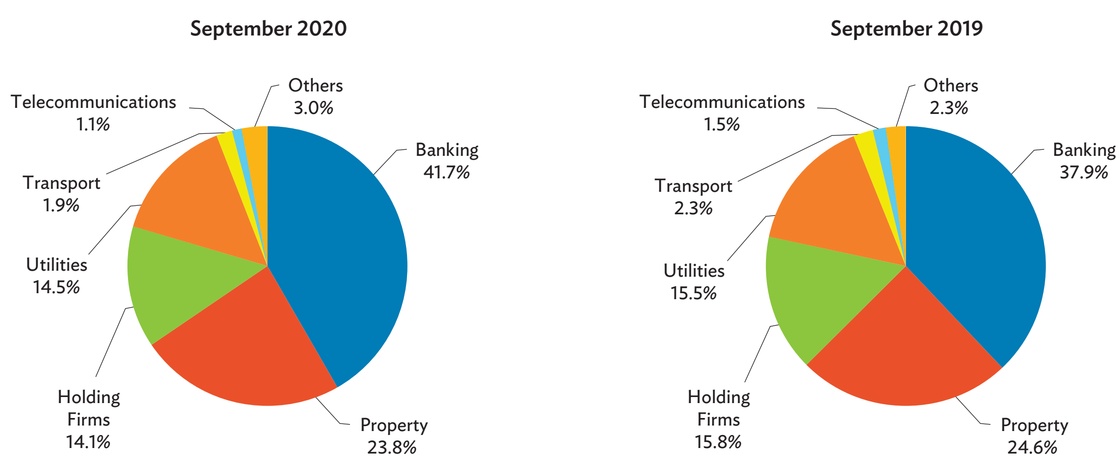
The BTr deferred its plan to issue samurai and panda bonds in 2020 as funds raised domestically were enough to cover the government's financing requirements. At the onset of the COVID-19 pandemic, the BTr considered tapping debt markets in the People's Republic of China and Japan to raise funds. However, the government's PHP540 billion advance credit from the BSP allowed the BTr to shelf this plan. Instead, the BTr will issue a second tranche of *Premyo* bonds to retail investors in November.[9]

Corporate bonds. The LCY corporate bond market rebounded in Q3 2020 to expand 3.8% q-o-q after contracting 0.4% q-o-q in Q2 2020. Corporate bonds outstanding reached PHP1,633.3 billion at the end of Q3 2020 on the back of more bond issuances during the quarter as the economy gradually reopened.

The banking sector remained the largest segment of the LCY corporate bond market in Q3 2020. The sector's share increased to 41.7% at the end of September from 37.9% at the end of September 2019 as banks upped their issuance volume over the past year (**Figure 2**). Properties and utilities companies hold the second and third spots, respectively, comprising 23.8% and 14.5% of the market; however, their shares were lower compared with September 2019. The holding firms, transport, and telecommunications sector saw lower shares in September 2020 versus a year earlier, while the share of "others" was slightly up.

The top 30 corporate issuers have an aggregate debt outstanding of PHP1,451.3 billion at the end of September or 88.9% of the total corporate bond market (**Table 2**). The banking sector comprised the largest share at 43.8%, which was equivalent to PHP649.9 billion. This was

Figure 2: Local Currency Corporate Bonds Outstanding by Sector



Source: Based on data from Bloomberg LP.

[10] *Premyo* bonds act as an investment and a ticket to win cash and noncash prizes for retail investors.

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in the Philippines

	Issuers	Outstanding Amount				
		LCY Bonds (PHP billion)	LCY Bonds (USD billion)	State-Owned	Listed Company	Type of Industry
1.	Metropolitan Bank	130.8	2.7	No	Yes	Banking
2.	Ayala Land	121.2	2.5	No	Yes	Property
3.	BDO Unibank	117.4	2.4	No	Yes	Banking
4.	SM Prime Holdings	103.6	2.1	No	Yes	Holding Firms
5.	Bank of the Philippine Islands	86.1	1.8	No	Yes	Banking
6.	SMC Global Power	80.0	1.6	No	No	Electricity, Energy, and Power
7.	Security Bank	66.3	1.4	No	Yes	Banking
8.	San Miguel	60.0	1.2	No	Yes	Holding Firms
9.	China Bank	56.2	1.2	No	Yes	Banking
10.	Rizal Commercial Banking Corporation	55.3	1.1	No	Yes	Banking
11.	Philippine National Bank	52.2	1.1	No	Yes	Banking
12.	SM Investments	48.3	1.0	No	Yes	Holding Firms
13.	Vista Land	43.6	0.9	No	Yes	Property
14.	Petron	42.9	0.9	No	Yes	Electricity, Energy, and Power
15.	Ayala Corporation	40.0	0.8	No	Yes	Holding Firms
16.	Aboitiz Power	40.0	0.8	No	Yes	Electricity, Energy, and Power
17.	Aboitiz Equity Ventures	37.0	0.8	No	Yes	Holding Firms
18.	Maynilad	32.5	0.7	No	No	Water
19.	Union Bank of the Philippines	26.6	0.5	No	Yes	Banking
20.	Philippine Savings Bank	25.4	0.5	No	Yes	Banking
21.	Robinsons Land	25.2	0.5	No	Yes	Property
22.	Manila Electric Company	23.0	0.5	No	Yes	Electricity, Energy, and Power
23.	Filinvest Land	22.0	0.5	No	Yes	Property
24.	San Miguel Brewery	22.0	0.5	No	No	Brewery
25.	East West Banking	17.7	0.4	No	Yes	Banking
26.	Robinsons Bank	16.0	0.3	No	No	Banking
27.	GT Capital	15.1	0.3	No	Yes	Holding Firms
28.	Doubledragon	15.0	0.3	No	Yes	Property
29.	PLDT	15.0	0.3	No	Yes	Telecommunications
30.	San Miguel Food and Beverage	15.0	0.3	No	Yes	Food and Beverage
Total Top 30 LCY Corporate Issuers		**1,451.3**	**29.9**			
Total LCY Corporate Bonds		**1,633.3**	**33.7**			
Top 30 as % of Total LCY Corporate Bonds		**88.9%**	**88.9%**			

LCY = local currency, PHP = Philippine peso, USD = United States dollar.
Notes:
1. Data as of 30 September 2020.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Bloomberg LP data.

followed by holdings firms and property firms with shares of 20.5% (PHP304.0 billion) and 15.3% (PHP227.0 billion), respectively. The corporate issuers are Metropolitan Bank, Ayala Land, BDO Unibank, and SM Prime Holdings with bonds outstanding of over PHP100 billion each.

Bond issuance activities from the corporate sector picked up in Q3 2020 to PHP126.3 billion from PHP27.6 billion in the previous quarter. As the economy gradually reopened, even amid continued uncertainty from the COVID-19 pandemic, firms returned to tap the capital market to fund their business operations and recovery plans. The timing is favorable as firms can take advantage of the low-interest-rate environment and abundant liquidity in the market.

Notable debt issuances in Q3 2020 were predominantly from the banking sector with the purpose largely to support their lending activities. BDO Unibank had the largest bond issuance during the quarter with a PHP36.0 billion 2-year bond (**Table 3**). Another notable bond issuance was the Bank of the Philippine Islands' landmark COVID-19 response bond, which raised PHP21.5 billion. It was the Philippines' first bond issued as a direct response to the COVID-19 pandemic. The proceeds will be used to support lending activities to eligible micro, small, and medium-sized enterprises to sustain or restart their operations amid financial difficulties caused by the pandemic.

Table 3: Notable Local Currency Corporate Bond Issuances in the Third Quarter of 2020

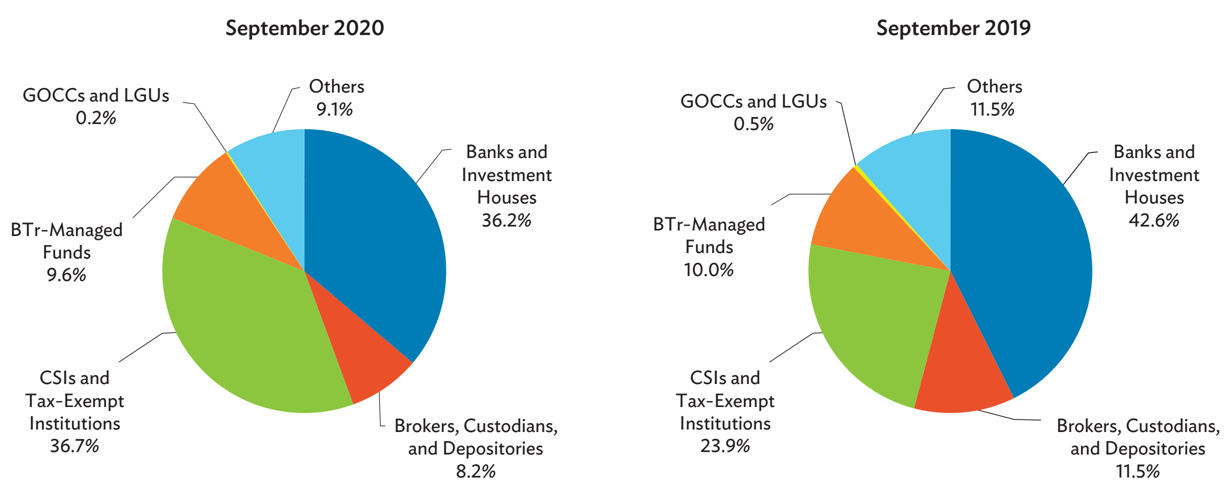
Corporate Issuers	Coupon Rate (%)	Issued Amount (PHP billion)
BDO Unibank		
2-year bond	3.13	36.00
Bank of the Philippine Islands		
2-year bond	3.05	21.50
Rizal Commercial Banking Corporation		
2-year bond	3.25	16.62
Security Bank		
2-year bond	3.13	13.50
Robinsons Land		
3-year bond	3.68	12.76

PHP = Philippine peso.
Source: Based on data from Bloomberg LP.

Investor Profile

Contractual savings and tax-exempt institutions and banks and investment houses had nearly the same share of LCY government bond holdings as one another at the end of September, which reflected a change in the investor landscape from a year earlier (**Figure 3**). Contractual savings and tax-exempt institutions' market shares rose significantly to 36.7% from 23.9% in September 2019. During the same period, banks and investment houses market share dropped to 36.2% from 42.6% a year earlier. BTr-managed funds had the third-largest market share with 9.6%, outpacing the "others"

Figure 3: Local Currency Government Bonds Investor Profile



BTr = Bureau of the Treasury, CSIs = contractual savings institutions, GOCCs = government-owned or -controlled corporations, LGUs = local government units.
Source: Bureau of the Treasury.

investor group and brokers, custodians, and depositories with 9.1% and 8.2% shares, respectively. Government-owned or -controlled corporations and local government units remained the smallest investor group with only a 0.2% market share.

Policy, Institutional, and Regulatory Developments

Bangko Sentral ng Pilipinas Issues Central Bank Securities

The BSP started issuing BSP securities on 18 September as an additional instrument to manage liquidity in the financial system. According to the BSP, this initiative will help the central bank shift to more market-based monetary operations and support the implementation of monetary policy under the interest rate corridor framework. The addition of BSP securities to the supply of risk-free financial instruments in the banking system could help in the development of the LCY bond market. The BSP securities will be one of the monetary policy tools to mop up excess liquidity. Initial offerings will be small in volume and have shorter tenors but will eventually be scaled up and have longer maturities. The issuance of the securities is allowed under the New Central Bank Act that was signed in February 2019.

Bangko Sentral ng Pilipinas Approves Provisional Advance to the Government of the Philippines

On 1 October, the BSP approved the Government of the Philippines' request for a provisional advance of PHP540.0 billion to be used for budget deficit financing amid the COVID-19 pandemic. This came after the BTr fully settled the previous PHP300.0 billion repurchase agreement on 29 September. The fresh funds will be settled on or before 29 December and will have zero interest. The new tranche is pursuant to Section 89 of the New Central Bank Act as amended in the Bayanihan II Act, which allows the government to avail of provisional advances from the central bank of up to PHP846.0 billion. Market participants expect the new funds to lift some burden from the government to increase borrowing.