Philequity Corner
By Ignacio B. Gimenez
June 4, 2007

6.9% GDP growth provides second wind to bull market

Just when the market began showing signs of consolidation and correction, a catalyst came about that propelled the PSE Index to a new peak of 3,547.35 and hit an even higher intraday peak of 3,557.48 last Friday. We are referring to the spectacular 6.9% GDP growth which came as a big surprise and exceeded expectations by most analysts.

While many economists were perplexed by the big jump in GDP, the few who paid close attention to what the president earlier stated to the press are reaping the benefits. In a May 17 interview with *The Wall Street Journal*, President Arroyo has indicated a goal of achieving annual economic growth rates of "at least 6.5% to reduce widespread poverty."

The 6.9% GDP growth was greatly appreciated by the market for the following reasons:

- it affirms the general positive direction of the economy, being the highest in 17 years and forms part of a long streak of quarterly growth
- it is broad-based, with strong contribution from services, industry and agriculture
- it was partly fueled by strong government spending

A bone of contention

Now, the last point may be a bone of contention for analysts. For some, this is not a healthy point as it only renders the strong 1Q07 growth as a one-off wonder thereby making the growth unsustainable.

While this may be true for the second quarter given the ban on new construction projects prior to the election, we tend to find it positive.

1. Firstly, we believe that the election is a momentary interruption to public spending. With the lifting of the ban, there should no longer be an impediment to pump-priming activities which the government appears bent on pursuing.
2. Secondly, we have been arguing that that the only way that the country can achieve higher growth rates is if the government leads the way in pump-priming the economy. Government's success in fiscal consolidation will be rendered meaningless if such gains are not channeled back to the economy. Thus, we find the rise in public spending to be a good sign and a positive development.

The need for more inclusive growth

In several past articles (see "*Economic Growth: Antidote to Poverty*," *Philippine Star* Aug. 7, 2006; and "*Investing With Social Relevance*", *Philippine Star* April 23, 2007), we have harped on the need for higher growth rates in order for the economic benefits to trickle down to the poorer segment of our society. After fiscal consolidation, the next phase in our economic story is growth. As such, we welcome any public spending to improve infrastructure in order to spur growth and development in more areas in the country. This will create greater opportunities for business and employment across the country, fueling the higher growth rates that we have been hoping for. Other than infrastructure, we have also encouraged government to spend on education, health and other basic services to improve the lot of more Filipinos. This, to our mind, will eventually render growth to be more inclusive and will ease poverty.

Newton's law

Another reason why we believe that the good performance of the economy and stock market will continue is summarized in our article "*Newton's Law of Inertia as Applied to the Stock Market* (*Philippine Star*, October 30, 2006). Following Newton's law of motion, we argued then that the economy and the market will continue to trend upward unless there are drastic changes in fundamentals and sentiment.

This is what a bull market is all about. In our view, the first phase of the bull market was prompted by the fiscal consolidation which put into motion a virtuous cycle of low interest rates, low inflation, strengthening peso and debt repayment. This also stimulated business for the private sector and created an opportunity for them to strengthen their balance sheets.

The next phase of the bull market will be triggered by economic growth. GDP growth needs to be accelerated, initially catalyzed by government's pump-priming efforts. The increased spending on infrastructure and social services should create more jobs, increase consumption, encourage private sector investments and eventually improve corporate earnings.

On the basis of better economic fundamentals, it is not farfetched that there will be a re-rating on the Philippines and its stock market. As it is, several big investment houses have already significantly upgraded their estimates on the economy. The recent strong economic data is big change from the previous anemic growth rates that the country has been posting. Consequently, we can now be taken out of the list of Asia's laggards.

****

Congratulations to former Albay Rep. and Presidential Chief of Staff Joey Salceda on two points. First, he has just won the gubernatorial race in his province. Second, he has been vindicated by the recent economic data after he has aggressively pushed for the growth phase in the economy.

For comments and inquiries, you can email us at info@philequity.net or at gime10000@yahoo.com.