**Philippines Investment Forum**

**Keynote Address**

**by**

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Honorable Mr. Benjamin E. Diokno, Secretary of Budget and Management, Republic of the Philippines, Honorable Mr. Amando M. Tetangco Jr., Governor, Bangko Sentral ng Pilipinas, distinguished guests, ladies and gentlemen: good morning. It is my great pleasure and honor to deliver a keynote address at this important event, alongwith other eminent speakers.

Today I wish to touch upon two key issues: first, the future of the Philippine economy after the realization of ASEAN Economic Community; and second, the roles of multilaterals and the private sector in driving an inclusive economy.

## Philippines Economic Outlook

The Philippine economy has emerged as one of the fastest-growing economies in ASEAN in recent years. Aided by a rising middle class, GDP grew on average 6.2% in 2010-2015, from 4.7% in the 2000s and 3% in the 1990s. In 2016, GDP growth accelerated to 7.0% in the second quarter, bringing the first half growth to 6.9%.

There are two key drivers of the Philippines' rapid growth. The first is investment, both private and public. Investment growth reached 27.7% in the first half of 2016. Private investment sustained brisk expansion while government expenditure accelerated with public construction, rising by 31.6%. Election spending partly lifted growth. The second is household consumption. This has been supported by remittances from Filipino workers overseas, low inflation, and a generally low level of household debts. While remittance growth has been moderate at 3.1% in the first half, remittances remain substantial at an equivalent of 9% of GDP. Increases in local employment—mostly in services and construction—also buoyed spending. Unemployment rate was down to 6.1% in April 2016 from 6.4% in April 2015.

The Government is on track in meeting its full year 2016 growth target of 6% to 7%, underpinned by domestic demand. Growth is seen remaining strong, though the pace could ease in the second half as the impact of election spending wanes, in addition to global economic uncertainties.

Private investment and household spending are expected to expand on positive sentiment from peaceful elections and the new government's pronouncements to enhance policies to lift FDIs, enhance ease of doing business, accelerate PPPs, and address infrastructure bottlenecks. Investment indicators are favorable including an expansion in imports of capital goods (double-digit growth since September 2015), and credits to businesses (~18% higher yoy in May). FDI yielded US$1.3 billion net inflows in the first quarter of 2016, 52% higher than the same period last year, channeled mainly to finance and insurance, construction, tourism, real estate and manufacturing.

However, net external demand was a drag on GDP growth as merchandise exports were sluggish, though partly mitigated by brisk services exports particularly business process outsourcing (BPO). Shipments to its top export markets, Japan (21% share) and the US (16% share) fell in US dollar terms, as also to the other key markets like PRC and EU. In contrast, imports rose sharply on robust domestic investment and consumption. Fortunately, the current account deficit of ~$9 billion (~3% of GDP) remained manageable because of strong inward remittances (at ~$29 million, i.e., 9% of GDP), thus yielding a very stable currency.

**Growth Challenges**

However, the Philippine economy is not without challenges. High rates of poverty and underemployment, and regional growth disparities imply that unless tackled intensively and extensively, growth prospects will soon reach their limits. The national poverty incidence stood at over 26% in the first half of 2015, though much higher in Visayas and Mindanao at 34% and 41%, respectively. There is wide income inequality across regions. Of the 18 regions in the country, just three (Metro Manila and 2 adjacent regions in Luzon) account for nearly two-thirds of GDP.

Another critical constraint to growth is the infrastructure deficit. Infrastructure enables access to education, healthcare, housing, and other social services that allow communities to lift up their standards of living and to stay resilient to external shocks. The quality of infrastructure here significantly lags behind some of the other emerging Southeast Asian countries. In 2015–16, the Philippines was ranked 106th out of 140 countries in terms of infrastructure quality, well below Malaysia (17th), Thailand (61st), and Indonesia (71st).

**ASEAN Economic Communities: Opportunities for the Philippines**

That said, the evolving global economic landscape as well as challenges facing the country offer exceptional opportunities for the Philippines to benefit from seamless economic integration with ASEAN countries in three ways:

(i) Removing trade barriers in sensitive areas;
(ii) Improving domestic regulatory environment; and
(iii) Removing behind-the-border constraints.

The biggest achievement of AEC 2015 is the reduction of tariff barriers. Currently, 70% of intra-ASEAN trade travels at the zero tariff rate. However, trade liberalization remains an unfinished business. Much work still needs to be done to bring down trade barriers in various sensitive areas including trade in services, agriculture, and mining. The Philippines has a competitive advantage in these sectors and thus can tap on further liberalization in services, agriculture, and mining industries under AEC. In addition, increasing trade ties under the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA) will serve as a crucial building block for the next phase of AEC and help position the Philippines as a regional trade hub in these sectors.

The Philippines potentially leverages on AEC regional cooperation for improving institutions and regulatory environment. According to the Global Competitiveness Report, as of 2014, the country was ranked 77$^{th}$ in terms of institutions and behind other emerging Asian countries. Several areas of regulatory coordination can benefit from AEC, especially competition policy and intellectual property rights. Additionally, tax harmonization initiatives under AEC can help the country streamline tax administration to meet the international standards.

Last but not least, AEC, as well as BIMP-EAGA, serve as platforms for tackling behind-the-border constraints including logistics, transport, infrastructure problems, and weak institutions. Regional cooperation helps the Philippines bolster transport and physical connectivity in various areas. These include:

- (i) implementing priority infrastructure projects (PIPs) in the transport sector;
- (ii) increasing private sector leadership in the ICT sector, such as the submarine terrestrial broadband cable connecting Borneo Island and Mindanao; and
- (iii) enhancing the memorandum of understanding in air, sea and land transport, including the implementation of specific ASEAN transport facilitation protocols

**Roles of Multilateral and Private Sector in Inclusive Economy**

**ADB Private Sector Operations and Support for PPPs in the Philippines**

ADB has been an ever-willing partner in promoting the inclusive growth of the Philippine economy. Gross ADB intervention in the Philippines to date is in excess of $18 billion. Private sector is part and parcel of infrastructure development for inclusive growth in the Philippines and, hence, holds the key to addressing the country's infrastructure challenges. ADB has significantly helped the Government accelerate infrastructure projects through private sector operations and support for PPPs in the Philippines since 1986. To date, ADB's cumulative approvals in 39 transactions amounted to $1.0 billion, and I would like to mention three important projects, undertaken here in the Philippines:

In February 2016, ADB supported climate-resilient infrastructure through the issuance of the first Climate Bond in Asia and the Pacific. This facility provided credit-enhancement to the Philippines' AP Renewables Inc. for the Tiwi-Makiling-Banahaw (Tiwi-MakBan) geothermal energy facilities. The Project involves AP Renewables Inc.'s refinancing of capital expenditure -- including acquisition and plant rehabilitation -- and ongoing operations and maintenance at Tiwi-MakBan, the 7th and 4th largest geothermal facilities in the world at two locations on Luzon. The PHP10.7 billion ($225 million equivalent) local currency bond comes in addition to a direct ADB loan of PHP1.8 billion ($37.7 million equivalent). The Climate Bond, which has been certified by the Climate Bonds Initiative, is truly an innovative transaction being the first project bond ever issued in local currency in the power sector in the Philippines. We hope to be able to use this modality more in the future to attract institutional investors to infrastructure, and to provide funding for important infrastructure in both the Philippines and throughout Asia.

In January 2015, a loan of up to $20 million was approved to support the 150 Megawatt Burgos Wind Farm Project in Ilocos Norte. The Project, which started operations in November 2014, is hailed as the largest wind farm in the Philippines and Southeast Asia. The Project contributes to energy security and supports the Philippine government's effort to build up its renewable energy sector. Furthermore, the operation of the wind farm would avoid the production of over 200,000 tonnes carbon dioxide equivalent emissions a year, contributing to improved and a more sustainable environment. It also serves as the main driver for the development of emerging renewable energy technologies in the country, having demonstrated the feasibility of large-scale wind farm projects in the Philippines. Notably, financing of this Project gained international recognition, securing the 2014 Asia Pacific Renewables Deal of the Year Award by Project Finance International; Trade Finance 2014 Deal of the Year Award; 2015 Asia Projects of the Year Award from Power Engineering International; and Best ECA-backed Green Deal Award of Trade and Export Finance.

Lastly, In December 2014, ADB financed the $75 million (P3.375 billion) share of the debt for the expansion and renovation of the Mactan Cebu Airport terminal.

Implemented by the Department of Transportation and Communications, the Project was the first large-scale PPP project awarded under the Aquino government's PPP program. The $766 million (P34.4 billion) project would deliver high-quality airport terminal operations in line with international standards and also provide new commercial facilities. Upon completion in 2019, the new and upgraded terminals are expected to significantly increase passenger traffic with passenger capacities reaching 12.5 million per year. The Project was recognized as the 2015 Transport Deal of the Year by Project Finance International.

Apart from direct private sector operations, ADB works hand in hand with the government to support PPPs through capacity development, the Project Development and Monitoring Facility, transaction advisory services, and policy and regulatory reforms. In 2015, a policy-based operation was approved to:

(i) strengthen viability gap funding mechanism;
(ii) improve project implementation; and
(iii) strengthen legal and regulatory frameworks including amendments to the Build-Operate-Transfer Law.

ADB’s Office of PPP provides transaction advisory to one of the largest PPP projects now being prepared, the North-South Railway Project – South Line. Infrastructure development in the regions, particularly Mindanao, is also a key area of support, of which improvements of about 500-km of roads in the Zamboanga peninsula is under preparation.

ADB aims to further scale up its private sector lending operations in its DMCs.

**Concluding Remarks**

In conclusion, Ladies and Gentlemen, the prospect of the Philippines’ economy is promising and, at the same time, challenging. We meet and brainstorm at an exciting time when the global economic environment is rapidly evolving, and the country is embracing broad-based economic and social reform agendas to tackle a wide spectrum of economic and social issues. A forum such as this one is of great value as it provides an opportunity for the private sector, the Government, and all stakeholders from all over the Philippines, to share experiences, promote best practices, network and learn from each other. This country holds out great potential with its vast assets, most importantly a responsible, educated, English-speaking population with a highly evolved entrepreneurial and services mindset.

In closing, I would like to thank the organizers for inviting me to share insights and experiences on the Philippines.

I wish you all a productive and successful forum.

Thank you.

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