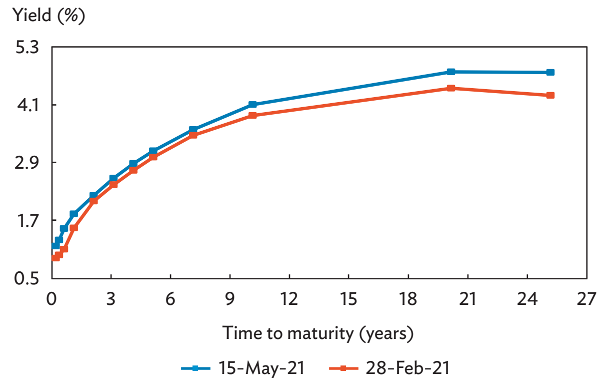
Philippines

Yield Movements

The yields of local currency (LCY) government bonds in the Philippines increased for all tenors between 28 February and 15 May, shifting the yield curve upward (**Figure 1**). Yields of bonds with longer maturities (10–25 years) increased the most with average gains of 35 basis points (bps). Comparable yield increases were seen in 1-month to 1-year bonds, which averaged gains of 32 bps. Smaller increases in yields, averaging 13 bps, were observed for securities with 2-year to 7-year maturities. Across the curve, the yield for 25-year bonds increased the most at 48 bps, while 2-year bonds and 7-year bonds had the smallest gains at 12 bps each. The yield spread between the 2-year and 10-year tenors widened during the review period from 178 bps to 189 bps.

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



Source: Based on data from Bloomberg LP.

The upward movement across the yield curve can be traced to inflation risks as consumer prices are still elevated. The inflation rate in May was 4.5% year-on-year (y-o-y), unchanged from April. The resulting year-to-date average inflation of 4.4% was still above the government's 2021 annual target of 2.0%–4.0%. The implementation of nonmonetary measures by the government, particularly on meat products, aims to temper supply-side inflationary pressure in the coming months. The Bangko Sentral ng Pilipinas (BSP) lowered its 2021 inflation forecast to 3.9% from 4.2%, while it raised its 2022 forecast to 3.0% from 2.8%.

The weak economic performance on the back of subdued economic activity may have also contributed to yield increases. With constrained business operations due to ongoing COVID-19 restrictions, tax revenue has been lower, resulting in expectations that the government will borrow more in the bond market for its funding needs, thus putting upward pressure on yields.

The Philippine economy remained in recession for the 5th straight quarter with GDP contracting 4.2% y-o-y in the first quarter (Q1) of 2021. This was an improvement from the 8.3% y-o-y decline in the fourth quarter (Q4) of 2020, but it was worse compared with the 0.7% y-o-y decline in Q1 2020. All major economic sectors posted declines during the quarter. On the demand side, all components posted declines except for government expenditure, which grew 16.1% y-o-y. Household expenditure, which contributes about 70% to economic output, declined by 4.8% y-o-y. Recent containment measures in Metro Manila and neighboring provinces is expected to weigh down on GDP performance in the second quarter and act as a drag on recovery. The government reduced its GDP growth target to 6.0%–7.0% in 2021 from the earlier target of 6.5%–7.5%.

The uptrend in domestic yields may also have taken its cue from United States (US) Treasuries, whose yields trended upward on the prospects of a strong rebound in the US economy.

The BSP kept its policy rate steady at 2.00% in its monetary policy meeting on 12 May as it expects inflation to decelerate in the second half of 2021 and settle within the target range of 2.0%–4.0%. The central bank also expects the economy to continue to recover in the coming months, and therefore an accommodative stance is needed to sustain traction. The BSP last reduced its key policy rate in November 2020 by 25 bps, which brought the cumulative rate cut in 2020 to 200 bps.

The Philippine peso sustained its strength against the US dollar despite the economy remaining in recession. The domestic currency traded at 47.8 per US dollar on 15 May, appreciating by 1.6% from 28 February. The appreciation of the peso was driven by inflows from overseas remittances and revenues from business process outsourcing. It also reflected lower demand for imports as economic activity remained constrained.

Size and Composition

The Philippine LCY bond market expanded in Q1 2021 by 6.5% quarter-on-quarter (q-o-q) to reach PHP9,122.1 billion (USD187.9 billion) at the end of March (**Table 1**). Quarterly growth accelerated from 5.3% q-o-q in Q4 2020, driven entirely by the government segment as the corporate segment saw contraction during the quarter. On an annual basis, the LCY bond market expanded 28.4% y-o-y. Government bonds accounted for 82.7% of the total bond market at the end of March, while corporate bonds accounted for 17.3%.

Government bonds. Total LCY government bonds outstanding expanded 8.4% q-o-q to PHP7,542.6 billion in Q1 2021, which was faster than the growth of 7.0% q-o-q in the previous quarter. Treasury bills and Treasury bonds primarily drove the increase, as the government continued to heavily borrow from the local market for its COVID-19 relief efforts and to support economic recovery.

Outstanding Treasury bills and Treasury bonds grew 10.5% q-o-q and 7.2% q-o-q, respectively, on the back of higher debt sales during the quarter, which included another tranche of Retail Treasury Bonds (RTBs). Securities from the BSP also contributed considerably to the bond market growth, with its outstanding debt increasing 35.2% q-o-q to reach PHP297.5 billion at the end of March. On the other hand, outstanding debt from government-related entities marginally decreased due to bond maturities and no issuances during the quarter.

Total securities issued by the government in the domestic market increased 55.8% q-o-q to PHP2,082.4 billion in Q1 2021. The substantial growth was supported by higher issuance volumes from both the Bureau of the Treasury (BTr) and the BSP.

Treasury bond sales in Q1 2021 reached PHP613.3 billion, more than triple the amount issued in Q4 2020, lifted by the issuance of RTBs in February amounting to PHP463.3 billion. The 3-year RTB issuance comprises the second-largest debt sale to date following the record PHP516.3 billion RTB issuance in August 2020.

Treasury bill issuance amounted to PHP372.6 billion in Q1 2021 on growth of 28.5% q-o-q, reversing the decline of 28.3% q-o-q in Q4 2020. The jump in issuance was due to higher offer volumes from the BTr during the quarter that were fully awarded. The opening of BTr's tap facility to accommodate the demand led to the higher-than-programmed debt sales.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2020		Q4 2020		Q1 2021		Q1 2020		Q1 2021	
	PHP	USD	PHP	USD	PHP	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**7,106**	**140**	**8,568**	**178**	**9,122**	**188**	**6.9**	**7.9**	**6.5**	**28.4**
Government	5,526	109	6,956	145	7,543	155	7.5	6.2	8.4	36.5
Treasury Bills	557	11	949	20	1,049	22	14.5	(8.4)	10.5	88.5
Treasury Bonds	4,930	97	5,720	119	6,130	126	6.8	8.1	7.2	24.3
Central Bank Securities	0	0	220	5	297	6	–	–	35.2	–
Others	40	1	66	1	66	1	(0.02)	18.3	(0.01)	65.2
Corporate	1,579	31	1,612	34	1,579	33	5.0	14.0	(2.0)	0.01

( ) = negative, – = not applicable, PHP = Philippine peso, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth 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.

The government borrowed more from the market as it ran a budget deficit due to lagging revenue collection and rising expenditure for its COVID-19 pandemic response. On the investor side, the preference for government bonds remained high on the back of the uncertainties brought about by the COVID-19 pandemic. Abundant market liquidity also boosted demand for such safe-haven assets.

The issuance of BSP bills climbed 30.5% q-o-q to PHP1,096.5 billion. The central bank increased its volume offer in Q1 2021 and auctions were all met with good demand except for an auction in February that was undersubscribed. The increase in issued securities during the quarter was indicative of high liquidity in the market.

While government-related entities had no LCY issuance in Q1 2021, the Development Bank of the Philippines returned to the international capital market in March with the sale of a 10-year USD300.0 million bond. The proceeds will be used to refinance its debt of the same tenor that was issued in 2011 and matured on 25 March 2021.

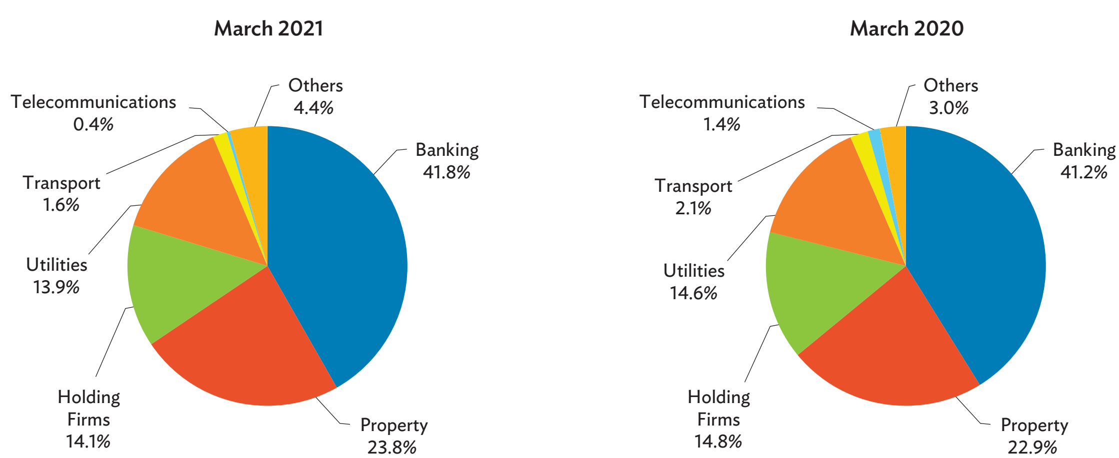
The government plans to borrow PHP3.0 trillion this year to fund its budget deficit. Of which, 85.0% will come from domestic sources and 15.0% from external sources.

Corporate bonds. Debt outstanding in the corporate sector declined by 2.0% q-o-q in Q1 2021 to PHP1,579.4 billion, following a 1.3% q-o-q drop in Q4 2020. The decline can be attributed to the maturation of bonds offsetting the new issuances during the quarter.

The market shares of corporate bond issuers marginally changed in March 2021 from a year earlier. The banking sector continued to hold the largest share of LCY corporate bonds outstanding at the end of March. Its debt comprised 41.8% of total corporate bonds outstanding, slightly up from 41.2% at the end of March 2020 (**Figure 2**). The property sector had the second-largest share of the market at 23.8%. The banking, property, and "other" sectors saw an increase in their respective shares of corporate bonds compared to a year earlier, while the remaining sectors saw their respective shares decline during the review period.

The aggregate debt outstanding of the top 30 corporate issuers amounted to PHP1,414.1 billion at the end of March, comprising 89.5% of the total corporate bond market (**Table 2**). The banking sector held the largest share of outstanding bonds with PHP633.8 billion or 44.8% of the total LCY corporate bond market. This was followed by holdings firms with PHP296.9 billion (21.0%) and property firms with PHP235.4 billion (16.6%). Ayala Land, BDO Unibank, and Metropolitan Bank were the top three issuers at the end of March with debts of over PHP100 billion each.

Figure 2: Local Currency Corporate Bonds Outstanding by Sector



Source: Based on data from Bloomberg LP.

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

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (PHP billion)	LCY Bonds (USD billion)			
1.	Ayala Land	113.9	2.3	No	Yes	Property
2.	BDO Unibank	109.9	2.3	No	Yes	Banking
3.	Metropolitan Bank	102.8	2.1	No	Yes	Banking
4.	SM Prime Holdings	95.7	2.0	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.	Rizal Commercial Banking Corporation	73.1	1.5	No	Yes	Banking
8.	Security Bank	66.3	1.4	No	Yes	Banking
9.	China Bank	61.2	1.3	No	Yes	Banking
10.	San Miguel	60.0	1.2	No	Yes	Holding Firms
11.	SM Investments	58.3	1.2	No	Yes	Holding Firms
12.	Philippine National Bank	52.2	1.1	No	Yes	Banking
13.	Aboitiz Power	48.0	1.0	No	Yes	Electricity, Energy, and Power
14.	Vista Land	43.5	0.9	No	Yes	Property
15.	Petron	42.9	0.9	No	Yes	Electricity, Energy, and Power
16.	Ayala Corporation	40.0	0.8	No	Yes	Holding Firms
17.	Maynilad	28.1	0.6	No	No	Water
18.	Aboitiz Equity Ventures	27.9	0.6	No	Yes	Holding Firms
19.	Filinvest Land	25.8	0.5	No	Yes	Property
20.	Philippine Savings Bank	25.4	0.5	No	Yes	Banking
21.	Robinsons Land	25.2	0.5	No	Yes	Property
22.	Union Bank of the Philippines	24.6	0.5	No	Yes	Banking
23.	San Miguel Brewery	22.0	0.5	No	No	Brewery
24.	East West Banking	16.2	0.3	No	Yes	Banking
25.	Robinsons Bank	16.0	0.3	No	No	Banking
26.	GT Capital	15.1	0.3	No	Yes	Holding Firms
27.	Doubledragon	15.0	0.3	No	Yes	Property
28.	San Miguel Food and Beverage	15.0	0.3	No	Yes	Food and Beverage
29.	Megaworld	12.0	0.2	No	Yes	Property
30.	Puregold	12.0	0.2	No	Yes	Whole and Retail Trading
Total Top 30 LCY Corporate Issuers		**1,414.1**	**29.1**			
Total LCY Corporate Bonds		**1,579.4**	**32.5**			
Top 30 as % of Total LCY Corporate Bonds		**89.5%**	**89.5%**			

LCY = local currency, PHP = Philippine peso, USD = United States dollar.
Notes:
1. Data as of 31 March 2021.
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.

Corporate bond issuance in Q1 2021 slightly declined by 0.2% q-o-q, which was an improvement from the 53.3% q-o-q drop in Q4 2020. Only five firms raised funds during the quarter, issuing a combined PHP58.9 billion worth of bonds. The weak issuance activity from the corporate sector was due to economic and business prospects remaining gloomy amid the ongoing COVID-19 pandemic and a resurgence of cases. These factors led firms to hold off expansion or issuance plans even as interest rates remained low. **Table 3** lists all issuances in Q1 2021, which were led by the banking sector.

Table 3: Notable Local Currency Corporate Bond Issuances in the First Quarter of 2021

Corporate Issuers	Coupon Rate (%)	Issued Amount (PHP billion)
China Bank		
3-year bond	2.50	20.00
Rizal Commercial Banking Corporation		
2-year bond	3.20	13.74
5-year bond	4.18	4.13
SM Prime Holdings		
2-year bond	2.46	7.50
5-year bond	3.85	2.50
Aboitiz Power		
5-year bond	3.82	8.00
Century Properties		
3-year bond	4.85	3.00

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

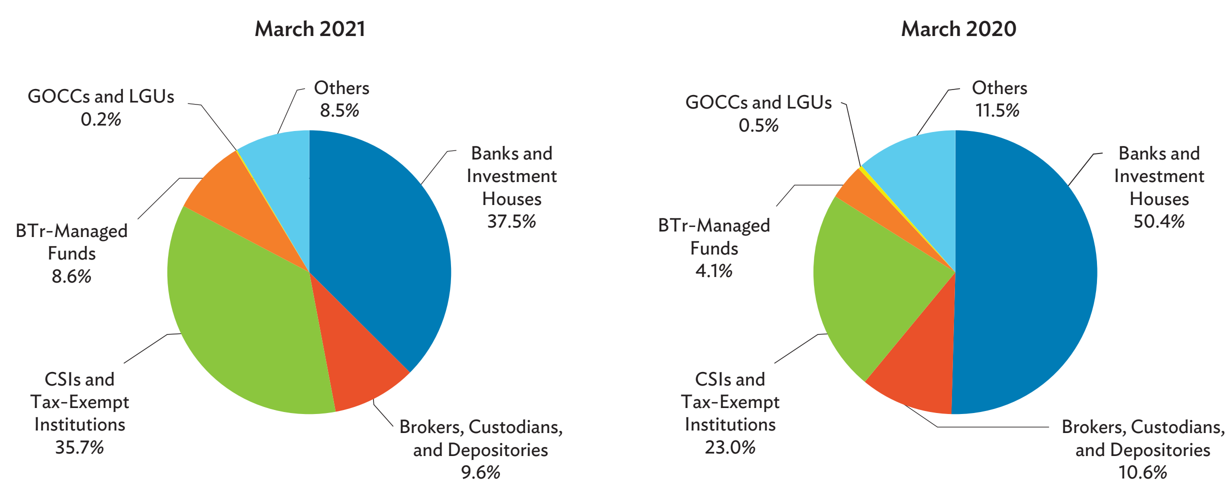
Investor Profile

The investor landscape for LCY government bonds in March was somewhat changed from a year earlier (**Figure 3**). Banks and investment houses, and contractual savings and tax-exempt institutions remained the first- and second-largest holders of LCY government bonds, respectively, at the end of Q1 2021. The market share of banks and investment houses, however, declined to 37.5% from 50.4% during the review period, while that of contractual savings and tax-exempt institutions increased to 35.7% from 23.0%. Government-owned or -controlled corporations and local government units continued to comprise the smallest market share at 0.2%. Changes in ranking based on market shares were seen among the remaining investor groups. Brokers, custodians, and depositories (9.6%) and BTr-managed funds (8.6%) held the third- and fourth-largest market shares, respectively, overtaking "other" investors (8.5%), which dropped to fifth.

Ratings Update

On 10 January, Fitch Ratings affirmed the Philippines' sovereign credit at BBB with a stable outlook. The affirmation was based on the rating agency's assessment that the Philippines had modest government debt levels relative to peers, robust external buffers, and medium-

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.

term growth prospects that remained strong. It also cited risk factors that could negatively affect the credit rating: (i) higher fiscal deficits arising from a reversal of reforms or departure from a prudent macroeconomic policy framework, (ii) failure to return to historically high economic growth rates, and (iii) weakness in external indicators. On the other hand, factors to affect the rating positively include a broadening of the government's revenue base and a strengthening of governance standards.

On 22 April, Rating and Investment Information maintained the Philippines' BBB+ sovereign credit rating with a stable outlook as it expects the economy to recover from the severe contraction, supported primarily by aggressive public investment while accommodative fiscal and monetary policies remain to boost growth. Additional factors cited by the ratings agency that contributed to the affirmation include the government's commitment to maintaining fiscal discipline, the accomplishment of comprehensive tax reforms and various regulatory reforms, the economy's strong external position, and a stable banking sector.

On 27 May, S&P Global Ratings affirmed the Philippines' BBB+ sovereign credit rating with a stable outlook based on the view that the economy will rebound strongly, which will improve the government's fiscal position. Good prospects for the economic recovery are backed by the ongoing vaccine rollout, a strong external account, and fiscal reforms that have made debt manageable. The rating agency noted that it may upgrade the Philippines' credit rating if the economy expands faster than expected and if fiscal consolidation is achieved in the immediate term. Deterioration in these metrics, however, may lead to a downgrade.

Policy, Institutional, and Regulatory Developments

Bangko Sentral ng Pilipinas Increases Net Open Foreign Exchange Limit

In June, the Monetary Board of the BSP approved an increase in the net open foreign exchange position (NOP) limit for banks in response to rising demand for foreign exchange that is underpinned by the increased volume of trade transactions and investments. The NOP limit was raised to either 25% of qualifying capital or USD150 million, whichever is lower. The previous limit was 20% of unimpaired capital or USD50 million. According to the BSP, the increase in the NOP limit is part of a larger set of amendments to the framework for the management of banks' open foreign exchange positions, which aim to make the calculation and measurement of a bank's NOP more risk-based. The amendments will take effect on 1 August 2021.

Bureau of the Treasury Plans to Borrow PHP555 Billion in the Second Quarter of 2021

The BTr is set to borrow PHP555 billion from the domestic debt market in the second quarter of 2021. For April and May, the monthly programmed Treasury bill offerings were PHP100 billion, while Treasury bond offerings were PHP70 billion. In June, the BTr increased its issuance plan by holding more auctions and shifting to a higher offer volume of Treasury bonds. The BTr is seeking to raise PHP215 billion from the market in June, comprising PHP75 billion of Treasury bills and P140 billion of Treasury bonds, through its weekly auctions.