After the storm

The Philippines copes with catastrophe

- Typhoon Haiyan, one of the worst storms in history, hit the central regions, with the worst damage in Eastern Visayas
- As the Philippines grapples with the terrible human cost, we examine the impact on the economy
- While agriculture has been badly hit, its share of total national production is small; negative supply shocks will likely push headline inflation higher in the coming months

The Philippines is no stranger to natural disasters, as recent events have proved. Less than a month after a 7.2 magnitude earthquake struck the island of Cebu, one of the strongest typhoons in history made landfall on Friday. At the epicentre is Tacloban city in Leyte province, where the storm destroyed homes and crops, and cut power and communication lines. Provincial officials estimate the death toll in Leyte to be around 10,000, with 20,000 homes destroyed. The government and aid agencies are rushing supplies to the area.

While Typhoon Haiyan (called Yolanda in the Philippines) caused great devastation in Leyte province and the surrounding area, the economic impact has been less severe on a national scale. Leyte province is home to 220,000 people and rice and sugarcane are the main crops. Early reports suggest half of the sugarcane production areas, equivalent to 2% of national production, were destroyed. If the island Negros is included, we estimate the loss to be around 3.5% of total production. The Eastern Visayas region, which bore the brunt of the storm, makes up around 2% of the country’s GDP. To put that in a national context, Metro Manila makes up around 35% of national economic output. While the economic impact will be limited, the impact on inflation is likely to be more drastic, with supply shocks pushing up headline inflation in the coming months. We expect inflation to accelerate going into 2014, but it should remain manageable and stay within the central bank’s 3-5% target.

President Benigno Aquino stated that the Philippines has PHP23bn (USD530m) to cope with the aftermath of the typhoon. Natural disasters cost the country between USD1.6bn and USD2.7bn a year, according to some estimates. In the next three years, the government aims to raise infrastructure spending to 5% of GDP from 3%.
Devastated but not destroyed

The government estimates that about 6,000 hectares of sugar area were flattened. The loss of rice production is forecast to be PHP124m, representing 0.01% of annual production. While production and consumption in the region will be reduced in the short term, the drag in the aggregate economy will not be substantial. Chart 2 shows the four major industries in the worst-hit areas of the Leyte province: sugarcane, corn, rice and fishing. Their share of total GDP is small. The sugarcane crop was hit hardest, but the region only contributes 4% to total sugarcane production (Chart 4). We estimate around 3.5% of total sugarcane crop production destroyed (including losses in Negros), equating to around 0.1% of GDP. We expect the total production loss in these four industries to come to around USD324m, or 0.2% of GDP (Charts 2 and 3). Losses extend beyond crops into homes and infrastructure, but even with the 8% loss of output in the region (based on government estimate), the impact will likely be relatively small, around 0.16% of GDP. But the loss could rise to 1.4% of GDP if the entire central areas lose around 8% of output.
The disruption to food and transportation will push headline inflation up in November and December. Inflation accelerated to 2.9% y-o-y in October from 2.7% in September due to higher food prices. Strong domestic demand, driven by higher inflows of remittances and a rebound of production, added another layer of inflationary pressures. The negative supply shocks from the storm, while temporary, will push headline inflation higher. We expect it gradually to accelerate towards year-end and into 2014. But headline inflation should stay on target as global oil prices remain subdued. We expect rates to stay on hold at the December meeting of the central bank; however, we think a hike looks imminent in 2014 in order to temper inflationary pressure and address potential tapering by the US Federal Reserve.

The President stated that there is about PHP23bn (USD530m) that can be galvanised to be spent on the relief efforts, rebuilding of towns and provinces. The sources are: PHP16bn from savings of different agencies, PHP6bn from the president’s social fund and PHP1bn from the calamity fund. According to the President, the primary effort will be building temporary shelters for displaced people, and providing food and medicine.

We expect the Philippines to remain resilient. Even with an adverse supply shock, the central bank has room to keep policy rates accommodative to support growth. Economic growth momentum is unlikely to be dampened by the storm, thanks to stronger economic management and robust demographics. We think remittance inflows and exports will perform well into year-end, cushioning the fall in output from the storm. Fiscal spending will likely increase, but we expect the bulk of the building efforts to be in 2014 once the situation stabilises. But the storm highlights a structural challenge that must be addressed – low investment in infrastructure and inadequate disaster preparedness. Chart 6 shows that the population has increased significantly between 1998 and 2013 from 74m to 98m. However, infrastructure spending as a share of GDP has declined from close to 5.6% to 3%. With strong population growth rates and frequent natural disasters, the Philippines must step up its infrastructure spending. The administration aims to raise spending on public works to 5% by 2016. If it succeeds, the future will look brighter.
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Source: CEIC, HSBC estimates
Disclosure appendix

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