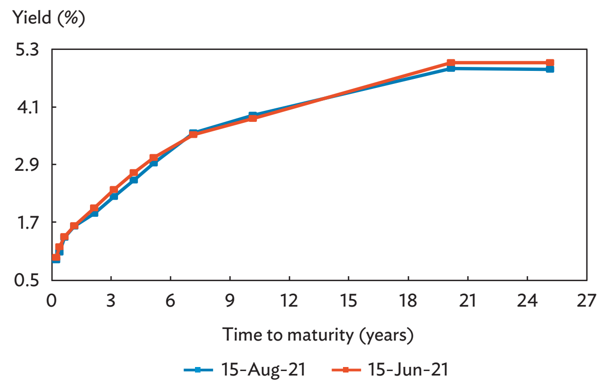
Philippines

Yield Movements

The yields of local currency (LCY) government bonds in the Philippines fell for all tenors between 15 June and 15 August except for bonds with 7-year and 10-year maturities (**Figure 1**). On average, yields dropped 10 basis points (bps) for all bonds that saw declines. The yield on the 1-year tenor had the smallest decrease at 1 bp, while the 4-year tenor had the largest drop at 15 bps. On the other hand, yields on bonds with 7-year and 10-year maturities climbed 4 bps and 7 bps, respectively. The movements caused the yield spread between the 2-year and 10-year tenors to widen during the review period from 184 bps to 202 bps.

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



Source: Based on data from Bloomberg LP.

High liquidity in the market and sustained demand for government bonds, along with recent developments in the economy, prompted the downward movement of yields during the review period.

Inflation concerns had dissipated as consumer prices eased further to a 7-month low in July, falling to 4.0% year-on-year (y-o-y) from 4.1% y-o-y in June. It was the first month in 2021 that the inflation rate fell within the full-year target of the Bangko Sentral ng Pilipinas (BSP) of 2.0%–4.0. Transportation largely contributed to the downward adjustment of overall prices. On the other hand, prices of the heavily weighted food and nonalcoholic beverages group remained elevated. The resulting year-to-date inflation remained above the BSP target at 4.4%. In August, the BSP raised its inflation forecast to 4.1% from 4.0% for 2021 and to 3.1% from 3.0% for 2022. The upward revisions could point to higher bond yields ahead.

The BSP continued its accommodative monetary policy stance, keeping the policy rate steady at 2.00% in its monetary policy meeting on 12 August. The decision came on the back of renewed risk to the ongoing economic recovery amid a rising number of COVID-19 cases. According to the BSP, it will continue to implement monetary policy support as long as necessary for the economic recovery to gain more traction. Meanwhile, while the inflation forecast for 2021 was shifted slightly upward, the risks associated with it were broadly balanced to warrant the current policy setting to remain unchanged. Prior to the policy meeting, the BSP hinted that a lowering of the reserve requirement ratio was possible, which may have also contributed to the downward pressure on yields. This possibility was dismissed later by the BSP, stating that a cut would be untimely.

The reimposition of the strictest mobility controls in early August to curb the spread of the delta variant of the COVID-19 virus threatened recovery prospects, leading to a decline in yields even as gross domestic product (GDP) posted growth in the second quarter (Q2) of 2021. The Philippines ended its recession in Q2 2021 as the economy expanded 11.8% y-o-y during the quarter. The Philippines had experienced 5 consecutive quarters of GDP decline, with the largest contraction (–17.0%) occurring in Q2 2020 at the height of the pandemic and the associated quarantine measures that brought the economy to a standstill. While the double-digit growth was impressive, it is largely a result of a low base effect. On a quarterly basis, GDP contracted 1.3% quarter-on-quarter (q-o-q) in Q2 2021, reflecting the impact of stricter mobility restrictions reimposed in the National Capital Region and surrounding provinces from March through May. GDP in the first half of 2021 expanded 3.7% y-o-y after the negative growth in the first quarter (Q1) of 2021 was revised up to –3.9% y-o-y from –4.2% y-o-y. In August, the government downgraded the growth target for full-year 2021 to 4.0%–5.0% from an earlier target of 6.0%–7.0% in May.

The Philippine peso began weakening against the United States (US) dollar in the middle of June. It traded at PHP50.5 per USD1.0 on 15 August, having lost 5.1% from 15 June. The domestic currency's depreciation was largely due to comments from the US Federal Reserve related to unwinding its loose monetary policy, with hints of tapering to its monthly asset purchases by the end of the year. This was compounded by a flight to safety among investors amid worries over rising COVID-19 cases.

Size and Composition

The Philippine LCY bond market expanded in Q2 2021 by 2.5% q-o-q to reach a size of PHP9,351.0 billion (USD191.6 billion) at the end of June, decelerating from growth of 6.5% q-o-q in Q1 2021 (**Table 1**). The quarterly growth was driven solely by the government segment as the corporate segment contracted during the quarter. On an annual basis, the LCY bond market expanded 25.1% y-o-y. Government bonds accounted for 83.8% of the total bond market at the end of June, while corporate bonds accounted for 16.2%.

Government bonds. Total LCY government bonds outstanding expanded 3.9% q-o-q to PHP7,833.9 billion in Q2 2021, which was slower than the growth of 8.4% q-o-q in the previous quarter. The increase in market size was mainly driven by Treasury bonds and augmented by BSP bills.

Outstanding Treasury bonds amounted to PHP6,351.0 billion in Q2 2021 on growth of 3.6% q-o-q, decelerating from 7.2% q-o-q growth in Q1 2021. The faster growth in the previous quarter was due to the large sale of Retail Treasury Bonds (RTBs), which inflated the market's size in that period. On the other hand, Treasury bills outstanding declined 2.5% q-o-q to PHP1,023.1 billion in Q2 2021 because maturities during the quarter offset new issuances.

Securities issuance from the BSP also contributed to the government bond market's growth, with its outstanding bonds increasing 34.5% q-o-q to reach PHP400 billion at the end of June. Outstanding debt from government-related entities fell 9.1% q-o-q due to bond maturities and the absence of issuance during the quarter.

Total securities issuances from the government segment declined 3.5% q-o-q to PHP2,056.4 billion in Q2 2021. The overall quarterly drop was due to lower Treasury bond issuance during the quarter, which offset the growth in Treasury bills and BSP bills.

Debt raised via Treasury bonds in Q2 2021 amounted to PHP332.0 billion, which was only about half the amount issued in Q1 2021. The quarterly decline was due to a high base in Q1 2021 when PHP463.3 billion in RTBs were issued. Without the RTBs, Treasury bond issuance in Q2 2021 was higher than in Q1 2020 as the Bureau of the Treasury (BTr) increased its borrowing

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q2 2020		Q1 2021		Q2 2021		Q2 2020		Q2 2021	
	PHP	USD	PHP	USD	PHP	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	**7,477**	**150**	**9,122**	**188**	**9,351**	**192**	**5.2**	**11.5**	**2.5**	**25.1**
Government	5,904	119	7,543	155	7,834	160	6.8	11.6	3.9	32.7
Treasury Bills	797	16	1,049	22	1,023	21	43.1	22.1	(2.5)	28.4
Treasury Bonds	5,068	102	6,130	126	6,351	130	2.8	9.8	3.6	25.3
Central Bank Securities	0	0	297	6	400	8	–	–	34.5	–
Others	40	1	66	1	60	1	(0.02)	83.3	(9.1)	50.2
Corporate	1,573	32	1,579	33	1,517	31	(0.4)	11.0	(3.9)	(3.6)

( ) = negative, – = not applicable, PHP = Philippine peso, q-o-q = quarter-on-quarter, Q1 = first quarter, Q2 = second 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.

target of the said securities to PHP280.0 billion in Q2 2021 from PHP180.0 billion in the previous quarter; the programmed issuance was fully awarded. Notably in June, the BTr increased its Treasury bond sales target to PHP140.0 billion, double the monthly target in April and May. The BTr had received a good reception on long tenors in previous auctions as investors sought better yields, thus prompting the adjustment.

Treasury bill issuance amounted to PHP427.4 billion in Q1 2021 on growth of 14.7% q-o-q. The increase was due to larger offer volumes from the BTr during the quarter that were fully awarded, while the opening of the tap facility to accommodate the demand resulted in higher-than-programmed sales of the short-term debt sales.

The government continued to ramp up borrowing from the market to fund its widening budget gap in response to COVID-19 and associated economic recovery plans. Preference for safe-haven assets like government securities remained high on the back of the uncertainties brought about by the pandemic and boosted by abundant market liquidity.

In Q2 2021, the Philippines also tapped the international bond market twice for its fund mobilization. In April, the Philippines successfully returned to the Japanese yen bond market with the issuance of a JPY55.0 billion 3-year, zero-coupon samurai bond. In the same month, the Philippines also issued the largest EUR-denominated bond in a three-tranche sale. A total of EUR2.1 billion was raised, comprising a 4-year bond (EUR650.0 million with a 0.25% coupon), 12-year bond (EUR650.0 billion with a 1.25% coupon), and a 20-year bond (EUR850.0 billion with a 1.75% coupon). The success of the two international debt sales underscored investor confidence in the Philippines' credit soundness.

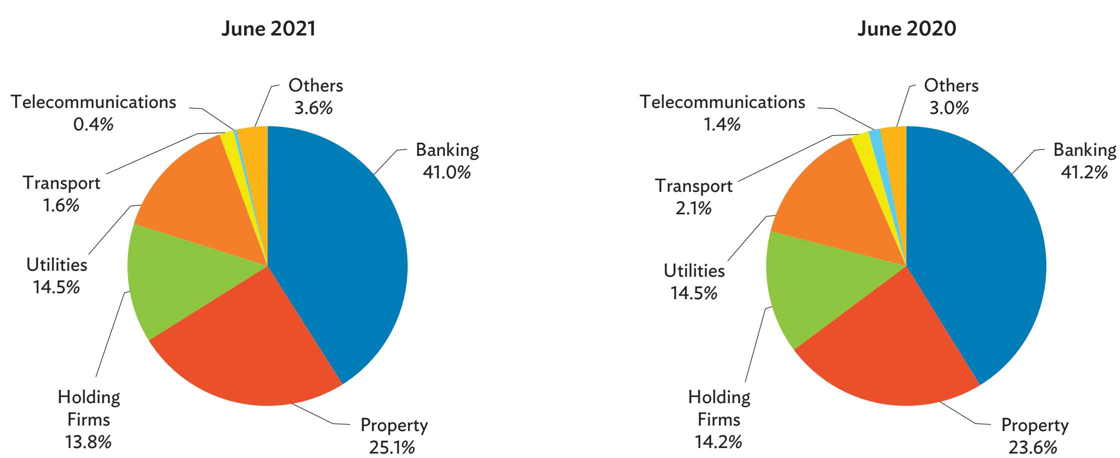
The issuance of BSP bills climbed 14.0% q-o-q to PHP1,250.0 billion in Q2 2021. The central bank increased its volume offer and auctions were all met with strong demand, which was indicative of market liquidity remaining high. There was no securities issuance from government-related entities during the quarter.

The government plans to borrow PHP3.0 trillion this year to fund its budget deficit.

Corporate bonds. Debt outstanding in the corporate sector declined 3.9% q-o-q in Q2 2021 to PHP1,517.1 billion after dropping 2.0% q-o-q in Q1 2021. The decline was underpinned by the maturation of bonds amid low issuance volume during the quarter.

The banking sector remained the largest segment of the LCY corporate bond market with a share of 41.0% at the end of June, which was almost unchanged from the end of June 2020 (**Figure 2**). Property companies and utilities firms remained in the second and third spots, respectively, comprising 25.1% and 14.5% of the market. The former's share increased over the year in review while the latter's was unchanged. The holding firms, transport, and telecommunications sector saw lower shares in June 2021 versus a year earlier, while the share of "others" went up.

Figure 2: Local Currency Corporate Bonds Outstanding by Sector



Source: Based on data from Bloomberg LP.

The aggregate debt outstanding of the top 30 corporate issuers amounted to PHP1,360.6 billion at the end of June, or 89.7% of the total corporate bond market (**Table 2**). The banking sector comprised the largest share at 43.8% (PHP596.4 billion). This was followed by holdings firms and property firms with shares of 20.7% (PHP281.9 billion) and 18.0% (PHP244.7 billion), respectively. Ayala Land, Metropolitan Bank and Trust Co., and BDO Unibank remained the top three issuers with outstanding debt at the end of June of over PHP100 billion each.

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	123.9	2.5	No	Yes	Property
2.	Metropolitan Bank and Trust Co.	121.8	2.5	No	Yes	Banking
3.	BDO Unibank	109.9	2.3	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.	China Bank	61.2	1.3	No	Yes	Banking
8.	San Miguel	60.0	1.2	No	Yes	Holding Firms
9.	Rizal Commercial Banking Corporation	55.1	1.1	No	Yes	Banking
10.	Security Bank	48.3	1.0	No	Yes	Banking
11.	Aboitiz Power	48.0	1.0	No	Yes	Electricity, Energy, and Power
12.	SM Investments	43.3	0.9	No	Yes	Holding Firms
13.	Petron	42.9	0.9	No	Yes	Electricity, Energy, and Power
14.	Vista Land	42.8	0.9	No	Yes	Property
15.	Ayala Corporation	40.0	0.8	No	Yes	Holding Firms
16.	Philippine National Bank	31.8	0.7	No	Yes	Banking
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.	East West Banking	16.2	0.3	No	Yes	Banking
24.	Robinsons Bank	16.0	0.3	No	No	Banking
25.	GT Capital	15.1	0.3	No	Yes	Holding Firms
26.	Doubledragon	15.0	0.3	No	Yes	Property
27.	San Miguel Food and Beverage	15.0	0.3	No	Yes	Food and Beverage
28.	Megaworld	12.0	0.2	No	Yes	Property
29.	Puregold	12.0	0.2	No	Yes	Whole and Retail Trading
30.	MTD Manila Expressway	11.5	0.2	No	No	Infrastructure
Total Top 30 LCY Corporate Issuers		**1,360.6**	**27.9**			
Total LCY Corporate Bonds		**1,517.1**	**31.1**			
Top 30 as % of Total LCY Corporate Bonds		**89.7%**	**89.7%**			

LCY = local currency, PHP = Philippine peso, USD = United States dollar.
Notes:
1. Data as of 30 June 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.

Issuance activity in the corporate sector in Q2 2021 remained weak, declining by 20.2% q-o-q, following a drop of 0.2% q-o-q in the previous quarter. While the number of corporate issuers during the quarter was the same as in Q1 2021, the total volume fell to PHP47.0 billion.

The reduced debt sales from the corporate sector were due to economic prospects remaining gloomy amid a resurgence of COVID-19 cases that negatively affected business and consumer confidence. This prompted firms to hold off on expanding or operating above pre-COVID-19 pandemic levels that would require capital mobilization. **Table 3** lists all issuances in Q2 2021. The majority were 3-year to 5-year tenors, led by Metropolitan Bank and Trust Co. with a PHP19.0 billion single issuance.

While corporate issuance in the domestic market was meek, two firms turned to the international debt market to generate funds. In April, Petron issued USD-denominated perpetual bonds amounting to USD550.0 million with a 5.95% coupon. In June, SMC Global Power raised USD600.0 billion through its perpetual bond issuance denominated in US dollars and carrying a coupon of 5.45%. Proceeds from the international issuances will be used mainly for debt repayment and general corporate purposes.

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

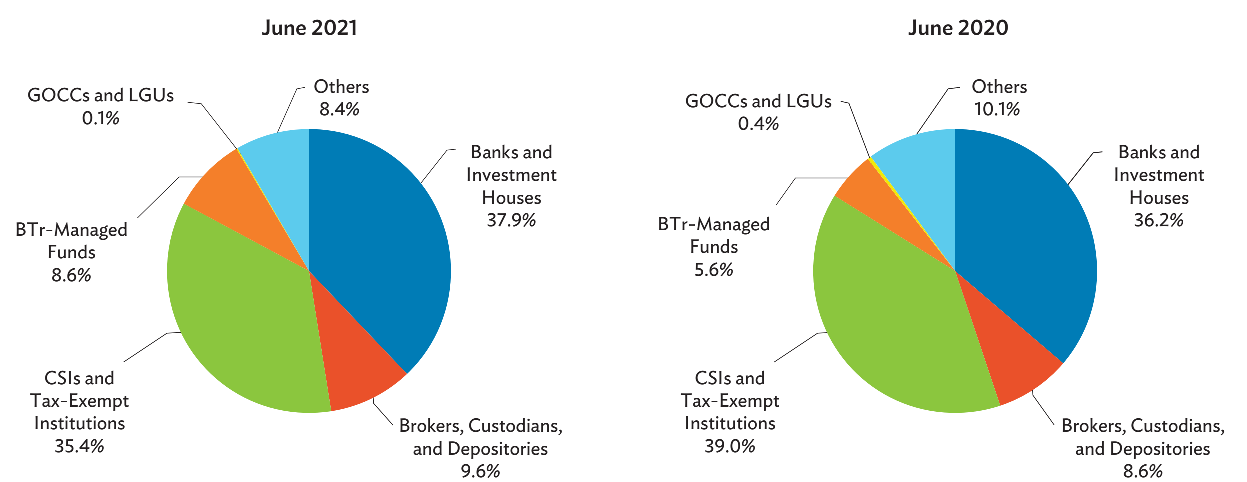
Corporate Issuers	Coupon Rate (%)	Issued Amount (PHP billion)
Metropolitan Bank and Trust Co.		
5-year bond	3.60	19.00
Ayala Land		
4-year bond	3.63	10.00
Ayala Corporation		
3-year bond	3.03	4.00
5-year bond	3.79	6.00
Energy Development Corporation		
3-year bond	2.86	2.50
5-year bond	3.73	2.50
AllHome		
4-year bond	5.00	2.00
Cirtek Holdings		
6-month bond	zero coupon	0.31
1-year bond	zero coupon	0.70

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

Investor Profile

The investor landscape for LCY government bonds in June was changed from a year earlier (**Figure 3**). Banks and investment houses were the largest investor group in LCY government bonds at the end of June, with their

Figure 3: Local Currency Government Bonds Investor Profile



BTr = Bureau of the Treasury, CSI = contractual savings institution, GOCC = government-owned or -controlled corporation, LGU = local government unit.
Source: Bureau of the Treasury.

market share climbing to 37.9% from 36.2% in June 2020. Banks and investment houses overtook contractual savings and tax-exempt institutions as the largest investor group, whose market share declined to 35.4% from 39.0% during the review period. Brokers, custodians, and depositories (9.6%); BTr-managed funds (8.6%); and "other" investor group (8.4%) were the third-, fourth-, and fifth-largest investor groups by market share at the end of June, respectively. Government-owned or -controlled corporations and local government units remained the investor group with the smallest holdings of government bonds, with their share declining to 0.1% from 0.4% during the review period.

Ratings Update

On 12 July, Fitch Ratings affirmed the Philippines' sovereign credit at BBB but revised the outlook to negative from stable. According to the rating agency, the affirmation reflected the economy's strong external buffers and government debt levels remaining below the median of similarly rated peers. The negative outlook reflected risks to the credit profile resulting from the adverse impact of the pandemic to the economy as well as challenges to fiscal consolidation. A rating downgrade remained possible if there were a sustained rise in the debt-to-GDP ratio, weaker medium-term macroeconomic prospects, and a deterioration of external position. On the other hand, enhancements to fiscal finances that would put the debt-to-GDP ratio on a downward trajectory and a strengthening of governance standards could lead to a rating upgrade.

Policy, Institutional, and Regulatory Developments

Bureau of the Treasury Plans to Borrow PHP685 Billion in the Third Quarter of 2021

The BTr planned to borrow PHP235 billion from the domestic debt market in July, comprising of PHP60 billion of Treasury bills and PHP175 billion of Treasury bonds. Less borrowing was set for August at PHP200 billion: PHP60 billion of Treasury bills and PHP140 billion of Treasury bonds. In September, the borrowing plan was set to PHP250 billion, comprising PHP75 billion of Treasury bills and PHP175 billion of Treasury bonds. The borrowing program in Q3 2021, totaling PHP685 billion, upsized the offer volume for longer-tenor securities, as the BTr tried to extend its maturity profile amid strong market liquidity and low interest rates.

Bangko Sentral ng Pilipinas Approves PHP540 Billion Loan to the Central Government

In July, the BSP approved another PHP540 billion short-term loan to the Government of the Philippines. It was the fourth time since March 2020 that the central bank extended credit to the government as a form of assistance to increase funds for the pandemic response. The government had repaid in June the loan drawn from the BSP in January, which amounted to PHP540 billion. The Bayanihan to Recover as One Act (Republic Act No. 11494) allowed direct provisional advances from the central bank of up to PHP850 billion.

Bangko Sentral ng Pilipinas Eases Foreign Exchange Regulations

On 10 August, the BSP amended the foreign exchange (FX) regulations to allow access to FX without prior BSP approval in select trade and nontrade current account transactions. According to the BSP, the amendment will promote ease of use of FX resources of the banking system and further simplify procedures and documentary requirements for FX transactions. These transactions include (i) the sale of FX by banks without prior BSP approval involving payments for e-commerce; living allowance and medical expenses of dependents abroad; and importation of goods with services covered by engineering, procurement, and construction contracts among others; (ii) FX derivatives transactions to be entered into by nonbank government entities; and (iii) use of peso receipts relating to trade transactions to fund the peso deposit accounts of nonresidents. The reform took effect 15 banking days after its publication.