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The Philippines Country Economic Memorandum: Issues in Adjustment and Competitiveness

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Asia Country Department II
Country Operations Division

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CURRENCY EQUIVALENTS

Average 1989	-	US$1.0 = 21.7
	-	P1.0 = 0.046
Average 1988	-	US$1.0 = 21.1
	-	P1.0 = 0.047
Average 1987	-	US$1.0 = 20.6
	-	P1.0 = 0.049
Average 1986	-	US$1.0 = 20.4
	-	P1.0 = 0.049
Average 1985	-	US$1.0 = 18.6
	-	P1.0 = 0.054

ACRONYMS AND ABBREVIATIONS

BIR	=	Board of Internal Revenue
BOI	=	Board of Investments
BOC	=	Bureau of Customs
CBA	=	Collective Bargaining Agreement
CODA	=	Committee on Official Development Assistance
CARP	=	Comprehensive Agrarian Reform Program
CPI	=	Consumer Price Index
DBM	=	Department of Budget and Management
DBP	=	Development Bank of the Philippines
GC	=	Government Corporations
GFI	=	Government Financial Institutions
GSIS	=	Government Service Insurance System
GDP	=	Gross Domestic Project
GNP	=	Gross National Project
GRT	=	Gross Receipts Tax
HICs	=	Highly-indebted Countries
ICC	=	Investments Coordinating Committee
MERALCO	=	Manila Electricity Distributor
NG	=	National Government
NPC	=	National Power Company
OIC	=	Omnibus Investment Code
OPSF	=	Oil Price Stabilization Fund
O&M	=	Operations and Maintenance
PNB	=	Philippine National Bank
QRs	=	Quantitative Restrictions
SSS	=	Social Security System
VAT	=	VAlue Added Tax

PHILIPPINES:

COUNTRY ECONOMIC MEMORANDUM

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PHILIPPINES
COUNTRY DATA SHEET

POPULATION (1989, million)	61224	AREA (sq. km)	300000
GNP p.capita (1989, US$)	705	DENSITY (1989, per sq. km)	204

POPULATION CHARACTERISTICS

Crude birth rate (per 1000)	30
Crude death rate (per 1000)	8

HEALTH

Infant mortality (per 1000 live births)	45
Population per physician	6700
Population per hospital bed	600

INCOME DISTRIBUTION (% of income)

Highest quintile	53
Lowest quintile	5

ACCESS TO SAFE WATER

% of urban population	49
% of rural population	54

NUTRITION

Per capita calorie intake (cal	2372
Per capita protein intake (g/d	54

EDUCATION

Primary school enrollment (gross, % of relevant age group)	106

GROSS DOMESTIC PRODUCT

	US$ mil 1989	% of GDP 1989	annual % change, const. prices 1974-81	1981-88	1989
GDP at market prices	44310	100	6.1	0.7	6.1
Gross domestic investment	8308	19	9.1	-7.4	15.9
Gross national saving	7154	16	8.0	-4.6	3.8
Current account balance	-1465	-3			
Exports of GNFS	10829	24	8.5	6.0	9.9
Imports of GNFS	11983	27	6.1	5.0	26.4

OUTPUT, EMPLOYMENT AND PRODUCTIVITY

	1989 Value Added US$ mil.	% share	1989 Employment mil.	% share	1989 VA per worker US$	% share
Agriculture	10391	23	9854	45	1055	52
Industry	14742	33	3452	16	4270	211
Services	19178	43	8543	39	2245	111
Total	44310	100	21849	100	2028	100

GOVERNMENT FINANCE

	1989 US$ mil	% of GDP	1985 % of GDP
National Government			
Current receipts	7029	15.9	11.3
Current expenditures	6556	14.8	9.1
Current balance	474	1.1	2.5
Capital expenditures	1376	3.1	2.5

MONEY, CREDIT AND PRICES

	1981	1985	1986	1987	1988	1989
		(US$ million, end of period)				
Money supply	2940	1833	2138	2547	2623	n.a.
Credit to public sector	2581	2963	3407	1712	1070	n.a.
Credit to private sector	13291	7547	4936	5769	6482	n.a.
		(% share of GDP)				
Money supply	7.6	5.7	6.9	7.4	7.2	n.a.
Credit to public sector	6.7	9.0	11.1	5.0	2.7	n.a.
Credit to private sector	34.4	22.9	16.0	16.7	16.6	n.a.
		(index number, 1980=100)				
GDP deflator	111.1	238.5	240.7	259.6	285.0	313.8

BALANCE OF PAYMENTS

	1981	1985	1986	1987	1988	1989
			(current US$ million)			
Exports of Goods & NFS	7513	6864	7702	8065	9479	10829
1. Merchandise (FOB)	5722	4629	4842	5720	7074	7821
2. Non-Factor Services	1791	2235	2860	2345	2405	3008
Imports of Goods & NFS	9554	5944	5868	7861	9467	11983
1. Merchandise (FOB)	7946	5111	5044	6737	8159	10419
2. Non-Factor Services	1608	833	824	1124	1308	1564
Resource Balance	-2041	920	1834	204	12	-1154
Net Factor Income	-527	-1317	-1321	-1221	-1210	-1141
(interest payments)	2186	1755	1616	1892	2053	2420
Net Current Transfers	325	172	235	376	500	830
Current Account Balance	-2061	-18	954	-444	-423	-1465
Long-Term Capital Inflow	1503	3094	1249	457	-59	998
1. Direct Investment	172	12	127	307	986	854
2. Net LT Loans (DRS data)	1494	1014	402	-68	71	720
a. Disbursements	2212	1639	1511	1356	1372	1838
b. Repayments	718	626	1110	1424	1301	1118
3. Other LT Inflows (net)	-163	2068	720	218	-1116	-576
Total Other Items (net)	226	-3224	-1072	-281	654	606
Changes in Net Reserves	332	148	-1131	268	-172	-139
Memo:						
Gross Reserves incl. Gold	2725	1098	2611	2312	2169	2350
Exchange rate (P per US$)	8.00	19.00	20.00	20.57	21.10	21.74

MERCHANDISE EXPORTS

	1981	1985	1986	1987	1988	1989
			(current US$ million)			
Coconut oil	533	347	333	381	408	377
Sugar	567	169	87	60	60	89
Logs and lumber	202	130	130	155	157	136
Copper	429	84	90	109	216	237
Manufactures	2406	2765	2969	3642	4338	5192
Other Exports	1585	1134	1234	1373	1895	1790
Total Merch. Exports FOB	5722	4629	4842	5720	7074	7821

EXTERNAL DEBT

	1981	1985	1986	1987	1988	1989
			(current US$ million)			
Stocks						
Public & Publicly Guar. LT	7466	13783	19285	23484	23475	24461
Private Non-Guar. LT	2761	2600	2294	1516	992	874
Total Long-Term DOD	10227	16383	21579	25000	24467	25336
IMF Credit	1133	1168	1266	1260	1093	1219
Short-Term Debt	9521	9092	5486	3792	3888	3797
Total incl. IMF & Net ST	20882	26643	28331	30052	29448	30352
Ratios to exports			(per cent)			
Total LT Debt Service	17.4	19.5	25.5	30.5	26.8	23.7
Total (LT+IMF+ST Int.)	33.5	32.0	34.4	39.0	32.3	29.1

IBRD/IDA LENDING

	1981	1985	1986	1987	1988	1989
			(current US$ million)			
IBRD						
Outstanding and disbursed	1330	2421	3017	3747	3408	3589
Undisbursed	1406	1065	878	805	983	1292
Total incl. undisbursed	2736	3486	3895	4552	4391	4881
IDA						
Outstanding and disbursed	41	84	92	99	102	102
Undisbursed	81	37	23	7	4	0
Total incl. undisbursed	122	121	115	106	106	102

EXECUTIVE SUMMARY

1. This report has two themes. The first is that, despite an impressive recovery from the crises of the mid-1980s, the Philippines economy has not yet attained a sustainable growth path. The need for further macroeconomic adjustment arises for three main reasons: first, because of the effects of rising domestic debt and interest rates; second, because of recent policy slippages, especially with respect to fiscal and exchange rate management; and, third, because of a series of exogenous shocks, including a prolonged drought during the winter and spring of 1989-90, an earthquake in July 1990, and recent turmoil in the Middle East which has raised oil prices substantially. The second theme is that, despite significant structural reform efforts, the country has not yet achieved a level of efficiency that would make it vigorously competitive in the world economy. To achieve this, the Philippines must broaden the scope and deepen the intensity of structural reform efforts.

Key Macroeconomic Issues

Crisis and Adjustment: 1983-88

2. This report is being released at a time of great uncertainty with respect to future oil prices. This uncertainty not withstanding, the Philippines already faced a series of challenges in areas of short term economic management and structural reform, so that the specter of a prolonged oil crisis catches the economy at an awkward moment. Policy makers recognize the urgency of repositioning the economy to be able to weather the oil crisis and to ensure that the economy does not regress to a situation which existed prior to the major stabilization efforts of the mid-1980s. Indeed, in this context, it is worthwhile to briefly review past progress and the details of recent developments.

3. Viewed against the backdrop of the deep recession of 1983-85, the recent achievements of the Philippines economy are very impressive. In 1984, the worst year of the recession, GDP declined by 6%, investment plunged by 43%, the external debt rose by 8% of GNP, and inflation soared to 50%. The recession was especially hard on the poor: a survey of household incomes showed that 59% of Filipino families (about 32 million persons) subsisted on incomes below the poverty line in 1985. During 1986-88, however, the economy recovered across a broad front. GDP and its principal sectoral components grew steadily. Consumption and investment grew strongly and inflation was kept at single-digit levels. The current account deficit, the fiscal deficit and the external debt were reduced relative to earlier levels. Most importantly, poverty was reduced sharply from 59% to 49% of all households; without this improvement, an additional 6 million persons would have joined the ranks of the poor. The recovery, and its consolidation over 1986-88, can be attributed to sound economic management and a bold series of reforms undertaken by Government.

4. Macroeconomic management was distinguished by a prudent fiscal stance, conservative monetary growth, and actions to reduce the external debt. Fiscal discipline, in the form of high revenue growth and low expenditure growth, helped to generate surpluses in the primary balance of the Government, which improved from a 1.5% deficit in 1986 to a 2.1% surplus in 1988. This, together with tight monetary policy, kept inflation at an average of 4.5% over the three years through 1988. Responsible external debt management initiatives, in the form of commercial and Paris Club reschedulings, and debt-equity swaps, postponed the bulk of repayments to after 1992 and retired about $1.6 billion of the debt, contributing to a reduction of the external debt by about 17% of GDP (from about 92% to about 75%) by the end of 1988.

5. These achievements are impressive by themselves, but acquire greater worth in comparative perspective. Among highly-indebted countries, the adjustment performance of the Philippines ranks near the top. Its growth has been relatively high and stable compared to that of such countries as Argentina, Brazil and Mexico, which have experienced multiple episodes of negative growth in the last ten years and at least one in the last three. Its fiscal adjustment has been deeper and more consistent, its inflation lower and less volatile, and its external debt reduction faster.

Macroeconomic Developments in 1989-90

6. Macroeconomic performance since the end of 1988 has been disappointing compared to the achievements of 1986-88. Three inter-related trends--increases in the fiscal deficit, interest rates and the current account deficit -- merit special consideration. The consolidated fiscal deficit rose from 3.1% of GDP in 1988 to 4% in 1989; in the first half of 1990, it was running at almost 5% of GDP. The interest rate on the benchmark financial asset, the Treasury Bill, rose by over 200 basis points (to 9.1%) in real terms during 1989; it has since averaged around 10% in real terms or 23% in nominal terms. The current account deficit rose from 1% of GDP in 1988 to 3.3% in 1989; it has since risen to almost 5% of GDP. These trends have been accompanied by a slowdown in growth, from 6.4% in 1988 to less than 3% in the first half of 1990, and an increase in inflation, from 8.8% in 1988 to around 13% currently.

7. A major source of macroeconomic stress in recent years has been the sharp increase in the domestic debt. Domestic debt rose from 19% of GDP in 1985 to around 24.6% in 1989. This increase was a part of the adjustment strategy followed to facilitate recovery from the recession and payments crisis of 1983-85. Despite significant fiscal adjustment, domestic debt increased since access to external finance was limited, the public revenue system was of low yield, and pressing infrastructure and poverty problems existed which required constant if not rising expenditures. Unfortunately, domestic capital markets have proved too thin to support this strategy: interest rates have risen sharply, creating great fiscal pressure and making macroeconomic management considerably more difficult. An escalating sequence linking rising interest rates to rising fiscal deficits to rising borrowing requirements has been established. This sequence must be broken for the country to return to a sustainable growth path.

8. Recent macroeconomic performance has also been affected by exchange rate developments. During 1989, the real effective exchange rate of the Philippines appreciated relative to key competitors such as Indonesia, Thailand and Malaysia as well as relative to major trading partners such as Japan and the USA. As a result, the current account deficit has been rising as export growth has slowed while import growth has remain remained relatively high. The Philippines also continued to lose market share in the developed countries. The deteriorating current account deficit raised expectations of devaluation which in turn were built into the interest rate structure, thereby aggravating fiscal imbalances. These developments have prompted a more rapid depreciation of the nominal exchange rate in recent months which, if continued and supported with fiscal and wage restraint, should improve external competitiveness.

9. In addition to the effects of the above-noted developments, macroeconomic performance and prospects have been adversely affected by a series of unexpected exogenous shocks. A prolonged drought lasting over the winter and spring months of 1989-90 substantially reduced crop output so that value added in agriculture grew by only 0.17% in the first half of 1990, compared to 4.25% in the first half of 1989. The drought was partly responsible for shortages in power availability which in turn cut growth in industrial output to 3.64% from the 6.86% registered in 1989. As a result, real GDP registered a meager 2.8% growth (compared to 5.8% over the same period in 1989). The prospects for the rest of the year are weak. A strong earthquake in July caused considerable economic damage in Central Luzon. Furthermore, turmoil in the Middle East has caused the price of oil to jump by almost 50%, a development which, if sustained, would cause growth to fall well below 3.5% in 1990.

Causes of Rising Public Debt

10. Since 1985, domestic debt has been issued mostly to finance large public sector borrowing requirements. Foreign reserve accumulation and debt reduction operations have required some domestic debt issuance in various years but such requirements have been minor relative to the needs of the consolidated public sector deficit. Among the principal components of the latter, the deficits of the National Government and of the Central Bank have been major contributors while the deficits of Government Corporations have been of secondary importance.

11. A closer look at the fiscal accounts of the National Government shows that revenues have risen substantially in recent years while non-interest expenditures have been curtailed. For example, total revenues rose from about 11% of GNP in 1985 to around 16% in 1989 while non-interest expenditures rose only modestly from around 11% of GNP to about 12%. The main reason why the deficits of the National Government have persisted despite these improvements is increasing interest payments. Indeed, this is also the main reason why the deficit of the Central Bank, which owes a substantial portion of the public debt, has continued to rise. The increasing bite of interest payments can be judged from the fact that interest payments made by the National Government

and the Central Bank rose from 3.6% of GDP in 1985 to almost 9% in 1989; just the domestic interest payments of the National Government were larger than the consolidated public sector deficit in each of the last three years.

12. Interest payments have increased largely on account of rising domestic interest rates combined with a rising debt stock. Three factors are at the root of the sharp rise in domestic interest rates since 1988. The first and most important factor is the rise in domestic debt. In order to borrow more from the public, the Government has had to offer increasingly more attractive rates. Second, recently rising current account deficits (and an appreciating real effective exchange rate) have raised expectations of peso depreciation and a premium for this has been built into current interest rates. Third, inflationary expectations have risen in the wake of economic and political difficulties since 1988; a premium for this too has entered domestic nominal interest rates. It should also be noted that the domestic capital market is relatively thin: it is dominated by a few large suppliers of credit and by a preference for short-term instruments. In such a context, demand shocks are exaggerated and interest rates tend to rise to higher levels than they would in broader and more competitive markets.

13. The consolidated fiscal deficit has also been affected significantly in 1990 by the operations of the Oil Price Stabilization Fund (OPSF). This fund is designed to buffer the retail price of oil and oil products. Since 1988, the peso price of imported oil has increased substantially because of increases in the world price and the nominal depreciation of the peso. Government chose not to pass along most of this increase to end-users. As a result, the OPSF has gone into a substantial deficit (about 10.7 billion pesos by end-June), which will have to be made up by additional budgetary allocations. The Government has since announced its commitment to maintain the OPSF in flow equilibrium and has increased the price of oil products by about 30% in September. While this increase brought the domestic oil prices in line with international prices as of end-August, further adjustment will be necessary given the current trends in international oil prices.

Consequences of Rising Public Debt

14. The main problem posed by current trends in domestic debt and interest rates is that they make the objective of high growth difficult to achieve. This can be illustrated by reference to two types of "crowding out" that occur with high and rising interest rates. One type consists of the crowding out of certain types of expenditures from the budget, while the other consists of crowding out of the private sector in the market for funds. Both types make it more difficult to achieve higher growth. For example, the prospects for higher growth are adversely affected when higher interest payments reduce the budgetary resources available for necessary infrastructure investments. Similarly, high interest rates discourage private investment, again entailing a loss of growth potential. This is a serious problem for the Philippines. Operating and maintenance expenditures and infrastructure capital outlays are barely above those of 1980 in real terms: the cost in terms of inadequate and decaying infrastructure is quite evident.

15. An associated problem is that the objective of improving income distribution and reducing poverty is also made more difficult to achieve. A rising share of interest payments in the budget typically reduces the share available for social expenditures which benefit the poor. In addition, if the higher financing needs of the public sector are satisfied through higher levels of indirect taxes, as is often the case, lower income groups may be affected disproportionately since they pay a larger share of their income as indirect taxes. Finally, to the extent that the best chance for escaping poverty is offered by economic growth, the reduction of growth potential through reduced public and private investments in productive capacity makes it more difficult to achieve poverty reduction.

Government's Revised Adjustment Program

16. The rising public debt poses a risk to the economy and a challenge to Government. At present trends, the consolidated fiscal deficit could rise to over 5% of GDP in 1990 and higher levels thereafter. A deficit sustained at this level would have a substantial upward effect on domestic real interest rates and would rapidly become untenable. Furthermore, as already noted above, the effects of even higher interest rates would be extremely adverse for growth, investment, inflation, and the management of the fiscal and external accounts. Under the circumstances, further fiscal adjustment merits top priority. Recognizing the gravity of the problem, Government has recently proposed a set of measures designed to reduce the consolidated public sector deficit by (a) raising revenues (b) reducing expenditures and (c) reducing interest rates.

17. Revenue Raising Measures. In mid-1990 the Government has proposed measures to raise both tax and non-tax revenues. Among the tax raising measures are: (i) increases in excise taxes on "sin" products (e.g. tobacco and alcohol) as well as soft drinks; (ii) increases in taxes on real estate transfers, business registration, and purchases of luxury items; (iii) increases in the business income tax rate and (iv) increases in forestry charges and other fees and charges of selected government agencies. Of these measures, the increase in excise taxes on tobacco and alcoholic beverages and in certain fees and charges have already been enacted into law. However, even if the full range of measures were passed by Congress, the revenue gain would approximately offset the loss from the change in the tax regime on oil products. Therefore, in light of recent events, additional significant tax generating vehicles will have to be found. It is to be hoped that revenues will be increased also through a vigorous effort to improve tax collections.

18. Among non-tax revenue measures are (i) an increase in dividend remittances from public corporations and (ii) an acceleration of the privatization program. As far as the latter is concerned, it is expected that strenuous efforts will be made to meet the 1990 target of offering for sale 50% of the total assets identified for privatization. Among these would be part of the assets of the Development Bank of the Philippines (DBP), Philippine National Bank (PNB), Republic Bank and Union Bank. For DBP the program calls for selling off regional operations to the private sector while, for PNB, the program calls for further sale of shares to the public, following

the hugely successful divestment of 30% of shares in 1989. Government hopes to raise an additional 6.5 billion pesos (or about 4% of 1989 revenues) from such operations in 1990. Given that past attempts to privatize have been characterized by slow progress due to legal, technical and bureaucratic difficulties, and given the difficulty of selling such assets in a high-interest rate environment, this target appears unrealistically high. Nevertheless, the principle of accelerating the privatization program is to be strongly endorsed and it is to be hoped that Government will take steps to minimize obstacles to successful implementation in this regard.

19. Reducing Expenditures. The program for reducing expenditures involves cuts in administrative expenses, personnel hiring freezes in most departments (except education, health and revenue collection), a wage and salary freeze for the public sector in 1990 and an 8% cap on increases in the wage bill in 1991 and 1992, and a substantial reduction of capital outlays under the Comprehensive Agrarian Reform Program (CARP). While these measures will cut current spending, other measures have been proposed that will substantially reduce future spending obligations of Government. Of these, potentially the most important is a decision to eliminate the Oil Price Stabilization Fund (OPSF) and to deregulate oil prices. The OPSF has been a major drain on the budget in 1989 and 1990, and while its current deficits will be met by additional appropriations, no further deficits will be permitted to accumulate after July, 1990. Another such measure is a decision to eliminate the fuel oil subsidy provided to the National Power Corporation. The expenditure reduction program currently envisaged is balanced in the sense that it seeks to reduce current as well as capital expenditures, and among the latter, it seeks to curtail a program that is presently overfinanced. This aspect merits support. In addition, it is to be hoped that the deregulation program with respect to oil prices and the OPSF will be implemented as soon as practicable.

20. Interest Rate Reduction Measures. Government intends to follow a two-pronged approach in order to get interest rates down. One prong is sound macroeconomic management featuring the reduction of the deficit and of inflation, as well as the adoption of a more competitive exchange rate policy. The other prong consists of more direct measures to reduce interest rates focussing on the reduction of financial intermediation taxes and increasing competition in the T-Bill auction system. Thus, the gross receipts tax (GRT) and the withholding tax on interbank deposits are both to be eliminated and reserve requirements are to be reduced as soon as monetary conditions are appropriate. While the reduction of financial intermediation taxes will have an adverse impact on fiscal revenues, this is expected to be offset by the positive fiscal impact of reduced interest rates and the longer run impact of a broader and deeper financial system.

21. Competition in the T-Bill market is to be increased through the expansion of the dealers network involved in the primary auction of Government securities and through greater involvement of the two large (public) insurance organizations, the Social Security System (SSS) and the Government Service Insurance System (GSIS), in the T-Bill market. There certainly is scope for further competition in the T-Bill market. Indeed, after the SSS and GSIS were permitted to place orders through primary dealers recently, T-Bill rates

softened considerably over a period of a few weeks. However, it should be noted that these two institutions have tax-exempt status; as a result, there is some foregone revenue for the Treasury in the case of T-bill sales to them.

22. In addition to improving auction procedures, Government should consider making T-Bills attractive to a wider group of investors, including small investors. A wider and deeper pool of potential investors would help reduce interest rates as well as lengthen maturities. One way to increase the access of smaller private investors is to further encourage the formation of mutual funds or unit trust accounts which invest exclusively in Government securities. This would ensure that small savers have better access to this market, without the administrative complexity of issuing small denomination T-bill series.

23. The objective of securing a larger market for T-bills might also be met through issuing dollar-denominated bills or peso bills with a rate indexed to the peso-dollar exchange rate. Government has recently experimented with such an approach and the initial response has been favorable. This is not surprising since this approach removes the exchange rate and inflation risk for investors and thereby helps attract more investors, secure a lower interest rate and enable the flotation of longer term instruments. It should be emphasized, however, that effective use of foreign-exchange-linked securities requires the maintenance of the exchange rate at a level consistent with medium-run balance of payments equilibrium.

Issues in Efficiency and Competitiveness

24. The last few years have been marked by bold reforms to reduce distortions in commodity and factor markets, to rationalize the role of the public sector and to maintain market orientation in general. Distortions have been reduced through the abolition of monopolistic marketing arrangements for sugar and coconut products, the removal of price controls and export taxes on several agricultural products, and the reduction of trade restrictions on a wide variety of inputs important for local industry. The role of the public sector has been rationalized through the restructuring and downsizing of the two largest Government financial institutions, the reorientation of the public investment program to focus on essential infrastructure, and the establishment of a program to improve the performance of public corporations and to privatize a selected set. Market orientation has been maintained in the setting of interest rates, credit allocation, exchange rates and the prices of most commodities.

25. Despite these creditable efforts, the Philippines has not yet achieved levels of efficiency that would make it vigorously competitive in world markets. Indeed, its share of exports to developed country markets has continued to decline and the productivity gap between it and its competitors has continued to widen. While these developments are undoubtedly influenced by macroeconomic considerations, especially exchange rate policy, they are also affected by the scope of structural reforms in comparative perspective. For better or worse, the Philippines is part of a global economy and its

fortunes depend not only on its own actions but also on those of other countries. Since many other countries have undertaken structural reforms in the 1980s, the Philippines must continue to restructure its economy at a speed and with a thoroughness that will enable it not only to improve efficiency for its own sake but to lessen the economic distance between it and its competitors.

26. The issue of economic efficiency is especially important for the Philippines at this juncture. To begin with, increased efficiency would permit more growth from available resources. This would help the country avoid excessive additions to the public debt which, as noted earlier, is a major source of recent and prospective macroeconomic problems. In the longer run, increased efficiency would result in higher levels of economic activity arising from an improved environment for the private sector. This would generate higher public revenues which would also facilitate the task of macroeconomic management. Finally, increased efficiency would help the Philippines maintain competitiveness in external markets. This is particularly important not only for balance of payments and external debt servicing considerations but also because a lack of competitiveness in the export sector (which is relatively labor-intensive and rural-based) is especially damaging to the poor.

27. The efficiency and competitiveness of the economy would be enhanced if measures were undertaken to render the trade regime more open, investment incentives more effective, financial intermediation less costly, the public sector more efficient and less pervasive in the marketplace, and infrastructure services (especially power and transportation) more reliable and less costly. Progress in each of these areas is described below and suggestions for further reforms are noted.

Trade Reforms

28. Recent Progress. The Philippines has undertaken significant trade reform since 1980. While nominal tariff rates have declined modestly from around 31% in 1982 to around 28% currently, effective rates of protection have declined substantially on account of the progressive removal of quantitative restrictions. The proportion of items subject to import restrictions declined from 36% of all importables in 1980 to just over 10% in 1989. Much of this import liberalization occurred in the last three years. Nevertheless, the Philippines' competitive position in world markets has not improved. This is largely because its principal competitors have maintained even more open economies. For example, Malaysia and Thailand both have import liberalization ratios of greater than 95% compared to 90% for the Philippines, and Malaysia and Indonesia have lower average tariffs.

29. Further Measures. Further trade reforms are necessary not only to improve resource allocation, but also to improve relative competitiveness. In terms of priorities, the most important measure would be the elimination of the remaining quantitative restrictions as soon as possible. If existing quantitative restrictions are replaced by initially high but progressively declining tariffs, there will be a positive fiscal effect as well. A second

priority would be measures to reduce the level and dispersion of tariff rates. Such measures would reduce the bias that still exists against exportables and agriculture and result in improvements in efficiency as well as equity since these sectors are labor-intensive. In this regard, recent proposals made by Government to reduce quantitative restrictions and reform the tariff schedule are steps in the right direction and need to be pursued vigorously.

Investment Incentives

30. Government has attempted to influence the size, location, composition and competitiveness of Philippine industry through a variety of industrial policy measures, ranging from fiscal incentives to capacity regulations. The major vehicle of industrial promotion has been the Omnibus Investment Code (OIC) adopted in 1987 and administered by the Board of Investments (BOI). However, while private investment has risen significantly in recent years, it is generally felt that this has had less to do with the incentives system than with the general economic recovery. As far as the incentives system is concerned, several concerns exist. Among these are (i) that the BOI should be more of a promotional body than a regulatory body; (ii) that the current regulations governing foreign investment are too restrictive and (iii) that Government's export promotion effort could be stronger.

31. The Role of the BOI. With regard to the BOI's role, concerns exist to the effect that the procedures involved in obtaining approval and incentives are cumbersome and result in significant delays for project start-up and that the system of granting incentives is characterized by excessive discretionary authority for the BOI and by lack of transparency. It has been proposed that the regulatory powers of the BOI be reduced and the institution be reoriented to focus primarily on promotional aspects. This could be achieved by reducing the discretionary power of the BOI over the award of incentives and by making such incentives transparent and automatic.

32. Foreign Investment. While the general type and level of incentives offered to foreign investment in the Philippines is comparable with that available in most ASEAN countries, it is arguable that the Philippines is in comparatively greater need of foreign investment. In addition to ensuring a stable and receptive political environment, Government should consider two economic measures which would significantly increase investor interest. The first measure would be to significantly reduce the number of business categories in which foreign investment is prohibited, that is, introduce a short "negative" list. A second significant inducement for foreign investors would be the re-opening of debt-equity swap facilities; the availability of such facilities was responsible for much of the increase in foreign investment observed in 1988 and 1989.

33. Export Promotion. The export performance of the Philippines has improved in recent years. Nevertheless, it has not been as strong as that of several competitor countries (e.g. Thailand and Malaysia) and not strong enough to reduce the current account deficit. In this regard, three sets of direct export promoting measures should be considered: (i) providing incentives (such as duty drawbacks) to a wider range of exporters, including

indirect exporters as well as those who export a small proportion of their total production; (ii) improving export financing facilities by introducing foreign currency loan schemes to finance imported inputs, a domestic letter-of-credit system for the domestic purchases of exporters, and a greatly expanded preshipment guarantee facility for export loans; (iii) improving the export policy and program coordination effort through the establishment of a trade promotion organization and strengthening of key Government agencies. It should be noted, however, that such promotional efforts are unlikely to be effective unless they are accompanied by a competitive exchange rate policy and a more open and less regulated trade and industrial environment.

Costs of Financial Intermediation

34. The costs of financial intermediation are high in the Philippines for reasons related to Government policy and financial market structure. Government policy features relatively high taxes on financial intermediation. The four main taxes are the gross receipts tax, the interbank withholding tax, and the taxes implied by credit allocation (to agrarian reform beneficiaries and/or the agricultural sector) and reserve requirements. These taxes account for about 3 percentage points of the nominal lending rate currently. In addition, operating margins and profits are relatively high in the Philippines, in part because a few large institutions dominate the financial sector to which entry has been restricted over the last twenty years.

35. Reducing Financial Taxes. The Bank has drawn attention to the problems of the Philippines financial sector previously and has encouraged reforms with the support of a sector adjustment loan. Among the reforms suggested are measures to reduce intermediation costs, to increase competition and to strengthen supervision and regulation of commercial banks. The Bank has recommended that intermediation costs be reduced by the elimination of the Gross Receipts Tax and the withholding tax on interbank deposits, and the abolition of the agri-agra requirement. Recently, Government has indicated that it may be able to eliminate the two taxes by the end of the year and to modify the agri-agra requirement so that it does not impose as heavy a burden to banks as it has till now. A far more important tax, however, is that implied by high reserve requirements. These cannot be reduced until monetary conditions are appropriate in the sense that inflation and inflationary expectations have been lowered.

36. Increasing Competition. Competition in the banking system is to be enhanced through a more flexible approach to bank and branch licensing. Recently, the Central bank issued a circular announcing that there was no moratorium on either the formation of new banks or the spread of branches. In practice, however, there has been little progress on this front. The system of approving branch applications relies too heavily on regulatory notions of branch-sufficiency in a given area and does not take adequate account of the benefits of branch competition. Most profitable geographical business areas are presently considered overbranched and applications for licenses are normally turned down. Similarly, despite several applications, only two commercial bank licenses have been granted in the last twenty years, both in recent months. While Government is understandably concerned about the

soundness of banks and the safety of the financial system, its approach has been over-cautious. A more appropriate stance would be to maintain a strict regulatory environment and relatively high capital-asset requirements for bank licensing, but to leave decisions regarding the opening of a bank or the location of a branch to entrepreneurs. Finally, competition in the banking sector would be enhanced by a more open approach to the licensing of foreign banks and to their operational scope.

Rationalization of Public Sector

37. The growth of public assets in the Philippines came about from two sources: "statism" in the 1970s which led to the establishment of a large number of public enterprises in many different economic sectors, and the acquisition of non-performing assets from government financial institutions following widespread business failures and defaults in the 1983-85 economic crisis. The rationalization program introduced by the Aquino Administration had the following main features: all acquired non-performing assets were to be sold to the private sector while, from among existing public enterprises, some were to be privatized and others to be abolished, consolidated, or merged as appeared necessary following a review of their role in the economy.

38. Progress in Privatization. The rationalization program has been relatively successful in disposing of acquired assets but less so in privatizing public enterprises. Privatization has been dogged by legal, technical and bureaucratic problems and the bulk of the program remains to be implemented. The budgetary impact of the program has so far been modest in that sales of assets have yielded meager revenues; however, potential savings have undoubtedly been gained since the sold corporations are no longer drawing expenses or subsidies from Government.

39. Proposed Measures. In the current context of pressing fiscal need privatization could play a very important role not only by providing some cash up front to the Government but also by stopping the drain on fiscal resources entailed by many public corporations. Towards this end Government has recently made the following proposals: to accelerate its privatization program, to reduce tax exemptions and subsidies presently enjoyed by some public corporations, and to reduce the deficits of public corporations through better management.

40. Under the accelerated privatization program it is envisaged that 50% of the total assets marked for privatization will be offered for sale by the end of 1990. It is expected that several government financial institutions will also be partially or fully divested. In particular, it is expected that there will be a further divestment of PNB as well as public offerings of the stocks of Republic Bank and Union Bank. It should be noted that the privatization program is unlikely to yield presently anticipated revenues if the current regime of high interest rates continues. In such an environment, financial assets are typically more attractive to investors than physical assets and Government will find it difficult to privatize unless it reduces the asking price substantially.

41. As far as budgetary support of public corporations are concerned, there has been significant progress under the present Government. Since 1986-87, most tax exemptions have been eliminated, the level of capital equity infusion reduced significantly, and public corporations have been made to pay market interest rates on their borrowings from the Government. However, some public corporations still enjoy tax exemptions and subsidies on the grounds that they provide goods or services of considerable social merit. Given current fiscal pressures, it would be advisable to carefully review the justification of these exemptions to see if further pruning is possible.

42. Government has taken steps to improve the management of public corporations by introducing a number of innovations such as monitoring, corporate planning and performance evaluation systems. Such systems were implemented in four public corporations in 1989 and it is expected that they will be extended to several others by the end of the year. Together with these measures, it will be important to continue to improve the internal cash generation of all corporations and especially of the major public utilities by raising user charges in line with costs and by resolving delinquent accounts speedily. The deficits of public corporations are substantially affected by their investment plans; given the current fiscal situation, it may be necessary to re-examine investment plans with a view to postponing, rephasing, or abandoning selected investments in support of fiscal adjustment.

Infrastructure Issues

43. Power. The main infrastructure issues which affect efficiency and competitiveness in the Philippines relate to the reliability of electric power and the adequacy and cost of transportation. The power sector was severely affected by the investment cuts of the macroeconomic stabilization program of the mid-1980s. Periodic shutoffs of power became a major problem in 1989 and 1990 as rapidly rising demand (based on the economic recovery experienced since 1986) outstripped slowly rising supply. Supply has risen slowly partly because of the lack of investments in power generation capacity and partly because of implementation problems with respect to the commissioning of combustion turbines which were supposed to fill the gap until longer-gestation generation plants came on line. Power outages became frequent in the first half of 1990 as a drought reduced hydroelectric production and several old power plants broke down under the pressure of constant operation.

44. The present power program of the Government relies on the use of combustion turbines to cope with short to medium run needs and the operation of new power plants (largely based on geothermal sources) from 1993 on to cope with demand over the long run. Until 1993, therefore, the cost of power will rise in the Philippines because incremental demand will be met from the most expensive source, oil-based combustion turbines; if recent increases in the price of oil are sustained, the outlook for cost will be even bleaker.

45. Transportation. Over time, a number of contradictory, discriminatory and anti-competition regulations have accumulated in the transport sector (mostly interisland shipping and road transport) that by now impede rather than enhance the growth of the sector as well as that of the economy

(especially through facilitating exports). Among the most damaging regulations are the franchising requirements for passenger and freight services, measured capacity criteria to control entry into the industry, restrictions on imports of transport equipment and spare parts, and fare controls. All these restrictions have made the transport industry relatively unattractive for existing as well as potential investors and have resulted in an industry characterized by high costs, low profits, and deteriorating fleets. Moreover, there is no reason to believe that these restrictions have achieved benefits in terms of safety or service.

46. Transport is a vital sector for the Philippines. Road and ship transport affects a vast spectrum of Philippine industry and transportation costs affect production costs significantly. Given that transport is potentially a competitive industry, there is little justification for the sort of entry, route and fare regulations that presently exist. The most important step that Government could take towards improving transportation would be to deregulate entry, routes and rates in both the interisland shipping and the road transport industry and to facilitate fleet modernization and expansion through the lifting of import restrictions on equipment and spare parts. Import restrictions should be lifted since there is little hope of meeting requirements in a timely and cost-effective fashion through reliance on domestic production. Regulatory attention should be diverted to safety considerations.

Private Sector Concerns

47. One of the principal objectives of the Philippines Medium Term Development Plan is to promote the role of the private sector in the future development of the economy. In order to do so, however, a facilitating environment must be created, an environment distinguished by minimum regulatory intervention and maximum infrastructure and policy support. This report has argued that, while Government has moved in the right direction, such an environment is not yet in place. A sub-theme running through this report is that the Philippines is a "high-cost" economy from the private sector point of view. Interest costs are high because of the pressure of the fiscal deficit on the one hand and the structure of the financial sector on the other. Energy costs are high because of dependence on imported oil, a dependence that has recently grown as new investments based on local energy sources have not yet come on stream. Transportation costs are high because of regulations affecting interisland shipping and road transport, as well as lack of adequate expenditures on infrastructure maintenance. Labor costs are effectively high because low real wages are offset by low productivity. The costs of doing business are also affected by the maintenance of an industrial regulatory system that limits competition in certain sectors and is ambivalent towards foreign investment in particular. All these considerations restrict the scope for the private sector to perform at potential. Under the circumstances, a strengthening of the ongoing reform process is called for in order to create an environment within which the potential of the private sector can be effectively harnessed for national economic development.

Projections and Financing Requirements

48. This report has argued that the Philippines needs to direct its future economic strategy to restoring macroeconomic balance through substantial fiscal adjustment as well as to enhancing economic efficiency through further structural reforms. The implications of such a strategy are examined in this report through a consistency framework, not a predictive model. The scenarios presented in the report are not meant to represent complete stabilization package, but rather to illustrate how the burden imposed on the economy by the growing domestic debt can be contained and even reduced. Three results merit special comment. First, a substantial macroeconomic adjustment is necessary in order to maintain even a modest growth rate in the next few years. Second, this growth can be increased by undertaking structural reform efforts along the lines discussed in this report and by further strengthening the fiscal effort. Third, the rise in oil prices, if sustained, will cause a sizeable financing gap to emerge as early as in 1990, despite steady increases in the assumed level of official aid disbursements.

49. The results indicate that the following would be required, at a minimum, to decelerate the growth of domestic public debt and reduce the pressure on interest rates and inflation: (i) a strong tax and privatization effort, yielding additional revenues of around 3% of GDP; (ii) restraint on current expenditures, leading--together with the revenue effort--to an increase in public savings of 3% of GDP between 1989 and 1995; and (iii) sufficient expansion of capital expenditure, from 4% to about 6% of GDP, to support necessary investment in infrastructure, in particular in power generation and in areas damaged by the earthquake. In order to sustain GDP growth of about 5% per year, this fiscal effort needs to be complemented by restoration of international competitiveness lost in 1988 and 1989, improvement of the regulatory framework for investment, and continuing efforts to reduce the foreign debt overhang through market-based mechanisms such as debt equity conversions.

50. The strategy described above is expected to lead, after 1992, to a stabilization of the ratio of domestic public debt to GDP. In addition, it could sustain GDP growth averaging 5.3% in 1992-1998 and per capita consumption growth of 2%, after a substantial deceleration in 1990-91 as a result of the oil shock. The growth rates, in real terms, of both imports and exports are expected to decline, from the very high levels of the most recent years, to average 8% for imports and 9% for exports; as a result, the non-interest current account surplus increases steadily after 1991.

51. In the enhanced policy scenario the growth rate could be increased by at least 1% per annum by undertaking a strong structural reform program in addition to intensifying the aforementioned adjustment effort. The structural reform program should include substantial progress in financial deepening and trade liberalization. While the adjustment-only scenario implies growth of around 5.3% per annum after 1992, the adjustment plus structural reform scenario supports GDP growth of 6.3%. Under present circumstances in the Philippines, with poverty being a large and persistent problem, every effort should be made to achieve the higher growth path as this hastens the movement

of many out of absolute poverty. In addition, in this policy scenario the drag imposed by the domestic public debt on the economy would be alleviated, as the ratio of domestic public debt to GDP gradually declines.

52. It is important to note that both policy scenarios are predicated on significant and swift policy action to reduce the size of the consolidated public deficit in 1991. It is very clear that the Philippines cannot respond slowly to its present economic difficulties. The oil crisis has come at a time when the economy had very little room to maneuver and postponement of necessary action will jeopardize availment of additional financing, increase the ultimate size of the required adjustment, and derail the attainment of a sustainable growth path that would allow the economy to grow out of poverty and debt.

Implications for External Financing Requirements

53. Recent international developments imply that the achievement of the growth goals of the Philippines will require a higher level of external support than originally envisaged. The recent increase in oil prices has dramatically changed the outlook for Philippine macroeconomic performance and external financing requirements. The economy is extremely vulnerable to an oil price shock, since the energy sector is still largely based on oil-fired power plants and since the Philippines imports virtually all its oil. Under the assumptions that oil prices continue to be around US$30 per barrel for the remainder of 1990 and in 1991 and that world trade growth and international interest rates are moderately affected as a result, the Philippines is expected to experience cumulative unidentified financing requirements of over US$1.8 billion in 1990-91.

54. Oil price developments clearly portend further macroeconomic difficulties for the Philippines. The best way to cope with this shock is to make use of market mechanisms to guide the necessary redeployment of resources, in the process increasing the efficiency and resilience of the economy. In this respect, therefore, an oil price shock heightens the urgency of further macroeconomic adjustment and structural reform: it is all the more important now that fiscal restraint be maintained, that the exchange rate stance be flexible, and that trade reforms and industrial deregulation be accelerated. At the same time, extraordinary financing assistance will be needed for the Philippines to weather the oil shock.

55. In the post-1992 period, assuming that oil prices return gradually to the levels prevailing prior to the outbreak of the Middle East crisis, the key aspect of the projected external payments situation is the emergence of sizeable financing gaps because of the "bunching" of maturities of previously rescheduled debt. Financing gaps averaging $1.2 billion a year during 1993-98 result largely from declining net disbursements on private, bilateral and multilateral debt, in decreasing order of magnitude. Combined with large interest payments on the external debt, this implies significant negative resource transfers from 1993 on. It is important to note that these gaps arise despite significant domestic fiscal adjustment and despite the assumption of continued increases in gross disbursements by official lenders

(at around 7% per year) accompanying improvements in the country's absorptive capacity. Consequently, these potential developments highlight the urgency of developing meaningful debt relief solutions for the country.

56. Implementing the needed adjustment and reforms package will surely test the policy resolve of the Government. It will also put to the test the position of creditors to whom repayments have been faithfully made despite political and economic obstacles. While additional adjustment and reform efforts are clearly required on the part of the Philippines, additional external resources will also be required to sustain these efforts, especially in view of a prolonged oil price shock. In this respect, the evolving macroeconomic situation in the Philippines presents a challenge to domestic policy makers and the donor community alike.

I. RECENT ECONOMIC AND POLICY DEVELOPMENTS

A. Introduction

1.1 This chapter reviews economic and policy developments in 1989 and the first half of 1990. The pattern of recent economic growth, fiscal and monetary developments, and the balance of payments, are discussed in Section B. The main conclusions of this section are that macroeconomic performance has been disappointing relative to achievements during 1986-88, that imbalances are emerging with respect to the fiscal and current account deficits, that the main source of stress in the economy is the rising domestic debt, and that strong macroeconomic and structural adjustment efforts will be required to lift the country out of its present predicament; such efforts are made even more urgent by the two most recent shocks experienced by the economy, namely, the earthquake of July 16 and the sharp increase in the price of oil occasioned by the turmoil in the Middle East.

1.2 Section C discusses the Government's recently announced program to arrest the growth of the fiscal and current account deficits and to improve macroeconomic performance. Four sets of measures are reviewed: measures to raise fiscal revenues, to cut expenditures, to reduce interest rates and to restore external competitiveness. The main conclusions of this section are that the Government's program address the issues in the right order of priority; in light of events following the Middle East crisis and unforeseen domestic developments such as the modification of oil products taxation, additional measures will also be needed in order to improve macroeconomic prospects.

1.3 Section D discusses issues in the utilization of external assistance. It reviews past problems in project implementation and preparation, discusses Government efforts to redress the concerns of external donors in this regard, and notes recent developments in the profile of aid disbursements.

B. Recent Economic Developments

Pattern of Recent Growth

1.4 After two years of relatively rapid growth the economy appears to be slowing down. GDP growth, which averaged 6% during 1988 and 1989 (see Table 1.1), is expected to reach only 3.5% in 1990. The principal components of aggregate demand show a similar pattern of change. Consumption growth, which had fueled the earlier stage of the recovery from the deep recession of 1984-85, is expected to be around 4.8% in 1990 after having averaged around 6.2% in the last two years. Investment growth, which was strong in 1988 and 1989 (averaging 16%) is expected to slow down to around 7% this year. Finally, export and import growth are tapering off from the rates experienced recently.

1.5 Sectoral Pattern. The slowdown affects all the major production sectors. Industrial growth, having peaked at 9% in 1988 and declined to 6.9% in 1989, is set to post another year of decline possibly to 4.6% in 1990.

Agriculture has had two relatively strong years in a row, having grown at 3.6% and 4.3% in 1988 and 1989 respectively; however, it is expected to grow by only 2.5% in 1990. Growth in the service sector is expected to decline to around 3.2% this year from an average of around 6% in 1988-89.

Table 1.1: KEY MACROECONOMIC INDICATORS

	1985	1986	1987	1988	1989	1990 1/
Annual Percentage Change						
GDP	-4.4	1.5	4.6	6.4	5.6	3.5
GNP	-4.2	2.0	5.8	6.7	5.7	3.8
Consumption	-0.1	-0.8	5.9	6.2	6.2	4.8
Investment	-21.7	-9.1	34.2	17.3	14.8	6.8
Imports of GNFS	-23.1	12.9	26.5	33.5	22.4	8.0
Exports of GNFS	-7.4	21.8	-1.3	15.9	11.7	6.0
Inflation	23.1	0.8	3.8	8.8	10.6	13.0
Industry	-10.2	-2.1	7.4	9.0	6.9	4.6
Agriculture	3.3	3.3	-1.0	3.6	4.3	2.5
Services	-4.6	3.2	6.6	6.3	5.4	3.2
Ratio to GDP (%)						
Consolidated fiscal deficit	-5.9	-4.8	-2.7	-3.1	-4.0	
Current account deficit	-0.1	3.1	-1.3	-1.1	-3.3	

1 / Projected.

Source: National Economic Development Authority (NEDA)

1.6 Causes of Economic Slowdown. The slowing down of the economy reflects the effects of both external and internal factors. Externally, growth stimulus has been declining since 1988 as seen, for example, in the slowing down of GDP growth in the industrial countries from an average level of 4.4% in 1988 to 3.4% in 1989 and to a projected 2.9% in 1990 (see Table 1.2). The combination of a sharp increase in oil prices and interest rates in 1989 and a sharp decrease in non-oil prices worsened the terms of trade for the Philippines and contributed to the reduction of growth stimulus from the external sector. The expected configuration of world demand and key prices (especially that of oil) suggests that the external environment will not be very supportive of Philippine growth this year.

1.7 Recent turmoil in the Middle East has led to a sharp increase in the price of oil. If oil prices persist at the increased level, the Philippines would suffer in several ways. First, its oil import bill would rise sharply. Second, higher oil prices would reduce the projected growth rates of industrial economies and depress their demand for developing-country exports. Third, world inflation and interest rates would probably rise. All these outcomes would aggravate the already large current account and fiscal deficits of the Philippines and push the economy towards lower growth and higher inflation.

Figure 1.1:Key Macroeconomic Indicators

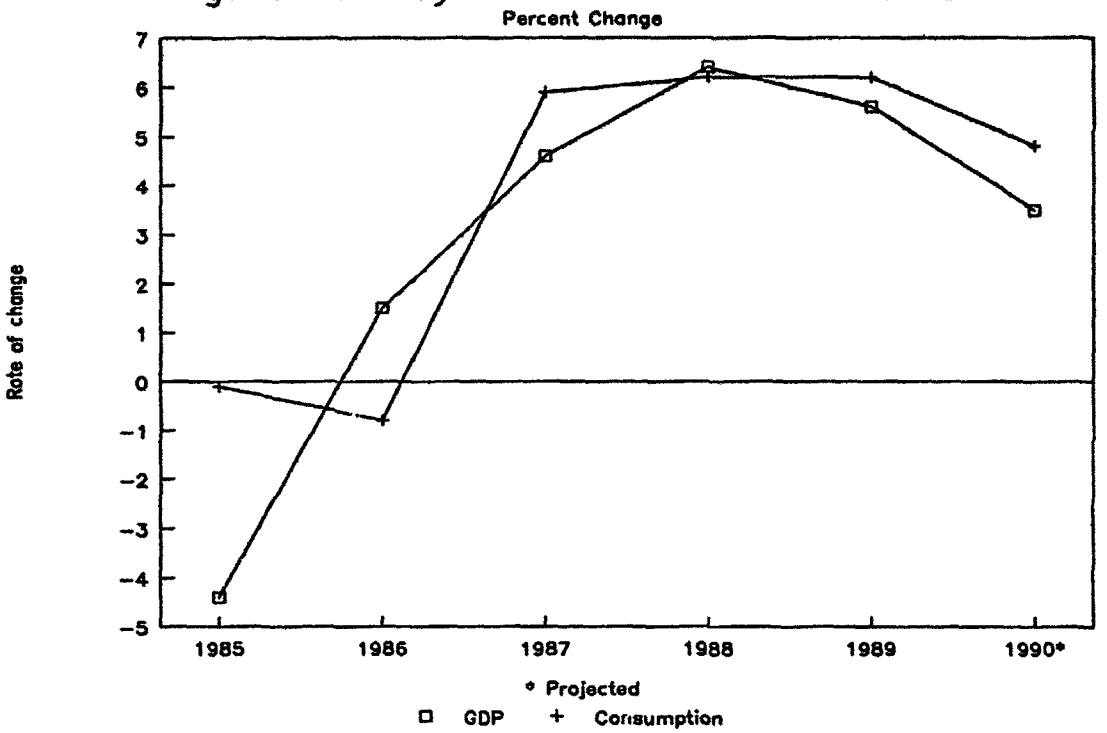


Figure 1.2: Key Macroeconomic Balances

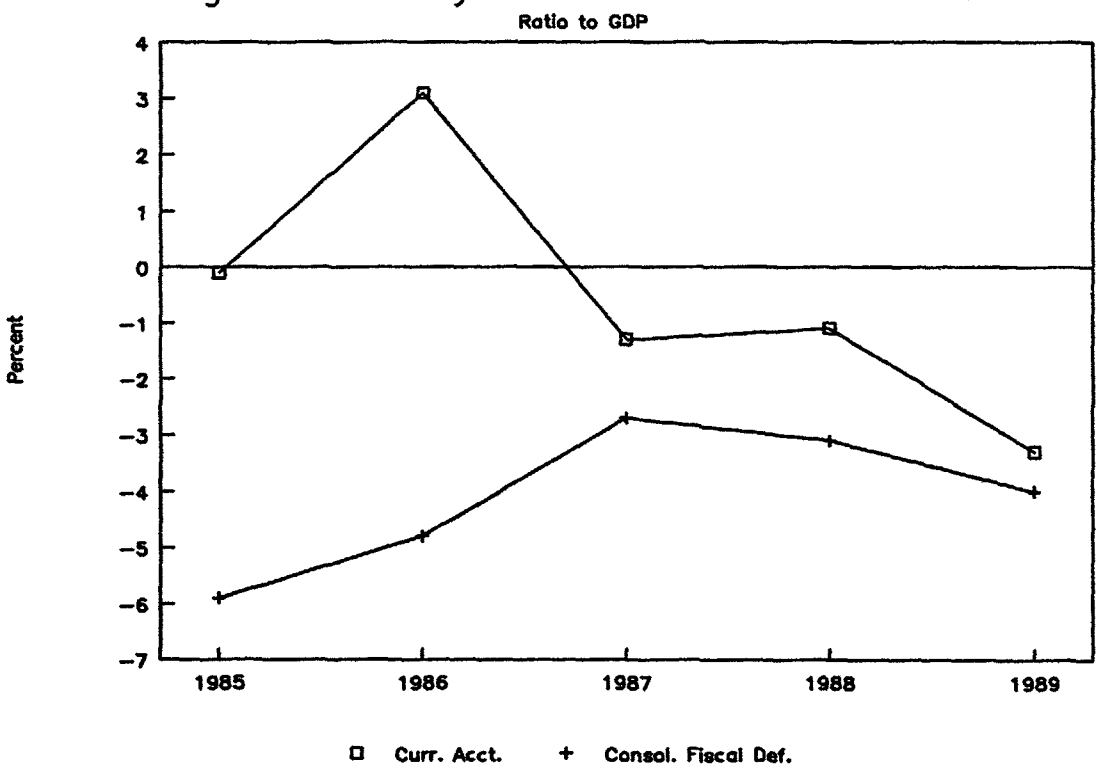


Table 1.2: EXTERNAL DETERMINANTS OF ECONOMIC PERFORMANCE
(Average Annual Growth Rates, Percent)

	1988	1989	1990 1/
GDP Growth			
Industrial Countries	4.4	3.4	2.9
North America	4.4	3.1	2.2
MUV (US$) 2/	7.3	-0.4	5.4
Oil Prices (US$)	-20.9	20.6	n.a
Non-Oil Prices (US$)	21.5	4.9	-10.3
LIBOR (Nominal, mean) 3/	8.1	9.4	9.1

1/ Projected prior to July/August developments in oil prices.
2/ MUV Index: Unit value of manufactured exports from industrial to developing countries.
3/ Six-month dollar LIBOR.

Source: World Bank Data

1.8 Among the internal factors that have affected recent performance is the sharp rise in domestic debt from around 19% of GDP in 1985 to around 24.6% in 1989. In 1989 and 1990, the domestic debt increased primarily because of increases in interest payments occasioned by rising domestic interest rates. A vicious circle linking rising interest rates to higher public sector deficits is in operation now. This connection also affects the current account deficit and inflation and must be broken for macroeconomic stability to be restored. Rising domestic interest rates are partly responsible for the real exchange rate appreciation that has occurred since the end of 1988, a development that has exacerbated the current account deficit. Inflation, too, has been fueled by cost increases arising from higher interest rates and lower output (relative to potential). Inflation and real exchange rate movements in 1989 and 1990 have also been affected by such actions as the large wage increase granted in mid-1989 and the relatively mild nominal depreciation undertaken during 1989.

1.9 Among exogenous factors that may be expected to affect growth in 1990 are the drought of the winter and spring of 1989-90, the power crisis of the spring of 1990, the earthquake of July 1990, recent developments in the Middle East, and the direct and indirect costs of continuing political instability. The drought has already resulted in large losses of spring crops and is the main reason for a projected agricultural growth rate of only 2.5% in 1990. The power crisis, which was partly caused by the drought and partly by the breakdown of several power plants in the Luzon grid, has affected manufacturing output, investment and exports and is the chief reason for a projected industrial sector growth rate of only 4.6% this year. Macroeconomic performance will also be affected by the earthquake that rocked Central Luzon

on July 16: preliminary estimates put the damage to public infrastructure and housing alone at around $600 million dollars. An even greater risk is posed by the recent jump in the price of oil, brought about by turmoil in the Middle East: if this increase is sustained, economic growth in the Philippines could well fall below 3.5% this year. Finally, political instability, most recently reflected in the December 1989 coup attempt, has weakened foreign investor interest, put pressure on the domestic currency and raised inflationary expectations. All these developments contribute to emerging fiscal and external imbalances and will constrain economic growth in 1990 and beyond.

1.10 Potential Consequences of Slowdown. While a slowdown seems unavoidable in the short run, a prolonged recession is avoidable if appropriate macroeconomic policy action is taken. This is important because a sustained reduction in growth will have adverse consequences for fiscal management, external debt servicing and, most importantly, poverty alleviation. Fiscal management or balancing the budget will be made more difficult in two ways: by the decline in tax revenues and the increased difficulty of selling Government assets marked for privatization in a slowing economy. External debt servicing will be made more difficult by the expected decline in export growth as well as by the increased reluctance of foreign investors to invest. Finally, poverty will most likely be exacerbated by a reduction of economic growth. Poverty is strongly related to economic growth in the Philippines: as already noted, poverty incidence declined from 59% to 49% during the spurt of economic growth from 1985 to 1988.

1.11 Domestic Resource Mobilization. Growth during the last three years has not reduced reliance on external finance. In 1986, the gap between the national savings and investment rates was around 3.3% of GNP. Since then, the gross national savings rate has fluctuated around an average of 15.5% while the investment rate has risen steadily to around 18.7% of GNP (see Table 1.3). The gap between national savings and investment rates rose to 3.3% of GNP in 1989 from 1.3% in 1987 and 1.1% in 1988; this gap is made up by foreign savings which flow into the country in the form of investment, grants and loans. Thus, in 1989, the reliance on foreign savings was of identical magnitude (relative to GNP) as in 1986.

1.12 Savings Performance. A disaggregation of recent trends in national savings indicates that the private savings rate remains lower than in the earlier part of the decade and has not been very responsive to interest rates or income growth. While nominal and real interest rates have risen in 1989, the private savings rate has actually dropped. Nor has the increase in per capita incomes since 1985 led to a corresponding sustained increase in the

Table 1.3: SAVINGS AND INVESTMENT RATES 1/

	1986	1987	1988	1989
Gross National Savings Rate	16.5	14.9	16.3	15.4
Public	-0.9	1.6	0.5	0.9
Private	17.4	13.3	15.8	14.5
Gross National Investment Rate	13.2	16.2	17.4	18.7
Public	3.1	3.3	3.1	4.0
Private	10.1	12.9	14.3	14.7

1/ Measured as ratios to GNP.

Source: National Economic Development Authority (NEDA)

savings rate.[1] Recent data also show that public savings remain stuck at a low level. This is best seen as both a cause and a consequence of the current fiscal crisis, a cause in the sense that low rates of public saving contribute to the fiscal deficit but an effect in the sense that such low rates are largely due to the high debt service burden carried by the national budget. Indeed, the low rate of public savings has persisted despite recent improvements in the tax and revenue effort and the achievement of a substantial primary surplus in the budget.

1.13 Investment. The national investment rate has risen steadily in recent years from 13.2% in 1986 to 18.7% in 1989. Nevertheless, it remains below that of principal competitor countries which suggests that, all other things being equal, the Philippines will continue to lag behind these countries in terms of economic growth for several years to come. Furthermore, the current rate is still below that required to sustain significant advances in economic welfare. In particular, the public investment rate continues to be relatively low in relation to the pressing infrastructure needs of the economy. This is not to suggest that there should be concern only for the level of investment: much investment in the 1970s was relatively unproductive and did not contribute to national economic welfare. For the future, policy must be

1/ The lack of responsiveness of the savings rate to income and interest rate changes is something of a puzzle. It is possible that income growth needs to be sustained over a much longer period to have a noticeable effect on the personal savings rate. It is also possible that the savings behavior of the lower-income groups is affected more by the savings deposit rate, which has declined in real terms, than by the much higher (and rising) real time deposit rate. Finally, it is possible that there have been recent changes in the distribution of income favoring lower income groups which tend to have lower marginal propensities to save. This is clearly an area for further empirical analysis.

directed not only at raising the investment rate but also ensuring its quality.

1.14 On the question of quality, the evidence from recent investment trends is mixed. On the one hand, private investment has risen sharply and continues to be robust in 1990 despite the rising cost of doing business as reflected in rising wages, interest rates, and energy prices. Indeed, private investment has been more prominent than public investment in recent years. For example, while public investment tended to average around 35% of total investment in the 1970s, it has averaged around 22% of total investment in recent years. To the extent that public investment had in the past featured several "prestige" projects this reduction in its share could be considered to be good for overall investment quality. On the other hand, to the extent that public investment creates infrastructure and "crowds in" private investment, the slow growth of public investment in recent years could bode ill for economic growth over the medium-term. Furthermore, recent private sector investment has not been of unambiguously high quality from the standpoint of overall economic efficiency. For example, the share of export-oriented projects has decreased: investments in export-related industries fell from 72% of total investments approved by the Board of Investments (BOI) in 1986 to around 55% in 1989. Also, the capital intensity of investments has risen: investment per worker in BOI-approved projects rose from around 12000 pesos in 1986 to 46000 pesos in 1989 (in real 1983 pesos). This raises concerns about the efficacy of trade and industrial policy in the Philippines.

Table 1.4: SELECTED INVESTMENT DATA 1/

	1986	1987	1988	1989
Export Oriented Investments to Total Investment(%)	72	62	50	55
Capital per Worker (000 pesos, 1983 prices)	12	15	26	46

1/ Investments refer to new and expansion project approvals by BOI.

Fiscal Developments

1.15 Consolidated Deficit. The consolidated public sector deficit declined from 5.9% of GDP in 1985 to 4.0% in 1989 (see Table 1.5). This was due largely to a decline in the National Government (NG) deficit equivalent to 3% of GDP since 1986 but also to improvements in the deficits of other components of the public sector accounts such as the Central Bank, Government Corporations (GC) and Government Financial Institutions (GFI). Improvement in

the NG deficit was due largely to an increase in revenue effort: the ratio of revenues to GDP rose from 12.8% in 1986 to 15.8% in 1989. Without this increase in revenues, the deficit situation would have been much worse, since expenditures have continued to rise more or less steadily since 1984-85.

Table 1.5: CONSOLIDATED PUBLIC SECTOR ACCOUNTS 1/
(Share of GDP, percent)

Agency	1984	1985	1986	1987	1988	1989
Consolidated Public Sector	-8.2	-5.9	-4.8	-2.7	-3.1	-4.0
National Government	-1.9	-1.8	-5.0	-2.8	-2.8	-2.0
NG Revenues	10.5	11.3	12.6	14.3	13.7	15.8
NG Expenditures	12.4	13.1	17.6	17.1	16.5	17.8
Government Corporations	-2.1	-1.3	-1.1	-0.5	0.3	-0.4
Central Bank	-5.1	-2.5	-2.9	-1.5	-2.0	-2.2
Govt. Financial Institutions	-1.6	-3.0	-1.9	0.2	0.3	0.3
Others 2/	2.6	2.8	6.1	2.0	1.2	0.2

1/ Note that (-) refers to a deficit.
2/ Includes NG transfers to Govt. Corporations, Local Govts, and other agencies.

Source: Department of Budget and Management

1.16 Government Expenditure Trends. Disaggregation of National Government expenditures by functional categories reveals several meaningful trends. First, personnel expenditures more than doubled in nominal terms since 1986. This was due both to growth in the number of personnel and to increases in the average compensation of Government employees, the latter measure being quite prominent in 1989 when compensation at the lower end of the Government pay scale was raised by around 35% through the Salary Standardization Act. While this measure was defended on the grounds that public sector salaries were too low to attract personnel of suitable skills and that, at the lower end, public sector wages were barely enough to keep employees above the poverty line, the timing of the salary increases was unfortunate in that they occurred during a year in which there were significant other pressures on the budget.

Fig. 1.3: Trends in Govmnt. Expenditure

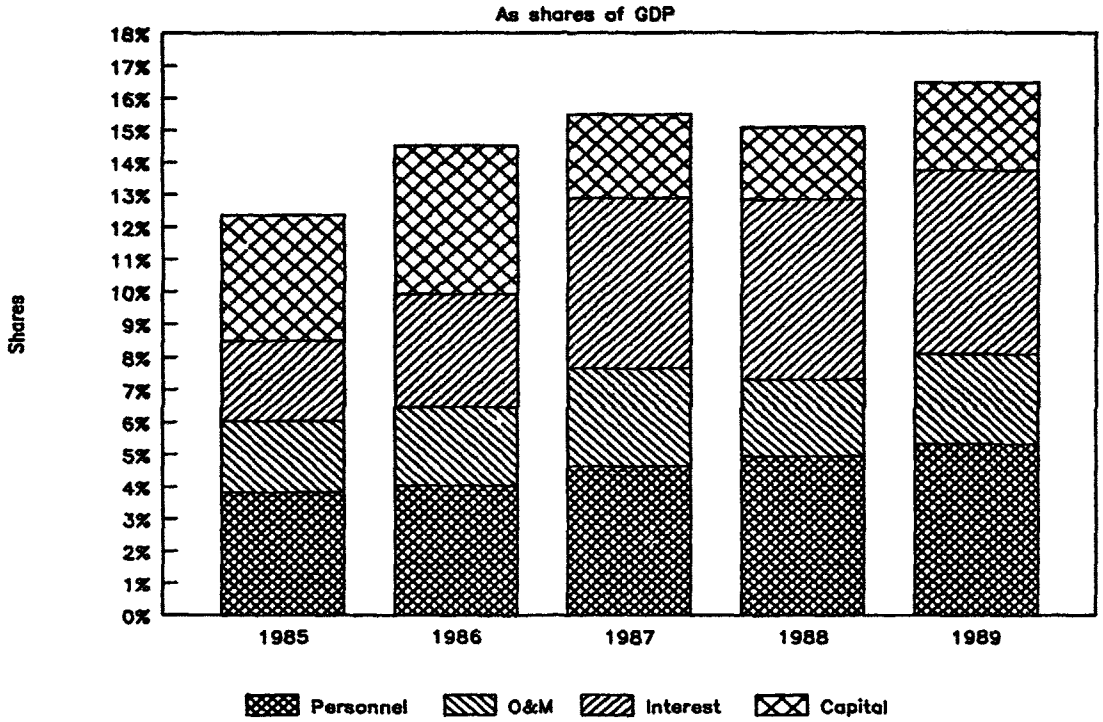
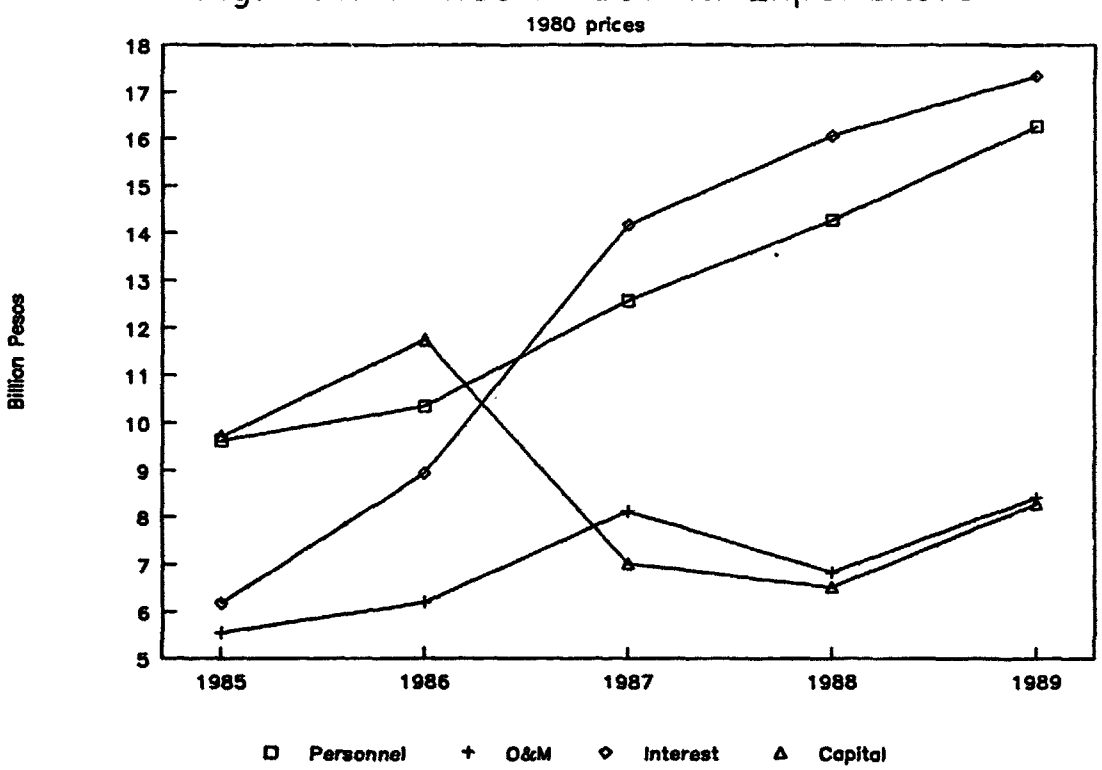


Fig. 1.4: Trends in Govmt. Expenditure



1.17 Second, interest payments on Government debt constituted an important source of pressure on the budget throughout 1986-89. Interest payments increased by 150% from a level of 21.6 billion pesos in 1986 to 54.8 billion pesos in 1989. While this was a significant increase in itself, it understates the true burden on the public accounts. The true burden would include amortization of the external debt as well as interest payments made by the Central Bank which holds much of the public debt. In recent years, payments by the Central Bank have been equivalent in nominal levels to the payments made by the National Government. The debt service burden of the National Government alone amounted to about 41% of total expenditures in 1989, up from about 22% in 1985.

1.18 Third, operations and maintenance (O&M) expenditures rose modestly from a level of 15 billion pesos in 1986 to 19.5 billion pesos in 1988 but then jumped to 27 billion pesos in 1989.[2] The spurt in 1989 was undoubtedly necessary since O&M expenditures had declined in real terms since the early 1980s, a victim of the recession and the ensuing fiscal squeeze. This decline in real terms is reflected in the poor state of infrastructure maintenance in the country as shown by deteriorating roads, bridges, ports and public facilities as well as the increasing frequency of breakdowns of power plants (especially in 1990).

1.19 Fourth, the trend in capital infrastructure outlays was similar to that of O&M expenditures. Such outlays rose modestly from 1986 to 1988 and then jumped in 1989. Again the jump was necessary in view of the state of infrastructure in the Philippines and the fact that infrastructure spending has not yet recovered in real terms to the levels of the early 1980s. The low level of capital outlays on infrastructure has contributed to the present electricity crisis brought on by inadequate and delayed investments in power generation capacity. Trends in O&M and infrastructure capital outlays suggest that the fiscal adjustment since the mid-1980s has been borne disproportionately by these categories of expenditures. Such a strategy essentially buys short-term adjustment at the expense of long-term growth and may not be viable over the longer run as foregone growth (due to inadequate infrastructure investments) constrains revenues and creates another source of pressure on the fiscal balance.

1.20 A fifth trend revealed by the disaggregated Government expenditure accounts is that equity contributions by the National Government to public corporations declined significantly from around 12.3 billion pesos in 1986 to only 2.2 billion pesos in 1989. The decline in real terms and relative to GNP is even sharper. This trend is consistent with Government efforts to make public enterprises more autonomous financially by raising resources from internal sources rather than by relying on Government transfers.

2/ In real terms (1980 prices) the increase in O & M expenditures was mere modest, amounting to only about 1.3 billion Pesos between 1985 and 1988 followed by a spurt of 1.6 billion Pesos in 1989.

Table 1.6: FUNCTIONAL ALLOCATION OF GOVERNMENT EXPENDITURES

	1983	1985	1987	1988	1989
Capital Outlays	27	18	13	11	14
Personal Services	26	25	20	26	26
O & M	21	16	13	13	14
Interest Payments	9	17	24	27	27
Other 1/	17	24	30	22	19
Total	100	100	100	100	100
Memo Item					
Debt Service/Expenditures	15	22	45	43	41
Expenditures/GNP	15	15	22	20	21

1/ Includes net lending, subsidy, tax expenditures and amortization.

Source: Department of Budget and Management

Table 1.7: GOVERNMENT REVENUE TRENDS
(Share of GNP, percent)

	1985	1986	1987	1988	1989
Tax Revenues					
Internal Revenue 1/	7.4	7.8	8.5	7.8	8.6
Customs Revenue	2.8	2.8	3.7	3.0	4.0
Non Tax Revenues 2/	1.3	2.2	2.2	2.9	3.2
Total	11.5	12.8	14.4	13.7	15.8

1/ Includes all BIR and other office collections.
2/ Includes income from fees and charges, foreign grants and proceeds from privatization.

1.21 Government Revenue Trends. Government revenues have almost doubled between 1986 and 1989, from around 79 billion pesos to almost 153 billion pesos. They have increased from around 12.8% of GNP in 1986 to 15.8% in 1989. Increases in collections have occurred across all major revenue categories with the most significant increase in percentage terms coming from Customs

Figure 1.5:Trends in Government Revenue

As Share of GDP

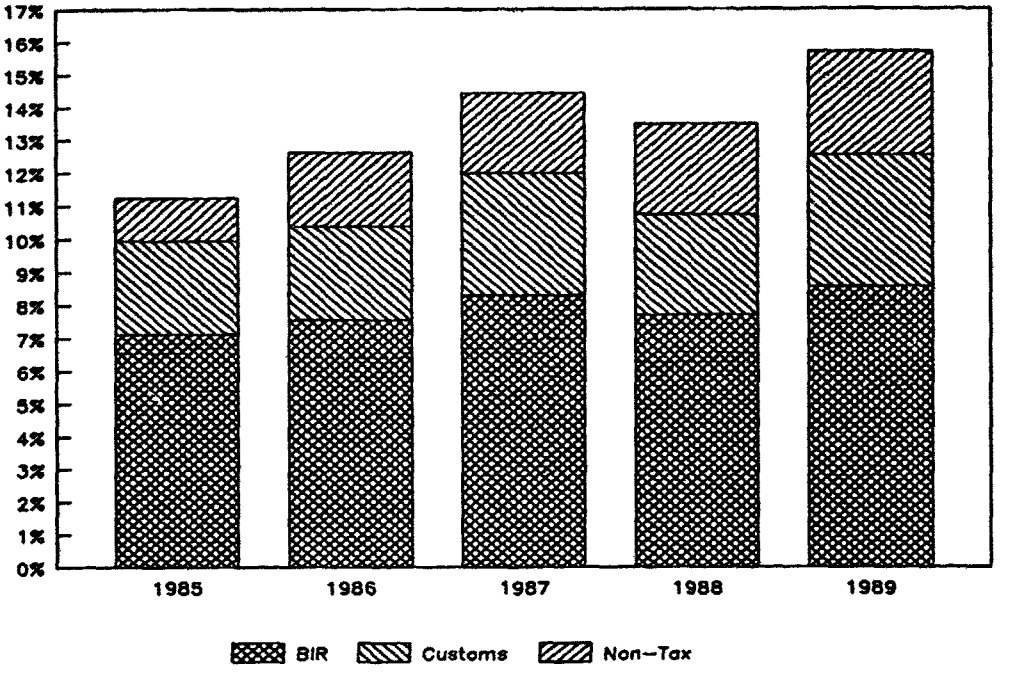
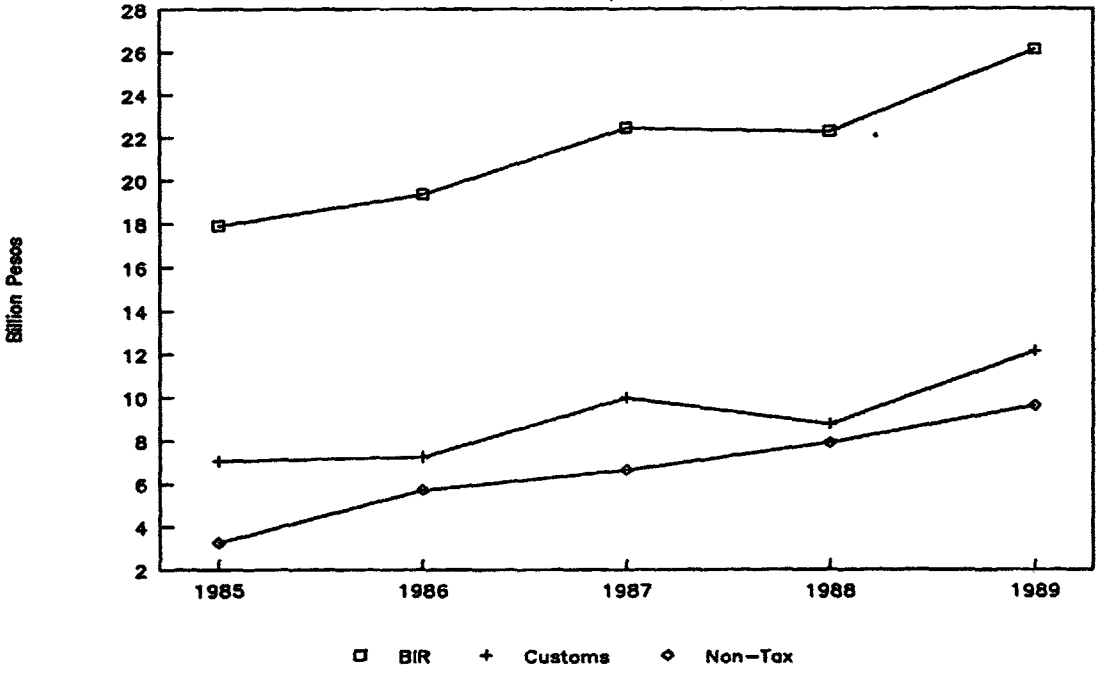


Figure 1.6:Trends in Government Revenue

Constant Prices (1980=100)



revenues (from 2.8% of GNP to 4%), followed by internal revenue (7.8% to 8.6%) and non-tax revenue (from 2.2% to 3.2%). While the overall revenue increase has been of great assistance to fiscal adjustment, the pattern suggests a fragility that may be of consequence in periods of slowing growth. For example, the bulk of the increase has come from import duties collected from a sharply rising level of imports. The ratio of Customs collections to import values has been constant at around 15%; this suggests that Customs revenues will decline if imports decline. To some extent, then, this source of fiscal improvement is of a conditional nature.

1.22 Similarly, the improvement of internal revenues in 1989 was due largely to increases in interest tax collections on Treasury Bill transactions. Since Treasury Bills are issued by the National Government, such taxes ultimately fall on the Government itself. As a result, the increase in revenues has a neutral fiscal impact since it constitutes a transfer from one Government agency (the Treasury) to another (the Board of Internal Revenue or BIR).

1.23 Recent VAT Performance. VAT collections, while rising, continue to fall below target. In 1988, the first year of the program, the shortfall in collections was blamed on a late start of the program (in April); in 1989, the shortfall was blamed on an inadequate collection budget (reflected in fewer personnel hired to collect VAT than thought necessary). Whatever the reasons, performance has not only been below targets but also considerably below potential. The potential collection from VAT, based on national accounts estimates of value-added, is huge and at present less than half the potential tax is being collected.

1.24 Fiscal Deterioration in 1990. Despite significant fiscal adjustment and despite an improvement in the National Government's deficit up to 1989, the Philippines faces a fiscal crisis in 1990. In the absence of corrective measures, the consolidated public sector deficit could reach as much as 55 billion pesos or 5% of GDP. The increase in the deficit is in part due to the pick-up of investment plans of Government Corporations as well as line agencies. Much of it is also due, however, to the Government's management of the Oil Price Stabilization Fund (OPSF) on the one hand and of the management of the national debt on the other.

1.25 The OPSF is a price buffer scheme for oil and oil products. As in all such schemes, the Government's contribution is determined by the extent to which it wants to shield end-users from increases in the price of oil. Since 1989, the peso price of imported oil has increased substantially because of both an increase in the world price and the depreciation of the peso. Government chose, however, not to pass along most of this increase to end-users. As a result, the OPSF has gone into a substantial deficit (10.7 billion pesos as of June 1990) which will have to be made up through additional budgetary appropriations.

1.26 Recently, Government has announced the decision to eliminate the present system of official price support for oil--starting in 1991--and in the interim to adjust the domestic oil prices in order to maintain the OPSF in flow equilibrium. While this decision will not reduce the large claim of 10.7 billion pesos that has already been established, it will protect the budget

from future claims. In September 1990, the domestic prices of oil products were raised by 30% on average, bringing them in line with international prices as of August 1990. Given the continuing upward trend in international oil prices, there is already renewed pressure for another round of price increase, or the OPSF will continue to accumulate deficits. Furthermore, in September 1990 the tax regime of oil products was modified from an ad valorem basis to a specific basis. This measure is not revenue-neutral and it is estimated to entail a revenue loss of P0.5 billion in 1990 and P6 billion in 1991. This will further aggravate the prospects for the fiscal deficit unless offsetting revenue-increasing measures are introduced.

1.27 Another factor behind the worsening fiscal deficit is the evolution of the public debt. The Philippines has a large public debt whose servicing absorbs around 41% of the budget. The debt has had to be financed domestically because the Philippines has had little access to external finance in recent years and also because the room for fiscal adjustment has been limited by a relatively low yield public revenue system on the one hand and high non-discretionary expenditures on the other. The level and financing of this debt has resulted in an escalating sequence of high interest rates and rising debt service payments. This sequence has already entered a phase that makes macroeconomic management very difficult. The cost of borrowing has been high for three main reasons: (a) domestic financial markets lack both breadth and depth in that there are few suppliers of credit and the predominant preference is for short-term loans; (b) Government has simultaneously pursued a low inflation target through tight monetary policy; and (c) the exchange rate has been permitted to appreciate in real effective terms and public anticipation of an eventual correction has been built into the domestic interest rate. The level and manner of financing the public debt is a key macroeconomic issue and is dealt with in detail in Chapter 2. The measures recently proposed by Government to control the burgeoning deficit are also discussed there.

The Balance of Payments

1.28 Current Account Deficit. The current account deficit deteriorated sharply in 1989 (see Table 1.8). After two years at relatively comfortable levels (averaging 1.15% of GDP), the current account deficit reached $1.5 billion in 1989 or 3.3% of GDP; an even larger deficit (up to 5%) could be registered in 1990. The deterioration in 1989 was due almost entirely to a substantial growth of imports (27%) which overshadowed the otherwise encouraging growth of exports (14%). The balance on invisible trade posted a surplus in 1989 as opposed to deficits in the previous two years.[3]

1.29 Composition of Imports and Exports. Among merchandise imports, capital goods imports increased the most during 1988 and 1989, an aspect which is

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3/ The balance on invisible trade improved significantly in 1989 despite disappointing performance on overseas remittances. Remittances increased by a meager 8% in 1989 after having grown at an average of 22% in the two previous years. Indeed, while remittances from overseas workers increased, those from overseas residents declined in nominal terms in 1989.

consistent with the increase in investment during these years and reflects business confidence in the medium-term economic prospects of the country. Some big-ticket items, namely the purchase of gas turbines by the National Power Corporation and of aircraft by Philippine Airlines, featured significantly in the increase of capital goods imports. While these were a small share of total imports, they were a large share of the current account deficit.[4] Consumer goods imports also rose significantly but their share of total imports remained less than 8.6%.

Table 1.8: EXTERNAL SECTOR ACCOUNTS
(US$ million)

	1984	1985	1986	1987	1988	1989
Current Account Deficit	-1116	-103	954	-444	-390	-1465
Trade	-679	-482	-202	-1017	-1085	-2598
Invisibles	-823	0	715	-76	-80	303
Capital Account	1205	1711	-81	-421	643	1527
DFI	17	17	140	326	986	854
Loans (MLT) Official	987	1376	1291	1731	1563	1939
Loans (MLT) Private	272	2586	1314	867	-849	885
Net Short-term Capital	549	-1731	-824	80	-303	-91
Memo						
GDP (current P billion)	32365	32941	30740	34388	39133	44387
Current Account/GDP (%)	-3.4	-0.3	3.1	-1.3	-1.0	-3.3
Exchange Rate (P/US$ avg.)	16.7	18.6	20.5	20.6	21.1	21.7

Source: Central Bank

1.30 Among merchandise exports, electronics and garments continued to be the dominant categories with the highest shares and with high growth rates. Both these categories, however, have weak linkages with the rest of the economy and cannot form the basis for a sustained and diversified export drive. They are characterized by enclave production, typically in export processing zones, and

4/ For example, purchases of power generators soared from only 63 million dollars in 1987 to 639 million in 1988 and 987 million in 1989. Purchases of aircraft, ships and boats soared from 33 million dollars in 1987 to 123 million in 1988 and further to 195 million in 1989. Broadly speaking, these categories have added almost 1 billion dollars to the import bill compared to 1987 levels; this sum is almost two thirds of the 1989 current account deficit.

involving primarily assembly and packaging operations. Spinoff benefits, in the form of backward linkages, entrepreneurial development, or technological advance have been minimal despite significant growth of export volume in the last decade or so. Furthermore, production is import intensive and contributes much less by way of net foreign exchange earnings than gross export values would imply. While domestic value added has grown in the garments sector the electronics sector has experienced a decline; current import intensity ratios of these industries are around 56% and 80%, respectively. Finally, the market for semiconductors (the main electronics item produced in the Philippines) has proved to be volatile; the world industry has been characterized by a couple of significant downturns in the 1980s and by shakeouts. Thus, even though the Philippine experience has been positive so far, it is arguable whether such an industry can be relied upon for consistent long-run export earnings.

1.31 Export structure has changed moderately in recent years, driven mostly by improvements in the export of garments. The share of manufactures has risen from around 60% in 1985-86 to around 63% in 1987-89 as the share of garments has risen from around 14.5% to around 19%. Given the fact that little real growth can be expected from traditional exports (such as agricultural products and minerals) and that the two key manufactured exports (i.e. electronics and garments) have weak linkages with the rest of the economy, the structure of exports needs to change more dramatically for there to be a significantly higher developmental impact from a given level of exports.

1.32 Export performance has been disappointing not only in the above-noted structural sense but also in that rates of growth have not been high enough to improve the current account, especially in 1989 and 1990. In part, this has been due to lack of support from trade and exchange rate policy. While exchange rate policy may be assessed in different ways using different measures, one critical measure, especially for exports, is the real effective exchange rate vis-a-vis Indonesia, Malaysia and Thailand, three key competitors; figure 1.7 shows that this has appreciated steadily since 1986, a development which has kept export growth rates below potential and contributed to the deceleration seen in 1989.[5] Indeed, during 1989, other measures of real exchange rates also showed appreciation, thereby contributing to the acceleration of imports and the widening of the current account deficit. Trade policy has also contributed by maintaining excessive levels of protection for domestic industries; despite some import liberalization in the last three years, effective rates of protection for many import-substitute

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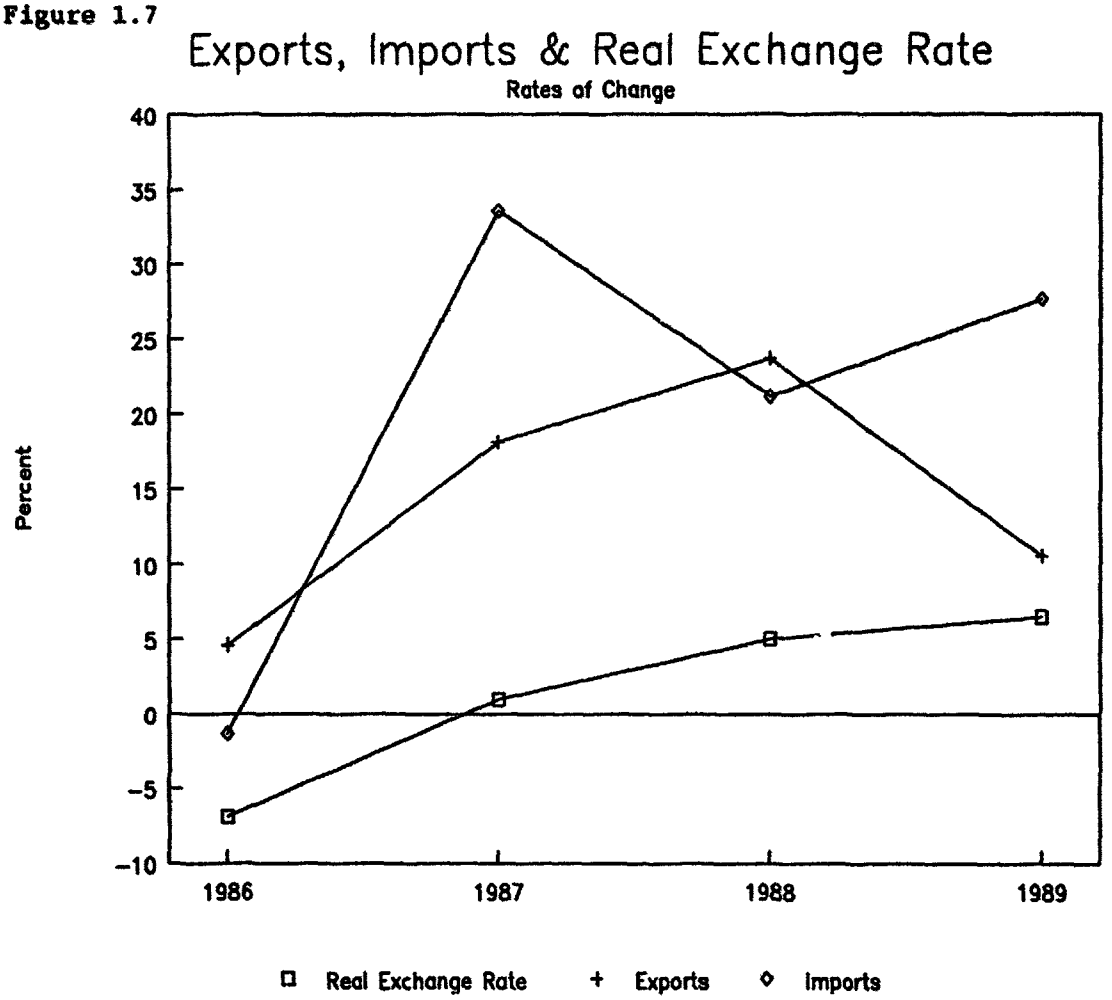
5/ The argument that depreciation would improve export growth has to be based on the comparative experience of Southeast Asian countries rather than on export price elasticity estimates for the Philippines. Such estimates are hampered by changes in the structure of Philippine exports in the last twenty years. Elasticity estimates based on aggregate exports tend to be biased downward because they do not take into account such changes as the significant increase in the share of electronics, garments, furniture and prawns in the export basket. They understate the importance of these price-sensitive items and overstate the importance of the relatively less sensitive items, such as primary products.

Figure 1.7



industries have remained high, thereby maintaining an investment bias in favor of such industries and against the export sector. This is reflected also in the investment data already mentioned which show the share of export-oriented investments approved by the BOI to have decreased over the last three years. To improve export performance it will be necessary to rectify trade and exchange rate policies to eliminate such biases. In addition, it will be necessary to promote exports directly through programs to provide exporters access to finance at competitive rates and to remove various institutional impediments. [6]

6/ The disappointing performance of exports is not necessarily due to protectionism on the part of the developed countries. While the Philippines does face non-tariff barriers of various kinds the effect on manufactured or non-traditional exports has not been substantial. Indeed, the Philippines typically fails to exhaust its quotas in major garment markets.

Table 1.9: TRADE STRUCTURE 1/
(Percent)

	1985	1986	1987	1988	1989
Share of GDP					
Imports	15.5	16.4	19.6	20.8	23.5
Exports	14.1	15.7	16.6	18.1	17.7
Share of Total Imports					
Capital Goods	15.4	17.1	18.0	20.1	23.3
Raw Materials and Intermed.	43.0	53.0	50.9	54.1	51.7
Mineral Fuels & Lubricant	28.4	17.2	18.5	13.4	13.4
Consumer Goods	8.6	7.9	8.1	7.3	8.6
Share of Total Exports					
All Manufactures	59.7	59.5	63.7	61.3	66.4
Electronics	22.8	19.0	19.6	20.9	22.4
Garments	13.5	15.5	19.2	18.6	20.1
Furniture	1.8	1.8	2.3	2.6	2.6
Chemicals	3.2	5.0	4.3	3.6	3.6

1/ Data for 1988-89 reflect new table format being used by Central Bank.

Source: Central Bank

1.33 Implications of Current Account Deterioration. Some aspects of the evolving structure of trade suggest that recent current account deterioration may not necessarily reflect a fundamental balance of payments disequilibrium. For example, as noted above, recent import growth has occurred largely in capital goods, raw materials and intermediate inputs which are normally associated with productive investment and growth. Also, some distortion is introduced by the relative importance of big-ticket one-shot purchases in recent import data. On the other hand, other data indicate that the Philippines is undergoing an erosion of competitiveness which, if unchecked, will produce continued balance of payments weakness. Evidence of declining competitiveness may be found in the deteriorating current account deficit as well as in the declining market share of Philippines' exports in major markets. Economic efficiency and relative competitiveness are key issues for the Philippines and are discussed in more detail later in Chapter 3.

1.34 The seriousness of any level of the current account deficit depends essentially on the external financing environment facing the country. In the case of the Philippines, external financiers are unlikely to finance sustained deficits at the 1989 level. The Philippines has not yet regained access to voluntary long-term private credit and general BOP financing from official sources is also becoming increasingly hard to come by. Hence, it is important

to arrest the growth of the current account deficit even if much of it is accounted for by investment related imports. The implication is that export growth must be accelerated to compensate for rising imports and that more powerful incentives have to be given to domestic entrepreneurs to shift from domestic to international markets.

1.35 Trends in Foreign Investment. Foreign investment shot up in 1988 and 1989 but appears to be falling off in 1990 possibly because of the persistence of infrastructure problems (especially with electricity supply) and rumors of coup d'etat. Balance of payments data show such investments to have amounted to US$986 million in 1988 and US$854 million in 1989, as compared to only US$326 million in 1987. Renewed confidence in the economy played a large part in attracting foreign investment during this years. In addition, the availability of a debt-equity swap facility also played a role: almost 80% of the foreign investment inflow for 1988 was due to this facility. A re-opening of this facility would certainly heighten investor interest, but since such facilities tend to have undesirable monetary consequences, it would not be prudent to rely on them alone to induce higher foreign investment. Other inducements must be found since there does exist an opportunity to increase foreign investment inflows substantially. The surpluses of Japan and the NICs are circling the globe in search of investment opportunities; these surpluses have been availed of by many neighboring countries, such as Malaysia, Thailand and Indonesia, and could be enticed into the Philippines in larger quantities by bold reforms in the system of regulations governing foreign investment. Among such reforms would be measures to enable foreign investors to enter a larger number of business sectors, keep management control for a longer period of time, and have more flexibility with regard to land ownership.[7]

1.36 Trends in Official Loans. Net medium and long term loan disbursements rose to about US$1.9 billion in 1989 from an average of about US$1.6 billion in the two years prior to 1989. This trend, however, masks two underlying developments that should provide cause for concern. First, official transfers from multilateral agencies have been negative on a net basis although far less so in 1989 than in 1988. Second, through 1988, commitments and undisbursed balances rose faster than disbursements and the aid pipeline was relatively clogged. The disbursement problem applies largely to project financing; program (or BOP support) financing has been disbursed more or less on schedule in recent years. Government is aware of the importance of increasing disbursements from committed loans and has recently undertaken a variety of measures to facilitate project implementation, measures which have resulted in a noticeable improvement in 1989.

7/ While the incentives framework needs to be improved, the role of the macroeconomic environment should not be ignored. At the current level of domestic interest rates, it may be difficult to attract foreign investment into physical assets since the return on financial assets is so attractive.

Table 1.10: NET RESOURCE TRANSFERS 1/
(in million US$)

	1988	1989
Total	-1766	-1411
Multilateral	-564	-34
Bilateral	44	178
Private Banks	-1092	-1485
Others	-154	-70

1/ Central Bank provisional estimates.

1.37 Trends in Private Loans. The flow of net medium and long term lending by private sources has tended to fluctuate with rescheduling and debt reduction exercises in recent years. While it is premature to assert that the Philippines has regained access to voluntary private credit, it was the second country, after Mexico, to benefit from a concerted debt reduction plan in which a substantial amount of "new" money was pledged by commercial banks. In the second quarter of 1990, it received US$482 million of this "new" money and about US$233 million dollars is expected to be disbursed during the rest of 1990. At the time of the debt-reduction agreement, commercial banks were of the view that, given the Philippines' strong macroeconomic adjustment during 1986-89, a return to creditworthiness was foreseeable.

1.38 External Debt Developments. Outstanding foreign debt stayed roughly constant during 1987-89 at a level of about US$30 billion dollars as new borrowings were offset by debt reduction operations such as debt-equity swaps and direct debt buybacks. As a result, debt ratios declined. Thus, the debt-to-GDP ratio declined to 69% in 1989 as compared to around 87% in 1987. Similarly, debt service declined to about 30% of exports in 1989 from a level of 39% in 1987. Clearly, much progress has been made in recent years in reducing the foreign exchange burden of the external debt. Some of this progress, however, has been at the cost of increasing the domestic debt burden. As discussed further in Chapter 2, the Philippine debt crisis has not disappeared but its form has changed somewhat: it is now more of an "internal" debt crisis and less of an "external" debt crisis.

Monetary Developments

1.39 Monetary developments in 1989 have been substantially different than in recent experience. The year was characterized by a sharp increase in base money, 35% at end-89, partly reflected by domestic liquidity, which grew at 18%. Some accidental factors contributed to the acceleration of money growth, such as the surge in money demand in December, after the coup attempt, which was accommodated to prevent disruption in banking activity and excessive price increases. The determining factor was however the very large financing

requirements of the consolidated public sector, which in turn reflected the increase in the National Government current expenditures--both interest payments and other expenditures--and the Central Bank operational losses--almost entirely net interest payments.

1.40 The emergence of a large consolidated public sector deficit in 1989 was due to a large extent to the mix of insufficient fiscal adjustment, tight monetary policy and the sterilization of official reserve accumulation and DDSR operations by the Central Bank in 1987-88. This had in turn resulted in the sharp increase in the stock of public sector domestic debt and interest rates in the same period. In 1989, these events led to unusually high monetization of the financing requirements of the public sector: indeed, expansion of base money was the largest source of financing to the consolidated public sector.

1.41 Table 1.11 summarizes the most important trends in money, interest rates, inflation and the exchange rate. The dramatic increase in base money which occurred in the last quarter of 1989 does not appear to be fully reflected by the other money supply indicators, though net domestic credit grew at a considerably higher rate than in 1988, and domestic liquidity continued to grow in excess of nominal GDP. Most recent developments, during the first quarter of 1990, indicate that base money and broad money growth has considerably slowed down: preliminary data indicate that, between end-December 1989 and end-March 1990, base money had decreased by 7.1% and broad money by 1.6%.

1.42 Interest Rates. Interest rates rose sharply during 1988 and 1989, and this tendency accelerated in 1990. The Treasury Bill rate, which averaged only 11.4% in 1987, rose to 14.4% in 1988, to 19.3% in 1989 and to 22% in the first half of 1990. As the T-Bill rate rose, it drew other rates along although not necessarily in proportion. Moreover, during 1989, the increase in all nominal rates was in excess of inflation; hence real rates also rose. The real T-bill rate rose from 5.6% in 1988 to 8.7% in 1989; it has been fluctuating between 9% and 10% in recent months.

1.43 The prevalence of high and rising real interest rates reflects the combined effects of the increase in the private demand for credit to support the economic expansion of recent years and the high demand for credit by the consolidated public sector, rising inflationary expectations associated with the economic and political difficulties of the past year, and the view that the current exchange rate stance is untenable given the size of the current account deficit and other indicators of external competitiveness. Among these factors, the rising public demand for credit may be the most critical. One measure of this demand is the average monthly volume of Treasury Bills auctioned in accordance with the Government's fiscal and monetary program. Treasury Bill transactions have increased from an average level of 15.4 billion pesos per month in 1987 to around 30.6 billion pesos currently; on a weekly basis, they have risen from around 3.7 billion pesos to around 7.3 billion pesos. Since these securities have short maturities (85% are of 90 day maturities), there is a need to refinance at short intervals, an aspect that quickly builds in inflation and exchange rate expectations into the interest rate structure.

Table 1.11: MONETARY DEVELOPMENTS

	1985	1986	1987	1988	1989
Money Growth (%)					
Net Domestic Credit	-4.5	-8.7	-30.5	3.6	17.0
Broad Money	9.5	13.5	11.3	23.1	25.1
Base Money	6.3	13.8	11.0	15.1	35.2
Interest Rates (Nominal)					
T-Bill (91 day)	27.0	14.4	11.4	14.4	19.3
Time Deposit (all mat.)	21.8	14.8	11.1	13.7	17.0
Secured Lending (all mat.)	28.2	17.4	13.3	16.0	19.4
Inflation (%)					
CPI	23.1	0.8	3.8	8.8	10.6
GDP Deflator	17.7	1.5	7.0	9.8	10.1
Exchange Rates					
P/US$ (Nominal)	18.6	20.4	20.6	21.1	21.7
Real Effective 2/	102.0	98.8	114.2	117.3	124.1
Real Effective 3/	89.4	71.5	67.1	66.0	69.7

1/ Preliminary.
2/ Narrow series vis-a-vis Indonesia, Malaysia and Thailand (1980=100).
3/ Series vis-a-vis major trading partners (1980=100).

1.44 Inflation. For the year as a whole, inflation in 1989 was 10.6% as measured by the Consumer Price Index and 10.1% as measured by the implicit GDP deflator. By the latter measure, inflation in 1989 was virtually the same in 1989 as in 1988. However, in the second half of 1989 inflation has experienced a substantial acceleration, rising to 13% on a 12-month basis.

1.45 Inflation in 1989 was fueled in part by large wage adjustments at the lower end of both private and public sector wage scales: private sector employees received an increase of approximately 40% in the minimum wage starting July 1989 whereas public sector employees received an increase in compensation of about 30% on average. Two other contributing factors were increasing energy and food costs. Energy costs were pushed up by the increase in oil prices in 1989; all of the increase was not passed along to end-users, however, and a substantial upward adjustment remains to be made in the course of this year. Food prices were affected by a drought beginning in the last quarter of 1989; the full inflationary impact of the drought will be felt in the course of 1990.

1.46 Inflation was recorded at over 12%, on an annual basis, in the first half of 1990. It would have been even higher had it not been for such factors

as price controls introduced in the aftermath of the coup attempt. It is likely that inflation will accelerate in the second half, in part as the effects of the drought and the earthquake make themselves felt in higher food and commodity prices and in part because domestic oil prices have increased by about 30% and are expected to be raised further in line with the substantial increase in world prices.

1.47 Exchange Rates. The peso-dollar nominal exchange rate depreciated steadily from 21.1 at the end of 1988 to 21.7 at the end of 1989. However, the movement in the nominal rate belies that in the real effective rate which appreciated in 1989; for example, the real effective exchange rate vis-a-vis chief competitors appreciated about 6%. This trend is in the process of reversal; in recent months, there has been a fairly rapid depreciation of the nominal exchange rate to a level of 25 pesos per US$ as of end-August. This trend, if continued and supported with fiscal and wage restraint, will help in restoring external competitiveness.

1.48 Monetary Management. In 1989, in the attempt to offset the effects of high monetary growth, the Government imposed higher reserve requirements, raised rediscount rates, and continued to engage in open-market operations, though to a lesser extent than during 1988. While these measures moderated inflationary pressures, they also contributed to the sharp increase in interest rates. A positive side effect of these measures was the homogenization of reserve requirements of long-term deposits across banks, which eliminated the lower requirements enjoyed by rural and thrift banks.

C. Revised Adjustment Program

1.49 The emerging fiscal and external imbalances have upset the original macroeconomic program of the Government, as agreed with the IMF in March 1989 and as revised in November 1989. Consequently, a new medium-term program is being drafted. While certain specific details have yet to be negotiated with the IMF, the broad program has been announced. The program gives top priority to fiscal adjustment and proposes to support this adjustment with complementary monetary and exchange rate policies. The fiscal adjustment program contains both revenue raising and expenditure reducing measures. In addition, measures have been proposed to reduce interest rates. It is expected that fiscal adjustment efforts will enable to reduce substantially the consolidated public deficit from its mid-1990 level of about 5% of GDP.

1.50 Revenue Raising Measures. The Government has proposed measures to raise both tax and non-tax revenues. Among the tax raising measures are: (i) increases in excise taxes pertaining to "sin" products (e.g. tobacco and alcohol) as well as to soft drinks; (ii) increases in taxes on real estate transfers, business registration, and purchases of luxury items; (iii) increases in the business income tax rate and (iv) increases in forestry charges and other fees and charges of selected Government agencies. Of these measures, the increase in excise taxes on tobacco and alcoholic beverages and in certain fees and charges have already been enacted into law. If the full range of measures is passed by Congress, it is expected that annual revenues will increase by about 0.4% of GNP. This would not be additional net revenue,

however, as it would approximately offset the revenue loss from the changes of tax regime on oil products introduced in September 1990. It is thus expected that the Government will announce further measures to raise tax revenues.

1.51 Among non-tax revenue measures are (i) an increase in dividend remittances from public corporations and (ii) an acceleration of the privatization program. As far as the latter is concerned, it is expected that strenuous efforts will be made to meet the 1990 target of offering for sale 50% of the total assets identified for privatization. Among these would be part of the assets of the Development Bank of the Philippines (DBP), Philippine National Bank (PNB), Republic Bank and Union Bank. For DBP the program calls for selling off regional operations to the private sector while, for PNB, the program calls for further sale of shares to the public, following the hugely successful divestment of 30% of shares in 1989. While it is difficult to predict what assets will be successfully sold and at what prices, Government hopes to get an additional 6.5 billion pesos from such operations in 1990 and 1991.

1.52 Reducing Expenditures. The program for reducing expenditures involves cuts in administrative expenses, personnel hiring freezes in most departments (except education, health and revenue collection), a wage and salary freeze for the public sector in 1990 and an 8% cap on increases in the wage bill in 1991 and 1992, and a substantial reduction of capital outlays under the Comprehensive Agrarian Reform Program (CARP). While these measures will cut current spending, other measures have been proposed that will substantially reduce future spending obligations of Government. Of these, potentially the most important is a decision to eliminate the Oil Price Stabilization Fund (OPSF) and to deregulate oil prices. The OPSF has been a major drain on the budget in 1989 and 1990, and while its current deficits will be met by additional appropriations, the Government has announced no further deficits will be permitted to accumulate after July, 1990. Another such measure is a decision to eliminate the fuel oil subsidy provided to the National Power Corporation.

1.53 Interest Rate Reduction Measures. Government intends to follow a two-pronged approach in order to get interest rates down. One prong is sound macroeconomic management featuring the reduction of the deficit and of inflation, as well as the adoption of a more competitive exchange rate policy. The other prong consists of more direct measures to reduce interest rates focussing on the reduction of financial intermediation taxes and increasing competition in the T-Bill auction system. Thus, the gross receipts tax (GRT) and the withholding tax on interbank deposits are both to be eliminated and reserve requirements are to be reduced as soon as monetary conditions are appropriate. While the reduction of financial intermediation taxes will have an adverse impact on fiscal revenues, this is expected to be offset by the positive fiscal impact of reduced interest rates and the longer run impact of a broader and deeper financial system.

1.54 Competition in the T-Bill market is to be increased through the expansion of the dealers network involved in the weekly primary auction of Government securities and through greater involvement of the two large insurance organizations, the SSS and the GSIS, in the T-Bill market. There is

scope for further competition in the T-Bill market. Indeed, when the SSS and GSIS were permitted to place orders through primary dealers recently, T-Bill rates softened considerably over a period of a few weeks. However, it should be noted that the sale of T-bills to these institutions involve some revenue loss for the Treasury since they both have tax-exempt status.

1.55 Exchange Rate Management. A competitive exchange rate policy would have several benefits. First, it would offset the recent appreciation of the real effective exchange rate, thereby restoring trade competitiveness and sustainable external accounts. Second, it would eliminate the premium for devaluation-expectation that is currently built into the domestic interest rate structure; this would help the fiscal adjustment process. Third, it would provide support for further trade reform measures designed to liberalize imports and reduce tariffs. In this respect, the relatively rapid depreciation experienced in recent months indicates a stronger resolve to improve macroeconomic performance through a more appropriate exchange rate stance. Government has also proposed reforms in the exchange rate market to reduce segmentation and lack of competition. This is to be accomplished primarily by expanding the number of participants in the legal exchange rate market through re-opening of off-floor interbank trading and licensing more dealers. In addition to these measures, it will be equally important to maintain fiscal and wage restraint; without such restraint, the benefits of nominal depreciation will be squandered.

D. Aid Utilization

1.56 The tight fiscal situation and the high cost of domestic debt suggest that enhanced access to official sources of external financing would be desirable. Such access would relax the fiscal constraint at a lower cost than the domestic alternative. In recent years, access to official development assistance from abroad has been constrained by the perception of low absorption capacity or an inability to utilize the amount of available financing. This perception is based on the observation that commitments have been rising faster than disbursements, that the average project is taking longer to implement, and that there is a dearth of suitable projects being prepared by Government to be funded from official external sources.

1.57 Determinants of Aid Utilization. The speed and efficiency of project implementation depends not only on unanticipated and uncontrollable factors (such as natural disasters) but also on controllable factors such as the quality of public sector management. Ultimately, improvements in aid utilization will have to come from improvements in the personnel and procedures that govern the flow and use of external finance. As far as procedures are concerned, recent evaluations have identified several aspects that hamper project implementation in the Philippines. Among the more important ones are: delays in the flow of funds to project implementation agencies, lengthy and complicated bidding, contracting, and procurement procedures, and managerial shortcomings.

1.58 Funding Delays. A review by NEDA of the implementation of public investment projects showed that funding delays featured in over 50% of the

cases where implementation was slow relative to schedule. Delays typically occur in the release of funding warrants from the Department of Budget and Management (DBM) to implementing agencies for such reasons as late submission of work and financial plans, late submission of monthly disbursement reports, and slow approval by DBM. Some implementing agencies aggravate the situation by requiring lengthy internal clearance procedures before work plans and disbursement reports are submitted to DBM. Further delays occur as the released funds travel from DBM to the central or regional office of the implementing agency and then further to the province or municipality actually doing the project.

1.59 Bidding, Contracting and Procurement Procedures. The desire to minimize fraud and corruption and to avoid the improprieties that marked the Marcos Administration have led the Aquino Administration to certain unnecessary and undesirable extremes as far as the systems of bidding, contracting and procurement (on public investment projects) are concerned. Overall, the systems in place feature too many levels of clearance and insufficient financial authority at lower levels of Government. For example, until recently, contracts greater than $2 million in value had to be approved by the President after clearance from a variety of Department Secretaries (e.g. DBM, DOF, NEDA). Such procedures have imparted a rigidity which inevitably delays project implementation.

1.60 Management Issues. Many implementing agencies lack the expertise to manage the projects that fall in their portfolio. This is reflected in poor planning, inadequate monitoring, and insufficient ability to redesign in the face of implementation problems. In addition to purely technical weaknesses, the frequency of changes in top management in recent years has seriously affected both morale and performance. For example, there were five changes of Secretary at the Department of Public Works and Highways between 1986 and 1989.

1.61 Aid Utilization Rates. Progress in aid utilization can be measured by a number of different measures. One measure is the number of years it would take to dissipate the existing pipeline at current rates of disbursement. This is essentially given by the ratio of disbursements to the outstanding undisbursed balance. By this measure, aid utilization deteriorated during 1986-88. The disbursement ratio for ODA project assistance declined from 10.6% to 6.8% implying an increase in the pipeline dissipation rate from 8.4 years to 13.77 years (see Table 1.12).

1.62 Table 1.12 reports data for project loans from all sources. Similar data for the above measure of aid utilization are not available for 1989. Disbursements based on IBRD loans only, however, show significant improvement in 1989. Figure 1.8 shows disbursements from IBRD project loans to have risen in 1989 after having fallen during 1986-88. Note that it is important to distinguish between program (BOP support) and project loans; if program loans are included, the profile of disbursements shows continuous improvements since 1986. In any case, it appears that recent measures may have begun to improve the project absorptive capacity of the Philippines.

1.63 Project Implementation Improvement Measures. Some institutional changes were introduced during 1987-89 to improve absorptive capacity. First, a Project Facilitation Committee was formed in 1987 with the objective of improving inter-departmental coordination on projects which cut across departmental lines, organizing teams to do systematic project reviews, setting up better systems to monitor project progress, and identifying implementation problems and solutions. Second, a Cabinet-level committee, called the Committee on Official Development Assistance (CODA), was formed in 1989 to coordinate ODA programming and management. The PFC was absorbed into CODA.

1.64 Several procedural changes have also been introduced. The most important among these are the following: (a) pre-audit requirements were lifted on many transactions of the public sector; (b) departments have been allowed to move funds from slow moving projects to fast moving projects at the discretion of the Departmental management; (c) higher limits were set on authority of Dept Secretaries to approve contracts; (d) it has been made possible for the lowest bid to be accepted even if it comes above approved agency estimates; (e) time limits have been set for the evaluation of bids; (f) "fast track" procedures have been permitted for urgent procurement needs.

Table 1.12: ODA PROJECT ASSISTANCE, 1986-1988
(US$ million)

	1986	1987	1988
Project Pipeline	2707.10	2710.85	3444.83
% of Total Pipeline	90.0%	85.4%	83.2%
Project Disbursements	321.52	308.34	250.11
% of all ODA Loan Disbursements	42.2%	34.5%	27.2%
Project Disbursements as % of previous year's project pipeline plus current year's net new project commitments	10.6%	10.2%	6.8%
Project Disbursement Rate	8.42	8.79	13.77

Source: USAID

1.65 Project Preparation Issues. Project preparation is a problem in that very few projects are being prepared relative to need and keeping in mind the lags between project preparation and implementation. For example, only about one fourth of the projects identified in the Public Investment Program for 1989 had been prepared by the middle of the year.

Fig. 1.8: Disbursement rate IBRD Loans

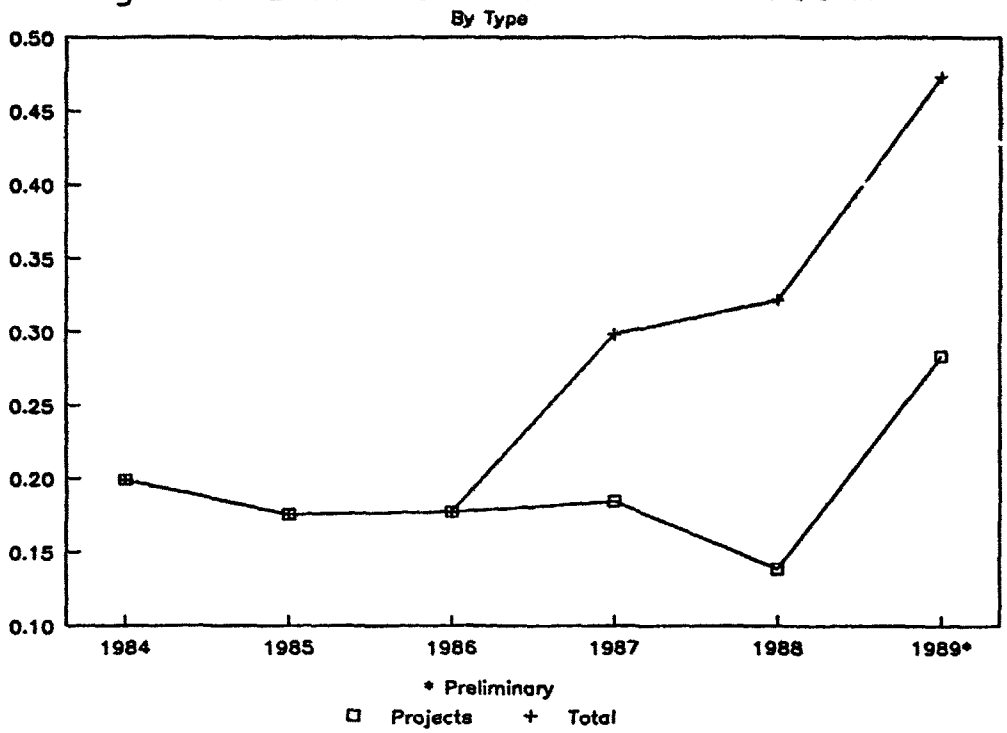
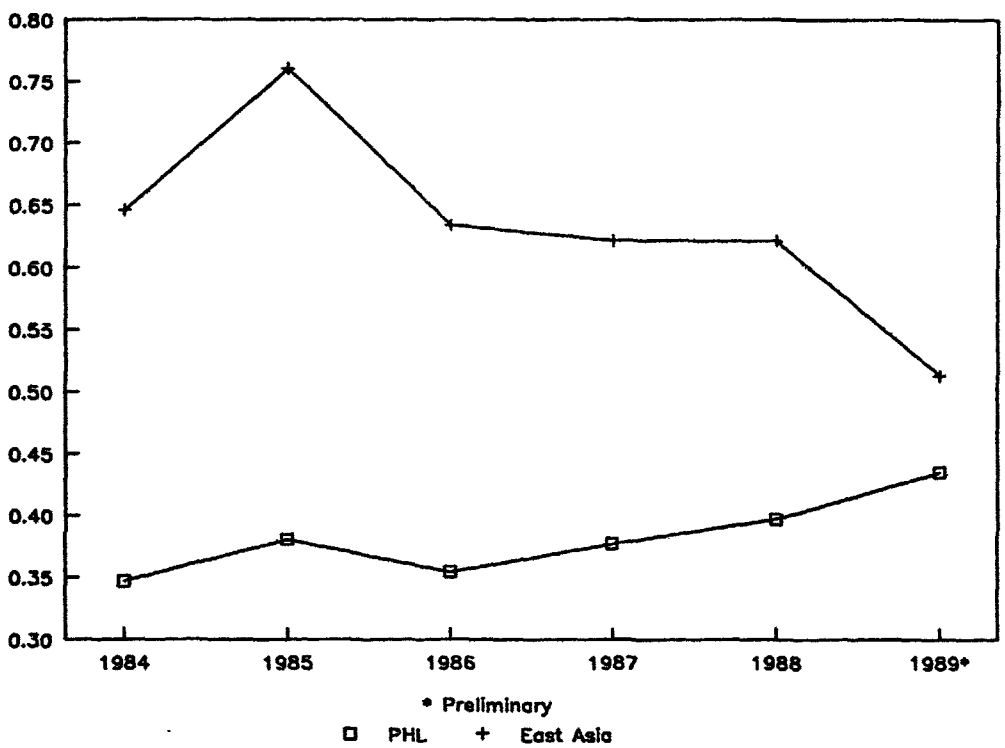


Fig 1.9:Disbursement rate all MLT Loans



1.66 There are several reasons for the inadequacy of project preparation. First, many Departments do not have adequate in-house technical capacity to prepare projects beyond the conceptual stage, i.e. to do feasibility studies. Second, project preparation budgets tend to be too low to generate an adequate flow of projects; for example, only about P20 million has been allocated in recent years by DPWH (the most sophisticated agency in terms of project preparation) in recent years; this amounts to only about 0.025% of DPWH's infrastructure budget. Third, most Departments do not have systematic project preparation procedures; there is a tendency to rely largely on external financing agencies and to initiate preparation largely upon learning of impending donor missions.

1.67 Some improvements have taken place in recent months. The Government allocated P300 million to a feasibility studies fund in 1989 to improve project preparation and almost P256 million of this were actually released during the year as compared to a meager P23 million released in 1988; an additional US$5 million has now been provided to this fund from UNDP.

1.68 Project processing has also improved in 1989. The Investments Coordinating Committee (ICC), which is the chief project approval body, has approved more projects and at a faster rate in 1989 as compared to 1988. Also, guidelines for evaluation and approval have been revised to exclude small projects from taking up the ICCs time. Furthermore, NEDA regional offices have been given greater authority to evaluate and select projects.

1.67 Conclusions. Efforts to improve the utilization of aid appear to have been effective in 1989. Nevertheless, as Figure 1.9 shows, the disbursement rate of the Philippines remains below the average of the East Asian countries. Efforts to improve absorptive capacity must be continued since there remains room for improvement and since the attendant benefits are considerable. Improvements in aid utilization would help current macroeconomic management in at least three ways: first, by getting needed infrastructure built in a timely fashion; second, by saving on loan and commitment costs as funds are disbursed faster; and, third, by encouraging official donors to raise their commitment levels on the evidence of improved absorptive capacity.

II. CAUSES AND CONSEQUENCES OF RISING PUBLIC DEBT

A. Introduction

2.1 The causes and consequences of rising public debt are reviewed and analyzed in this chapter. This issue is important for several reasons. First, the level and financing of the public debt play a central role in explaining the current macroeconomic predicament of the Philippines, a predicament characterized by increases in interest rates, inflation, the current account deficit, and the consolidated public sector deficit. Second, there is a risk that the stabilization achieved by the Philippines since 1985 will be upset by public debt developments. There are many examples of countries that have succeeded in stabilizing the economy for a short period of time only to see macroeconomic imbalances reappear in the medium run.

2.2 Stabilization programs often involve a trade-off between short-term and long-term objectives. Stabilization achieved through debt accumulation, whether domestic or foreign, buys time for structural reforms to be put in place. In the long run, however, a rising stock of debt makes it harder to sustain macroeconomic balance since the servicing of the debt introduces an additional constraint. For countries with large debt stocks to begin with, adjustment via additional debt is usually not viable for long. In the Philippines, the recovery from the recession and crises of 1983-86 was facilitated by the issuance of domestic debt since access to external finance was limited. The breathing space thereby achieved, however, has given way to a renewed need for adjustment as domestic interest rates have risen sharply and debt servicing has become a heavy burden on the budget.

2.3 There are several reasons why domestic interest rates have risen to a level that makes macroeconomic management more difficult. First, there has been an increase in Government demand for credit to finance the public sector deficit. Second, domestic capital markets are thin: they are dominated by only a few large suppliers of credit and the predominant preference is for short-term instruments. Third, increasing current account deficits have raised expectations of faster depreciation, a premium for which has been built into domestic interest rates. Finally, inflationary expectations have risen in the wake of economic and political difficulties in recent years; a premium for this too has entered domestic nominal interest rates.

2.4 The rest of this chapter is organized as follows: Section B discusses the evolution of the current macroeconomic situation in terms of the mix of policies implemented in the 1987-89 period and their outcomes. The adjustment experience of the Philippines is compared and contrasted with that of selected other highly-indebted countries (HICs). Section C examines the main causes and consequences of the increase in the public debt and the costs of financing the debt. Section D discusses policy options being explored by Government to deal with the problem.

B. Macroeconomic Adjustment During 1987-89

The Policy Mix

2.5 During the 1987-1989 recovery, the macroeconomic strategy pursued by the Philippines had four principal objectives: controlling inflation, boosting growth, maintaining external balance, and managing the external debt overhang. Towards these ends, the policy mix combined a prudent fiscal stance by the National Government, conservative monetary growth, external debt reduction schemes and a passive exchange rate policy. The evolution of the policy instruments and outcomes for the period 1985-89 is summarized in Table 2.1.

2.6 Fiscal discipline was a central element in the policy mix. The measures of the budget deficit included in Table 2.1 indicate that by and large the fiscal accounts continued to improve in 1987 and 1988, thus deepening the adjustment started in the aftermath of the debt crisis, but this was followed by some deterioration in 1989. Particularly impressive is the improvement in the primary fiscal balance of the National Government, from a 1.5% of GDP deficit in 1986 to a 2.7% of GDP surplus in 1989. This significant adjustment was, nevertheless, not enough to compensate for an increase in interest payments and persistent deficits of the Central Bank and public corporations. The overall fiscal balance, after improving during 1985-87, has deteriorated in 1988 and 1989.

2.7 Monetary aggregates were allowed to accompany growth in nominal GDP, thus maintaining an adequate level of liquidity to support economic activity (see Table 2.1). The Central Bank expanded the monetary base to increase holdings of international reserves, to finance debt reduction operations and, most importantly, to finance operational losses arising largely from the service on its external debt. In the absence of sterilization, the increases in the monetary base resulting from these transactions would have led to large increases in money supply and inflation. In order to avoid these undesired effects, the Central Bank sterilized part of these increases in the monetary base by issuing Treasury Bills, on behalf of the Treasury, and keeping the proceeds from the sales (in excess of budget deficit financing requirements of the Government) as deposits of the National Government. This operation amounted to a contraction in domestic credit from the Central Bank to the National Government (see Table 2.1). In addition, the Central Bank also maintained a policy of tight domestic credit to the banking system. Such a monetary policy stance was necessary to control monetary growth and hence inflation. At the same time, because this policy resulted in the placement of increasing stocks of T-bills in thin financial markets, interest rates rose, with unfavorable consequences for the fiscal deficit.

Table 2.1: SELECTED MACROECONOMIC INDICATORS AND OUTCOMES, 1985-90

	1985	1986	1987	1988	1989
Instruments:					
1. Fiscal Policy					
a. Fiscal Deficit/GDP	1.8	5.0	2.8	2.8	2.0
b. Primary Deficit/GDP (- surplus)	-0.6	1.5	-1.9	-2.1	-2.7
c. Consol. Deficit/GDP	5.9	4.8	2.7	3.1	4.0
2. Monetary Policy					
a. Monetary Base (%)	14.1	31.0	13.8	16.3	35.2
b. M1 Growth (%)	6.4	19.2	22.8	13.7	30.7
c. Net Domestic Credit (%)	11.4	-19.5	-54.3	-74.8	-96.3
3. Devaluation (%)	11.4	9.6	0.9	2.6	3.0
Outcomes:					
1. GDP Growth (%)	-4.3	1.4	4.6	6.4	5.6
Nominal GDP Growth	13.3	2.4	13.0	16.6	16.7
2. Investment/GDP	12.4	11.1	14.2	15.7	17.1
3. Treasury Bill Rate (% per annum)	27.0	16.0	13.0	15.7	19.7
4. Inflation (%)	23.1	0.8	3.8	8.8	10.6
5. M1/GDP	5.8	6.8	7.4	7.2	8.4
6. M3/GDP	22.0	24.3	24.0	25.3	23.6
7. Real Exchange Rate (1985=100)	100.0	78.0	71.8	69.8	73.8
8. Domestic Debt (% of GDP)	19.0	23.0	22.8	25.1	24.6
9. Current Account Deficit (% of GDP)	-0.1	3.2	-1.4	-1.0	-3.5
10. Resource Balance (% of GDP)	6.0	8.5	3.4	0.0	-1.9
11. Net Long-term Capital (Bill. US$)	3.1	1.3	0.6	0.0	1.0
12. International Reserves (Bill. US$)	1.1	2.5	2.0	2.1	2.3
13. Foreign Debt (% of GDP)	80.6	92.2	88.5	74.5	68.7
14. Real Exchange Rate (Competitors)	100.0	93.1	94.0	98.7	105.1

2.8 The third element in the strategy were policies to reduce the burden of external debt. Three successive agreements with Paris Club creditors--in 1984, 1986 and 1989--and two with commercial banks--in 1985 and 1987--resulted in postponing the bulk of repayments to after 1992 and in limited repricing of outstanding debt. In 1986, several mechanisms for the reduction of the stock of external debt were put in place, including debt/equity, debt/debt, debt/assets conversion programs. Between their introduction and end-89, debt/equity swaps retired US$0.8 billion of foreign debt, and debt/debt and debt/assets swaps about US$1.3 billion. A new financing agreement with the commercial creditors led to a concerted buyback operation in January 1990, that retired US$1.3 billion of commercial debt at 50% discount. The total foreign commercial debt retired to date can thus be estimated at approximately US$3.4 billion.

2.9 Finally, after the devaluation of 1986, exchange rate policy has been largely passive, characterized by a moderate nominal depreciation of the peso against the U.S. dollar. In part, the stability of the exchange rate helped to control inflation, and in part to control the fiscal deficit (since a devaluation increases the cost of servicing external debt). The trade-weighted real exchange rate depreciated in 1987 and 1988; this trend was

reversed in 1989, however, when there was a small real appreciation. The competitor-weighted real exchange rate--based on a narrow group of competing countries (see Table 2.1, line 14)--has appreciated steadily since 1986, however.

2.10 The Philippine policy mix shares common elements with that of the more successful adjusters within the highly-indebted countries. Although the size of the initial reduction in the budget deficit looks small when compared to other adjusting countries, such as Chile, Mexico or Morocco, the initial fiscal imbalance was also smaller in the Philippines. In addition, since the size of the Government bureaucracy remains small compared with countries elsewhere the reductions in Government expenditure were also smaller. Mexico, for instance, cut its non-interest expenditures by 9 percentage points of GDP between 1982 and 1986 and the operational deficit fell by 5 percentage points to 3.3% of GDP. The Philippines, on the other hand, was able to bring down the budget deficit to a similar level with small reductions in non-interest expenditures (the main cuts were in public investment and subsidies). A policy of tight domestic credit was also followed in Mexico, although the Philippines was more effective in the sense that inflation has remained low since the mid-eighties. Finally, although exchange rate policy was less aggressive than in other HICs, the Philippines succeeded in achieving and sustaining a real depreciation--relative to prior to the debt crisis--similar to that of other HICs. In summary, relative to other highly-indebted countries, the Philippines relied less on exchange rate depreciation and fiscal cuts and more on tight credit to achieve its inflation and external balance objectives.

Outcomes

2.11 The policy mix discussed above has been successful in restoring growth, fostering investment, controlling inflation, and improving external debt indicators, from 1986 onward, and it is perhaps one of the best among highly indebted countries on these four counts. There are signs, however, that this performance cannot be sustained over the medium-term: internal debt and the associated interest payments are mounting, putting pressure on interest rates and inflation, and the current account deficit, if it persists, will be increasingly difficult to finance.

2.12 Philippine adjustment in the aftermath of the debt crisis was remarkable in many respects. Table 2.2 summarizes the macroeconomic performance of four HICs after the debt crisis. The initial adjustment (1983-84) in the Philippines was very drastic and, as a result, the economy suffered negative growth and low investment levels. This was not unusual among HICs, but the depth of the initial recession and the size of the fall in investment was somewhat larger in the Philippines than in other countries. Nevertheless, growth and investment recovered in 1986-89, and the overall performance during this period has been comparable with that of the most successful HICs during this period. Philippine export performance has also been strong among HICs; this was facilitated by the real depreciation in the mid-eighties and the macroeconomic stability experienced during the period. As other HICs, the Philippines was effective in sustaining a real depreciation throughout the post-1982 period (although there was a reversal in 1989). In contrast to

Table 2.2: COMPARATIVE ADJUSTMENT PERFORMANCE

	1980	1981	1982	1983	1984	1985	1986	1987	1988
1. GDP GROWTH (%)									
Philippines	5.2	3.9	2.9	0.9	-6.0	-4.4	1.5	4.6	6.4
Brazil	9.3	-4.3	0.7	-3.4	5.1	8.3	7.5	3.6	-0.3
Chile	7.8	5.6	-14.2	-0.7	6.3	2.4	5.6	5.7	7.4
Mexico	8.4	8.8	-0.6	-4.2	3.6	2.6	-3.8	1.5	1.1
2. EXPORT GROWTH (%)									
Philippines	12.7	1.1	-1.1	9.0	8.3	-7.4	21.8	-1.3	15.7
Brazil	22.7	21.3	-9.2	14.3	22.1	6.9	-10.2	5.3	20.6
Chile	14.3	-9.0	4.7	0.6	6.8	6.9	9.8	8.8	6.1
Mexico	6.1	11.6	21.8	13.6	5.7	-4.4	3.2	9.8	2.0
3. DOMESTIC INVESTMENT/GDP									
Philippines	30.7	30.6	28.3	26.7	17.0	13.9	12.9	15.6	17.3
Brazil	22.9	21.1	20.0	14.7	15.5	16.7	18.5	22.2	23.1
Chile	21.0	22.7	11.3	9.8	13.6	13.7	14.6	16.9	17.0
Mexico	27.2	27.4	22.9	20.8	19.9	21.9	18.4	18.6	20.3
4. CURRENT ACCOUNT DEFICIT (% OF GDP)									
Philippines	-5.4	-5.3	-8.0	-8.0	-3.4	-0.3	3.1	-1.3	-1.0
Brazil	-5.4	-4.5	-6.0	-3.3	0.0	-0.1	-1.6	-0.5	1.3
Chile	-7.3	-14.7	-9.7	-5.9	-9.5	-8.4	-7.0	-4.6	-1.3
Mexico	-5.5	-6.4	-3.7	3.6	2.3	0.2	-1.4	2.6	-1.7
5. FISCAL DEFICIT (% OF GDP)									
Philippines	-1.3	-4.0	-4.2	-1.9	-1.9	-1.8	-5.0	-2.8	-2.8
Brazil (Operational)	-0.7	-5.6	-8.0	-4.8	-2.7	-4.3	-3.6	-5.5	-4.3
Chile	5.4	2.6	-1.0	-2.6	-3.0	-2.4	1.0	-0.1	-0.7
Mexico	-3.0	-6.4	-14.8	-7.6	-7.1	-8.4	-13.1	-9.4	-9.6
6. TOTAL EXTERNAL DEBT/GDP									
Philippines	49.4	54.0	61.3	70.3	74.9	80.9	92.2	87.4	75.1
Brazil	29.6	30.6	33.9	47.2	49.4	45.7	40.0	40.9	32.3
Chile	43.8	48.0	71.1	90.7	102.8	127.4	125.7	113.5	89.0
Mexico	29.5	31.3	49.5	62.4	54.0	52.5	77.7	77.4	57.5
7. REAL EXCHANGE RATE (1980=100)									
Philippines	100.0	103.2	107.1	90.1	89.2	97.6	76.2	70.1	68.2
Brazil	100.0	121.4	128.4	104.2	104.2	100.4	94.4	95.0	102.6
Chile	100.0	118.0	106.7	86.9	85.3	68.9	58.2	54.0	50.5
Mexico	100.0	113.6	81.6	71.7	83.8	86.3	60.4	55.6	68.6
8. IMPLICIT GDP DEFLATOR (%)									
Philippines	15.6	11.1	8.4	11.5	50.2	23.1	0.8	3.8	8.8
Brazil	90.7	103.2	97.4	152.7	212.1	235.2	150.9	199.7	684.6
Chile	29.1	12.2	13.5	26.6	14.3	32.9	19.3	21.2	21.1
Mexico	26.7	26.0	60.9	90.5	59.1	56.7	74.3	139.3	103.8

other HICs, this was achieved without experiencing a permanent increase in inflation (as was the case in most Latin American countries, even in the successful ones).

2.13 The Philippines has also succeeded in managing its external resource transfer and staying current in interest payments on external debt. The ratio of external debt to GDP has declined from its peak in 1986 of 92% to 68% in 1989; the ratio of debt to exports has also declined by about 28% during the same period. While the Philippines is still far from returning to commercial creditworthiness, the progress achieved in this area should not be overlooked. Its performance has been stronger than the average for middle income HICs, which, as a group, experienced a more limited improvement of their external debt indicators.

2.14 After three years of strong growth, the Philippine economy is entering a critical phase. In the absence of policy changes a reversal in performance is a distinct possibility. Its origin is the significant rise in domestic debt and debt servicing costs that has accompanied the adjustment effort. Domestic debt rose by almost 40% in real terms between 1985 and 1989 (from around 19% to around 25% of GDP). The cost of servicing this debt rose even more dramatically from 1.7% of GDP in 1985 to 4.4% in 1989. Since then, Treasury Bill rates have been hovering at around 25% in nominal terms (or around 12% in real terms); holding other factors constant, this implies a further increase in the cost of servicing domestic debt of over 1.5% of GDP relative to 1989. The situation is potentially destabilizing as higher domestic debt will lead to larger deficits, higher interest rates, and even higher domestic debt. This vicious cycle needs to be stopped quickly if the country is to avoid a resurgence of macroeconomic instability of the type experienced at the outset of the external debt crisis.

C. Rising Domestic Debt

Causes of Rising Domestic Debt

2.15 Domestic debt in the Philippines was issued to finance the following items: (i) large public sector borrowing requirements, (ii) accumulation of international reserves, and (iii) debt reduction operations. Table 2.3 shows the relative importance of each of these factors during the period 1986-1989.

2.16 Table 2.3 indicates that large deficits in the consolidated public sector accounts have been the most important reason for the rise in domestic debt. Reserve accumulation was very important in 1986 but has since been a minor factor. External debt reduction operations increased debt accumulation in 1988, when debt-equity swaps reached their peak, but have been unimportant in other years. On the financing side, available foreign borrowing, although positive on average, has contributed less than either monetary base creation or domestic debt accumulation. Monetary base growth has been moderate until the exception of 1989. The remaining source of financing, domestic debt, has been the largest each year.

Table 2.3: EXPLAINING THE RISE IN DOMESTIC DEBT
(billion pesos, current prices)

	1986	1987	1988	1989
Uses				
Consolidated Public Sector Deficit	29.6	18.6	25.0	42.7
Foreign Reserve Accumulation	25.8	-5.1	2.1	5.8
Debt Reduction Operations	.3	5.5	13.4	3.9
Financing				
Change in Foreign Debt	10.0	-.3	5.0	13.4
Change in Monetary Base	12.9	7.2	9.7	24.3
Change in Domestic Debt	32.8	12.1	25.8	14.7
Memo Items				
Change in Domestic Debt from Stock Statistics	13.1	25.5	35.8	--
Stock of Domestic Debt 1/ 2/	94.8	120.3	156.1	--

1/ Net of Government deposits with the banking system.
2/ Central Bank data on holders of publicly issued securities; note that debt numbers differ slightly across different sources of information.

2.17 Policies aimed at controlling debt accumulation will have to concentrate primarily on improving the fiscal accounts. In addition, while there is a need for increasing official reserves and further DDSR operations, targets must be set so that these can be financed with external resources and thus do not further increase domestic debt. Strong fiscal adjustment is required because of the absence of viable financing options: the excessive monetization that occurred in 1989 needs to be stopped in order to lessen inflationary pressures while the availability of foreign financing remains limited.

2.18 A closer look at the consolidated public sector accounts is provided in Table 2.4 which shows that each of three major components, namely the National Government, public sector enterprises and the Central Bank, contributes significantly to the consolidated fiscal deficit. Despite rising primary surpluses, the National Government's overall accounts remain in deficit and make up almost half of the consolidated deficit. Similarly, while the deficit of public corporations declined to 1988, it has risen in 1989; moreover, if all transfers from the National Government to public corporations were factored in, the deficit of the latter would be higher. Finally, the operating deficits of the Central Bank have been rising since 1987 and are currently about as large as those of the National Government.

Table 2.4: CONSOLIDATED PUBLIC SECTOR DEFICIT
(Share of GDP, Percent)

	1985	1986	1987	1988	1989
Central Bank	-2.5	-2.9	-1.5	-2.0	-2.2
National Government	-1.8	-5.0	-2.8	-2.8	-2.0
Monitored Corporations	-1.3	-1.1	-0.5	0.3	-0.4
Other 1/	2.8	6.1	0.2	0.3	0.3
Consolidated Deficit	-5.9	-4.8	-2.7	-3.1	-4.0
Memo Items:					
Primary Balance (- = Deficit)	0.6	-1.5	1.9	2.1	2.7
Debt/GDP	19.0	23.0	22.8	25.1	24.6

1/ Includes social security, local Governments, and adjustments of transfers from the National Government to GFIs and monitored corporations. The latter is necessary to avoid double counting.

Source: Department of Budget and Management

2.19 The main reason why the deficit of the National Government has persisted despite substantial improvements in revenue collection and significant reductions in non-interest expenditures is the increase in interest payments occasioned by rising domestic and international interest rates. Indeed, this is also the main reason why the deficit of the Central Bank has continued to rise. The increasing bite of interest payments is shown in Table 2.5. Interest payments by the National Government rose from 18.3% of total expenditures in 1985 to almost 34% in 1988; they are expected to reach up to 36% in 1990. Interest payments by the Central Bank have also been rising sharply, from about 7 billion pesos in 1985 to about 27 billion pesos in 1989. Indeed, net interest losses account for virtually all of the net losses of the Central Bank currently, as opposed to being a small fraction in 1985 (when losses from foreign exchange exposure were more significant). The importance of interest payments to the present fiscal situation can also be illustrated by the fact that the domestic interest payments of the National Government alone are larger than the consolidated fiscal deficit in 1988 and 1989.

Table 2.5: INTEREST PAYMENT TRENDS
(billion pesos)

	1985	1986	1987	1988	1989
National Government					
Interest Payments	14.7	21.0	36.9	45.9	54.6
On Domestic Debt	10.5	15.2	24.3	32.2	41.0
On Foreign Debt	4.2	5.8	12.6	13.7	13.6
Interest/Total Exp.(%)	18.3	19.1	30.8	33.7	31.8
Interest/GDP (%)	2.4	3.3	5.2	5.6	5.7
Domestic/GDP	1.7	2.4	3.4	3.9	4.3
Foreign/GDP	0.7	0.9	1.8	1.7	1.4
Central Bank					
Interest Payments (P billion)	7.2	27.2	18.3	23.2	26.9
On Domestic Liabilities	0.7	11.2	4.8	8.5	10.7
on Foreign Liabilities	6.5	16.0	13.5	14.7	16.2
Net Interest/Total Net Income (%)		102	94	96	96
Memo Items					
Nominal T Bill Rates	27.0	16.0	13.0	15.7	19.7
Real T Bill Rates	4.0	15.0	9.2	6.9	9.1

Source: Department of Budget and Management and Central Bank

Causes of High Interest Rates

2.20 The rise in the real stock of public debt has been accompanied in recent years by rising interest rates. For most of the period since 1986, inflation rose pari-passu with nominal interest rates. Thus, real interest rates did not show an upward pattern. This tendency, however, shows a break towards the end of 1989 as real and nominal interests rates went up significantly; a trend that continued throughout the first half of 1990.

2.21 It is useful to bear in mind that high real interest rates are a phenomenon observed across highly indebted countries and that they largely reflect the scarcity of capital in the aftermath of the debt crisis. Real interest rates in the Philippines have hovered between 6 and 8% in recent years; this is roughly twice the real rate on LIBOR, but still lower than the rates of other HICs (such as Argentina, Brazil and Mexico). The increase in late 1989, however, marks a break with the previous trend. The rise in interest rates has been dramatic, with T-bill rates reaching around 29% in recent months, and is a reflection of the accelerating deterioration of macroeconomic balances.

2.22 Three factors are at the root of the more recent rise in interest rates. First, and most obvious, is the increase in domestic debt. In order to place larger stocks of domestic debt the Government had to offer more

attractive rates of return. Indeed, in recent months, the interest rate on T-bills has increased more than interest rates on alternative financial instruments, and it is now higher than the prime rate charged by some banks. Second, the rise in inflation that has been taking place since 1985 could continue in the future. This puts upward pressure on nominal interest rates as people try to maintain the same real returns on domestic assets. Third, the increasing current account deficits (reaching 3.5% of GDP in 1989) are making it more likely that the Central Bank would follow an aggressive exchange rate policy. If the Central Bank maintains its current exchange rate policy and the policy is not fully believed by the private sector (i.e. they continue to expect a devaluation), high interest rates will be unavoidable. In fact, the large degree of substitutability between foreign and domestic assets in the Philippines means that a higher interest rate has to be offered in order to keep funds in domestic assets. Otherwise, financial capital would flow out of the country on expectations that a higher rate of return can be obtained abroad. This is the problem that Mexico has faced for the last two years, as it adhered to a crawling peg exchange rate policy and avoided devaluation in excess of a pre-announced target because of concerns about rekindling inflation. The cost in Mexico has been extremely high real interest rates, a protracted fiscal problem, and low investment and growth.

Consequences of Rising Public Debt

2.23 Macroeconomic Management. The main problem arising from the present trend in domestic debt and interest rates is that it makes macroeconomic management more difficult. In the absence of corrective measures the possibility exists of a resurgence of inflation and other manifestations of macroeconomic instability similar to the situation faced by the Philippines in the earlier part of this decade.

2.24 While the size of the Philippine domestic debt is not large when compared with many other countries, it is large relative to the domestic capacity for financing. Malaysia, for example, has lived with a domestic debt to GDP ratio of around 70% for several years. This has not posed major problems for macroeconomic management and performance for four reasons: first, Malaysia has comfortable access to foreign financing; second, it has a much larger financial system with a relatively developed capital market in which the Government can borrow without pushing interest rates up; third, it has a high yield public revenue system; and, fourth, its rate of private savings is relatively high. The problems are more severe in those developing countries that are already overburdened by large external debt and where domestic financial markets are thin and access to foreign finance is limited. This has been the case in both Brazil and Mexico, where domestic debt to GDP ratios of around 20% of GDP have created major problems for macroeconomic management.

Table 2.6: DEBT CARRYING CAPACITY: MALAYSIA AND PHILIPPINES (1989)

	Malaysia	Philippines
Ratio to GNP (%)		
Public Savings	9.4	0.3
Revenues	25.8	15.8
Private Savings	19.4	15.0
M 3	60	19
Stock Market Capitalization	67	33
External Debt	26.6	68.7
Domestic Debt	70.5	18.0
Memo Items		
Real Lending Rate	4.0	8.3
Real T-Bill Rate	-.-	9.0
Foreign Investment (US$ billion)	1.5	0.4

2.25 In Mexico, for instance, because of high real interest rates the cost of servicing domestic debt was around 6% of GDP in 1988 and 1989; this made it very difficult to maintain the small budget deficits needed to maintain low inflation. In Brazil, large interest payments were compounded by the extremely short maturity of domestic debt. This became an issue early this year when, on the verge of hyperinflation, the Central Bank had to refinance almost its entire domestic debt on a daily basis. [1]

2.26 The situation is made more difficult by the fact that most of the Philippines' domestic debt is of short maturity. This limits the power of monetary policy to fight inflation because it shortens the lag with which tight money increases the average interest rate on outstanding debt. In addition, since the domestic debt service is growing faster than revenue increases, the fight against inflation is more difficult. In such a situation investors must expect the authorities to sooner or later resort to expansionary domestic credit policies and inflate their way out of the problem. This expectation complicates matters because it gets built into the domestic inflation and interest rate structure.

1/ The macroeconomic problems and strategies of Mexico and Brazil are discussed in recent Bank Country Economic Memoranda for these countries.

Table 2.7: DOMESTIC DEBT AND REAL INTEREST RATES

	1988		1989	
	Domestic Debt (% of GDP)	Real Interest (%)	Domestic Debt (% of GDP)	Real Interest (%)
Philippines	18.9	6.9	18.0	9.1
Mexico 1/	23.3	20.6	22.3	29.2
Brazil	19.5	5.4	28.0	27.7

1/ Average annual interest rate on 91-day Treasury Bills.

Sources: Philippine Financial Statistics; Banco de Mexico; Brazil Country Economic Memorandum, 1990; and IFS.

2.27 Projections based on a scenario in which the Philippines does not tackle the consolidated budget deficit of the public sector are shown in table 2.8. Underlying this scenario are the assumptions that: (i) no increase in the revenue effort takes place, so that both tax revenues and revenues from the privatization program remain at their 1989 level, as a percentage of GDP; (ii) current expenditures are maintained at their 1989 level with the exception of OPSF subsidies, which rise starting in 1990; (iii) capital expenditure is maintained at its 1989 level; (iv) GDP growth averages 4-4.5% per year, as appears to be consistent with the failure to increase public investment to the level necessary to improve basic infrastructure; and (v) real interest rates stabilizes around 10%.

2.28 Under these assumptions, between 1990 and 1995 the consolidated public sector deficit increases from 5.1% to 6.8% of GDP, while the primary balance remains in surplus at about 2.6%. Domestic public debt necessary to finance the fiscal deficit rises gradually from around 25% to around 34% of GDP; this feeds back into interest payments which increase from 4.3% to 5.9% of GDP due to the increase in domestic debt alone, as the real interest rate is assumed to be constant throughout the period.

2.29 The first major implication of this scenario is that a substantial improvement in the primary balance of the public sector is necessary to break this vicious circle; that is, the Government will have to continue increasing its primary surplus to finance interest payments on domestic debt. Since the rate of growth of GDP is smaller that the real interest rate, in the absence of this effort the budget deficit will be larger in the future, thus making more difficult the sustainability of low inflation. The second major implication is that, if the fiscal adjustment is delayed, the increase in the stock of domestic debt will most likely result in higher real interest rates, and will thus deter investment and threaten the sustainability of long run growth.

Table 2.8: POLICY INERTIA SCENARIO
(Share of GDP, per cent)

INERTIA	1988	1989	1990	1991	1992	1993	1994	1995
CONSOLIDATED PUBLIC SECTOR 1/								
Total Revenues	19.6	20.8	21.2	21.1	21.0	21.0	21.0	20.9
Total Current Expenditures	19.6	21.7	23.3	23.2	23.5	23.6	23.6	23.6
Expenditures excld. Interest	11.2	13.1	13.7	13.7	13.7	13.7	13.7	13.7
Interest Payments	8.4	8.6	9.6	9.5	9.8	9.9	9.9	9.9
Domestic Debt	4.2	4.5	4.7	4.6	4.9	5.2	5.6	5.9
Foreign Debt	4.1	4.1	4.9	4.9	4.9	4.7	4.3	4.0
Capital Expenditures	3.0	4.1	4.1	4.1	4.1	4.1	4.1	4.1
Cons'd Public Sector Balance 2/	-3.0	-5.1	-6.3	-6.2	-6.6	-6.7	-6.8	-6.8
Primary Balance	4.9	3.0	2.6	2.6	2.6	2.6	2.6	2.5
Net Interest Bills	-7.9	-8.1	-9.0	-8.9	-9.2	-9.3	-9.3	-9.3
Domestic Debt	-3.8	-4.1	-4.2	-4.2	-4.4	-4.8	-5.2	-5.5
Foreign Debt	-4.0	-4.0	-4.8	-4.7	-4.7	-4.5	-4.2	-3.8
DEBT STOCKS								
Domestic Public Debt	22.8	22.6	25.4	26.7	28.2	30.3	32.0	33.6
Foreign Public Debt	63.3	59.1	64.8	64.7	64.6	62.0	59.3	56.0

1/ Including National Government, Local Government Units, Central Bank, and Non-Financial Public Corporations; excluding Government Financial Institutions.

2/ If Governemnt Financial Institutions are included, the consolidated public sector deficit in 1989 is 4.2% of GDP instead of 5.1.

Source: Staff Calculations

2.30 Other Consequences. In addition to making macroeconomic management more difficult, rising public debt in the Philippines has a number of undesirable monetary and fiscal consequences. On the monetary side, two effects are becoming noticeable. The first is the crowding out of the private sector, resulting from rising interest rates and limited access to foreign borrowing; the second is a growing reliance of commercial banks on income from Government securities. The increase in interest rates has already been documented and its link with the rising public debt shown (see Table 2.5). It is estimated that, if domestic debt were at the same level as in 1986, real interest rates would be 2 points lower than current levels.

2.31 Crowding Out of the Private Sector. It should be noted that the full effect of crowding out may not have been felt in recent years because of the existence of excess capacity in the economy. Now that excess capacity has been sharply reduced and capacity expansion is becoming critical, the required investment is likely to be substantially curtailed by a burgeoning Government borrowing program. This is not to say that private investment has not grown substantially in recent years. What should be borne in mind is that the growth has been from a very depressed level and could have been even higher were it not for the relatively tight credit and high interest rates that have been prevalent, especially in 1989. Furthermore, to the extent that a higher level of private investment would have added to productive capacity whereas Government borrowing has not significantly added to such capacity (i.e. public investment has been curtailed in recent years as a share of GNP and as a share of total expenditures), there has clearly been some loss of medium-term growth opportunity.

2.32 The crowding out phenomenon also affects the prospects for direct foreign investments as well as for the privatization program. In an environment of high interest rates, the return on financial assets is typically higher than the return on physical assets. Therefore, Government will find it difficult to entice investors to buy assets marked for privatization unless special incentives are offered. Even if investors were found, they would inevitably face difficulties in raising loans that are required to restructure most Government companies.

2.33 Shifts in Bank Asset Portfolios. The high yield and low risk of Government securities is attractive to banks and large institutional investors (such as pension funds). Since 1983, commercial banks' holdings of Government securities have risen from P3.8 billion to P18.5 billion or from 1.7% to 6.2% of total assets (see Table 2.9). An even clearer indication of the role played by Government securities in the activities of commercial banks is the fact that commercial banks' income from such securities rose from only 0.3% of total income in 1983 to 15.2% in 1988. This shift in portfolio preferences towards Government securities is discomforting to the extent that it reflects a shift away from the normal business of commercial banks, which is lending to the private sector in support of investment. It is legitimate to speculate whether such a large shift in the portfolio composition of commercial bank assets is good for the long-run development of the economy. If such a shift continues at present rates, there is a danger that the financial intermediation function of the commercial banking system may atrophy.

2.34 There is an irony in the monetary consequences of the rising public debt. On the one hand, the role of the Government in the economy is being reduced via privatization and nationalization of public corporations. On the other hand, the rising public debt has led to a situation where the Government is becoming more and more important to the investment decisions of the private sector because of the size and the composition of its deficit.

Table 2.9: GOVERNMENT SECURITIES HOLDINGS OF COMMERCIAL BANKS, 1983-88 1/
(in billion Pesos)

	1983	1984	1985	1986	1987	1988
Total Assets	223.4	272.7	275.7	227.7	247.9	299.8
Investments in Government Securities	3.8	8.3	8.8	12.2	13.3	18.5
% to Total Assets	1.7	3.0	3.2	5.4	5.4	6.2
Total Income	28.9	39.0	36.1	28.5	29.8	31.0
Interest from Trading Govt. Securities	0.1	0.4	3.6	3.5	4.1	4.7
% to Total Income	0.3	1.0	10.0	12.3	13.8	15.2

1/ These data do not reflect recent changes in coverage of commercial banks.

Source: Central Bank

2.35 Development Consequences. The rising burden of debt service also has strong consequences for fiscal priorities. A telling indicator of the changes brought about by a rising public debt burden is to be found in the composition of budget expenditures: during 1983-89, the proportion of expenditures devoted to debt service rose from 15% to around 44%, whereas the proportion devoted to economic and social development expenditures dropped from 53% to 37% (see Table 2.10). During the same period, capital expenditures have dropped from 27% to 14% of total expenditures. For several years now debt service has been the single largest component of Government expenditures. This change in the composition of expenditures has implications for both growth and income distribution. Long-run economic growth is restricted to the extent that expenditures are directed away from much needed infrastructure investments.

Table 2.10: SECTOR ALLOCATION OF GOVERNMENT EXPENDITURES

	1983	1985	1987	1988	1989 1/
Economic Services	32	23	16	16	21
Social Services	21	17	16	19	16
Defense	14	12	8	11	9
Other 2/	18	26	15	12	10
Debt Service 3/	15	22	45	43	43
Total	100	100	100	100	100

1/ Preliminary data.
2/ Includes net lending and general public services.
3/ Includes interest payments and amortization of domestic and foreign debt.

2.36 An increase in debt service obligations typically generates pressure to raise additional revenues and/or to reduce other items of expenditure in the national budget. Often, indirect taxes are raised so as to generate additional revenues quickly, and development expenditures are reduced since the political pressure to maintain current and defence expenditures is usually stronger. In the case of the Philippines, this pattern of adjustment may also be discerned. As already noted, expenditures on economic and social services have dropped since 1983 and particularly sharply since 1986. On the revenue side, the ratio of indirect taxes to total taxes has remained at a relatively high 70% for many years and recently, proposals have been advanced to raise tax rates on "sin" products (e.g. tobacco, alcohol). The reason why this pattern of adjustment should be a matter of concern is because it is regressive in its income distribution effects: lower income people pay a proportionately larger share of their income as indirect taxes and receive a larger share of development expenditures, especially social expenditures.

D. Revised Adjustment Strategy

2.37 The rising public debt poses a challenge to Government. On the fiscal side, existing obligations have to be serviced while at the same time development expenditures have to be raised so as not to hobble growth and exacerbate poverty. On the monetary side, the deficit that is fed in large part by the rising debt has to be financed while keeping interest rates and inflation under control and avoiding excessive distortion of the financial intermediation process. Recognizing the gravity of the problem, Government has recently proposed a revised macroeconomic program in which fiscal adjustment is the main objective to be supported by complementary monetary and exchange rate policies (see Chapter 1, Section C for details).

2.38 Fiscal Policy. A reduction in the deficit of the consolidated public sector is the most important element for restoring macroeconomic balance. It

will help on three counts. First, it will reduce the public sector borrowing requirements and thereby retard the increase in domestic debt. Second, it will contribute to a reduction of domestic interest rates. Third, the resulting fall in domestic absorption will help to improve the current account. Finally, by restraining aggregate demand it will help to control inflation. In this regard, the priority given by Government to reducing the consolidated public deficit is quite appropriate.

2.39 The proposed fiscal effort contains both measures to increase revenues as well as to reduce expenditures. The expenditure reduction proposals seek to cut personnel expenditures and to maintain capital expenditures except as related to the CARP. This is a sensible approach since generalized reductions in capital outlays affect long term growth prospects. Fiscal adjustment to date has featured relatively large cuts (in real terms) in capital outlays, to the detriment of the country's infrastructure and growth potential. Additional external financing could play a facilitating role in this area as it provides the needed breathing space until public savings can be increased to the necessary level.

2.40 Interest Rate Reduction Measures. Interest rate reductions would help the fiscal adjustment process tremendously. Such reductions can be achieved through policies to reduce inflation and to maintain a competitive exchange rate as well as by direct measures focussing on the reduction of financial intermediation taxes and increasing competition in the T-Bill auction system. In this regard, there is considerable merit in Government proposals to eliminate the gross receipts tax (GRT) and the withholding tax on interbank deposits and to lower reserve requirements as soon as monetary conditions are appropriate. Similarly, there is merit in Government proposals to increase competition in the T-bill market by expanding the dealers network and permitting greater participation in this market by the two large public insurance organizations, the Social Security System (SSS) and the Government Service Insurance System (GSIS). With regard to potential purchases by these public insurance organizations, it should be noted that their tax-exempt status deprives the Government of some revenues from T-bill sales; whether the net fiscal effect is positive or negative will be ascertained from experience.

2.41 In addition to improving auction procedures, however, Government should consider making T-Bills attractive to a wider group of investors, including small investors. A wider and deeper pool of potential investors would help reduce interest rates as well as lengthen maturities. One way to increase the access of smaller private investors is to further encourage the formation of unit trust accounts which invest exclusively in Government securities. This would ensure that small savers had better access to the T-bill market, without the administrative complexity and cost of issuing small denomination T-bill series.

2.42 Another way of tapping a larger market for T-bills is to remove the element of exchange rate risk from such instruments by indexing the T-bill rate to the peso-dollar exchange rate or by issuing dollar-denominated bills. This would make such instruments more attractive both to domestic and to foreign investors, thereby enabling a larger client base and better rates. While the market-oriented auction procedure for T-bills effectively builds in

the expected exchange rate depreciation into the peso-denominated rate, a rate advantage can be derived in issuing foreign-exchange-linked instruments from the difference in risk aversion between ordinary investors and the Government itself. Ordinary investors typically require a greater premium than the expected depreciation rate on account of being risk averse. There is no reason why a less risk averse Government should pay this. Another advantage of indexation is that it is a precondition for the development of a longer maturity mix of Government securities in a potentially inflationary economy like the Philippines. Over the long run, the exchange rate must reflect domestic versus foreign inflation differentials; hence, the index provides a hedge against future inflation. It should be emphasized, however, that successful use of foreign-exchange-linked securities requires the restoration and maintenance of the exchange rate at a level consistent with medium-run balance of payments equilibrium.

2.43 Monetary Policy. Reliance on fiscal policy alone is unlikely to be sufficient to restore macroeconomic stability. Monetary policy has a role to play also, but it should take into account the fact that the cost of reducing inflation could be very high in the present environment of high interest rates. Monetary policy should basically seek to maintain adequate liquidity while avoiding further increases in domestic debt as a result of sterilization. For this to be accomplished it would be useful to follow a less aggressive policy for reserve accumulation; a high level of reserve accumulation will only add to domestic debt at a time when the destabilizing effects of rising debt are already at a critical level. In this vein, it would also be useful to avoid using domestic finance to implement external debt reduction, whether through debt buybacks or through debt-equity swaps.

2.44 Given the domestic debt problem it would be inappropriate to make lower inflation a priority to be pursued independently of progress on the fiscal side. The experience of both successful and unsuccessful stabilization programs in the last two decades shows that unless Government succeeds in generating a large enough primary surplus to finance domestic debt, attempts at stopping inflation are likely to fail. Since the current rate of inflation in the Philippines, while high, is not high enough to become a major destabilizing factor it might be preferable to concentrate policy efforts on reducing the stock of domestic debt.

2.45 Exchange Rate Policy. The authorities hope to be able to use the exchange rate to more effectively achieve balance of payments objectives. As such, there will likely be the need for an effective real depreciation, at a minimum to the level established in 1988. To be successful, such an attempt will have to be appropriately supported by fiscal and monetary policy. While the recent real appreciation was in part related to an "accommodating" exchange rate policy, it would have been difficult to avoid in any case given the current monetary and fiscal stance. In 1989, fiscal policy contributed to a situation of generalized excess demands, as evidenced by the rise in inflation and the increase in the trade balance deficit. A policy of tight

Central Bank domestic credit was also responsible for the real appreciation, as it induced, through high interest rates, large capital inflows.[2]

2.46 In summary, given the present configuration of interest rates, inflation, and the current account and fiscal deficits, the recommended policy package for the Philippines is a combination of tighter fiscal policy featuring a primary surplus large enough to substantially meet interest payments on internal and external debt, slower build-up of international reserves, and the restoration and subsequent maintenance of a competitive exchange rate. Furthermore, reductions in external debt should not be done at the expense of increases in domestic debt.

2/ International experience indicates quite strongly that devaluations work best only if accompanied by sound fiscal and monetary policies. Chile, for example, was able to undertake and maintain a real depreciation in response to debt crisis in 1982, which did not lead to an increase in inflation. The key to its success was the very tight fiscal stance maintained throughout the period, the adoption of a crawling peg system to maintain competitiveness, and the elimination of indexation on domestic wages to reduce rigidities and slow the transmission from devaluations to domestic prices (this had been a problem in Chile earlier). An additional reason for this success was that the devaluation took place in a period in which the domestic currency was clearly overvalued. Thus, the devaluation essentially "corrected" what at the time was a disequilibrium structure of relative prices as opposed to trying artificially to change relative prices simply through a devaluation.

III. ISSUES IN ECONOMIC EFFICIENCY AND COMPETITIVENESS

A. Introduction

3.1 The issue of economic efficiency is especially important for the Philippines at this juncture. To begin with, increased efficiency would permit more growth from available resources. This would help the country avoid excessive additions to the public debt which, as shown in the preceding chapter, is a major source of recent and prospective macroeconomic problems. In the longer run, increased efficiency would result in higher levels of economic activity arising from an improved environment for the private sector. This would generate higher public revenues which would also facilitate the task of macroeconomic management. Finally, increased efficiency would help the Philippines maintain competitiveness in external markets. This is particularly important not only for balance of payments and external debt servicing considerations but also because a lack of competitiveness in the export sector (which is relatively labor-intensive and rural-based) is especially damaging to the poor.

3.2 The Philippines economy suffers from low productivity. Despite relatively low wage costs, it is not sufficiently competitive once productivity is taken into account. A clear example of this is available in comparative data from the textile sector. As Table 3.1 shows, the Philippines would appear to have among the lowest supply prices of the sample of textile exporters shown but, once adjustments are made for productivity and product quality, it has one of the highest effective supply prices. Another issue for the Philippines is that its productivity has stagnated whereas that of its neighbours and competitors has risen, in some cases dramatically. This is shown in Figure 3.1 which maps manufacturing sector productivity indices for selected Asian countries since 1970. The figure shows that the present level of productivity in the Philippines is only marginally higher than the 1970 level and has never been more than 20% higher in the last two decades. It also shows that productivity growth in such competitor countries as Thailand and Malaysia has been quite high. Thailand's productivity has more than doubled since 1970 while Malaysia's has grown by about 60%. Clearly, from productivity considerations at least, it would appear that the competitiveness of the Philippines has declined in the last two decades.[1] A revealing index of the decline of external competitiveness is provided by the behavior of the share of Philippines exports in key world markets. Table 3.2 shows that Philippines market share has been declining in most export products and in most developed country markets throughout this decade.

1/ The consequences of low productivity growth were offset somewhat by even slower real wage growth for most of the last twenty years. However, more recent trends in unit labor cost are disturbing from the standpoint of competitiveness. Since 1987, unit labor costs have risen sharply in the Philippines as real wage growth has exceeded productivity growth. This development becomes even more significant when compared with a declining unit labor cost trend in Malaysia, a key competitor country.

FIGURE 3.1

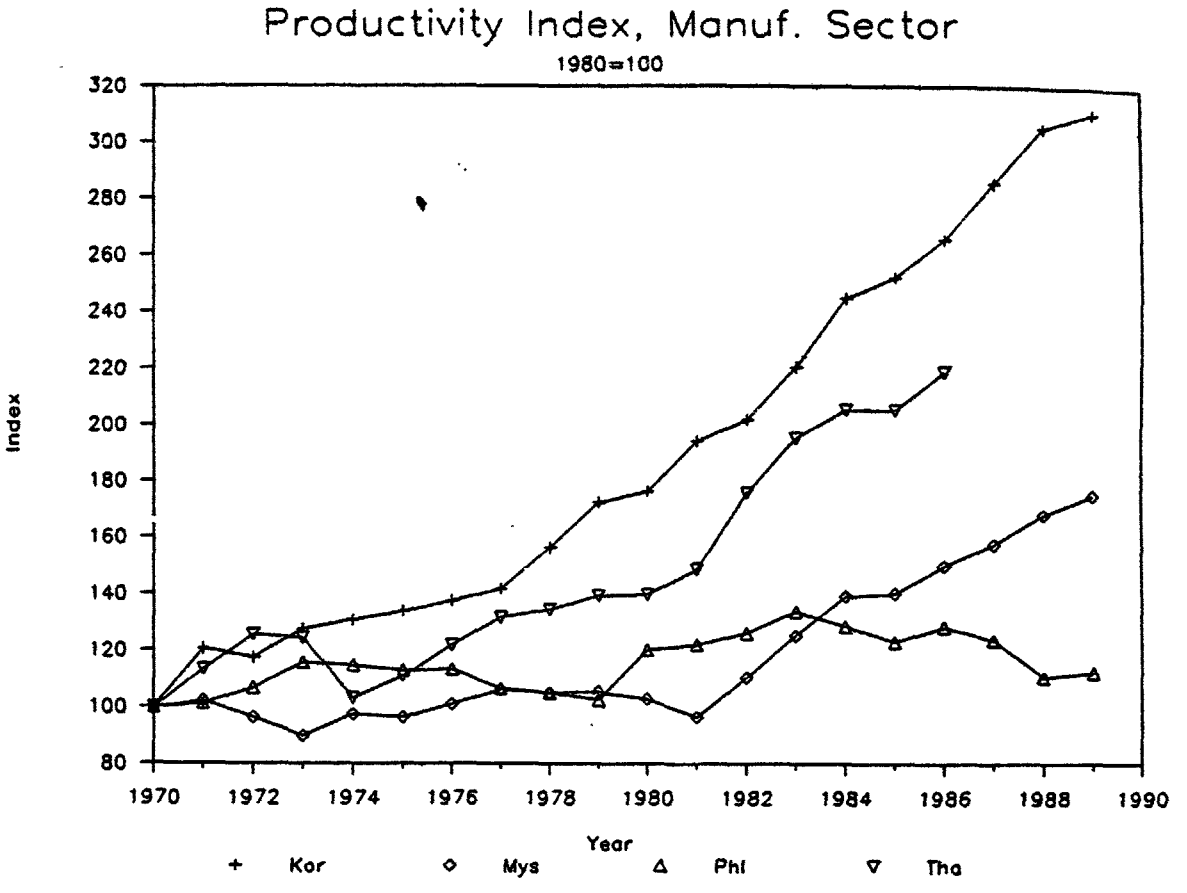

Productivity Index, Manuf. Sector
1980=100
Index
320
300
280
260
240
220
200
180
160
140
120
100
80
1970
1972
1974
1976
1978
1980
1982
1984
1986
1988
1990
Year
+ Kor
◇ Mys
△ Phl
▽ Tha

Table 3.1: RELATIVE SUPPLY PRICES QUOTA RESTRICTED TEXTILE AND APPAREL PRODUCTS, 1984

	Unadjusted for differences in labor productivity and product quality	Adjusted for differences in labor productivity and product quality
China	10	55
Hong Kong	68	68
Indonesia	8	52
Korea	38	49
Malaysia	19	46
Philippines	12	62
Singapore	54	62
Taiwan	59	59
Thailand	19	59

Source: Trela I. and J. Whalley (1988), Do Developing Countries Lose from the MFA?, NBER Working Paper 2618, Cambridge, Mass.

3.3 The present chapter discusses the structural determinants of economic efficiency and competitiveness in the Philippines. Seven areas of concern are highlighted: the openness of the trade regime, the effectiveness of investment incentives, the cost of financial intermediation, labor market developments, the size of the public sector, taxation, and the level and role of infrastructure spending and regulations. In each of these areas, recent reform efforts are discussed from the point of view of evaluating the extent to which they have improved overall economic efficiency on the one hand and relative (external) competitiveness on the other. Shortcomings of reform efforts are noted and areas for further adjustment are identified.

Table 3.2: EXPORT MARKET SHARES IN SELECTED COUNTRIES (1980-89)
(Philippines Exports as Percentage of World Exports)

	Food and live animals	Beverages and tobacco	Crude materials exc.fuels	Animal vegetable oil.fat	Chemicals	Basic manufac.	Machines transport equipment	Misc. manufac. goods
EEC 12								
1980	0.29	0.43	0.42	4.60	0.00	0.08	0.06	0.36
1983	0.20	0.32	0.39	5.45	0.01	0.08	0.11	0.32
1986	0.23	0.24	0.27	4.08	0.01	0.05	0.11	0.27
1989	0.22	0.14	0.24	3.88	0.02	0.06	0.09	0.34
Japan								
1980	3.75	0.50	5.04	8.56	0.67	0.37	0.63	1.12
1983	2.50	0.68	3.57	9.49	0.79	0.59	0.20	0.65
1986	2.59	0.42	2.35	4.98	0.45	0.65	0.16	0.46
1989	2.68	0.13	2.46	4.25	0.32	0.76	0.27	0.44
U. S. A.								
1980	2.74	0.29	1.08	40.55	0.08	0.57	0.68	1.71
1983	2.27	0.51	0.69	39.26	0.04	0.34	0.88	1.54
1986	1.50	0.12	0.31	31.14	0.17	0.17	0.35	1.35
1988	1.57	0.12	0.32	23.12	0.15	0.24	0.39	1.69
1989	2.04	0.07	0.28	21.32	0.13	0.24	0.44	1.84

B. Efficiency through Trade Reforms

3.4 Impact of Trade Reforms. Trade reforms are generally undertaken to improve resource allocation. In practice, this means the redeployment of factors of production from one sector to another in a way that enables an economy to produce more efficiently. Efficient production is also encouraged by the fact that the more open an economy is to trade, the more competition there is for domestic producers. In the Philippines, a program of trade reforms was started in 1981 and has been continued, with some interruption in 1983-85, to the present time. This program has had two components: import liberalization (or the reduction in the number of imports subject to restrictions) and tariff reform (or the reduction of the level and dispersion of tariffs). The latter component was more important in the pre-1983 period while the former has been more important since 1986. Tables 3.3 and 3.4 document various dimensions of recent trade reform efforts in the Philippines.

Table 3.3: TRENDS IN TARIFF PROTECTION

	1982	1985	1989
Nominal Tariffs 1/			
All Sectors	31.3	27.6	27.6
Agriculture	30.5	27.3	27.0
Mining	13.3	13.1	12.9
Manufacturing	31.8	28.0	28.0
Effective Rates of Protection 2/			
All Sectors	n.a.	44.0	36.5
Agriculture	n.a.	9.0	5.2
Mining	n.a.	-0.2	-2.0
Manufacturing	n.a.	73.4	55.5

1/ Unweighted average of book rates.
2/ Weighted average using price comparison method.

Sources: Tariff Commission and E. Medalla, An Assessment of Trade and Industrial Policy, 1986-88, Working Paper #90-07, Philippine Institute of Development Studies.

3.5 The benefits of trade reform are typically reflected in labor productivity trends in the manufacturing sector. Figure 3.1 shows that Philippine productivity declined in the 1970s but has generally risen in the 1980s. While this improvement is not uniquely attributable to trade reforms, the pattern is consistent with the timing and intensity of trade reforms in the Philippines in the last twenty years. In particular, the post-1980 period in which trade reforms have been implemented has seen an increase in productivity. Efficiency gains can also be seen in the trend of a more sophisticated measure of productivity, the total factor productivity index. This index declined in the 1970s but has been positive in most years during the 1980s, as can be seen in Table 3.5. Indeed, were it not for the disruptive effects of the deep recession of 1983-85, the gains in total factor productivity during the 1980s would have been greater.

Table 3.4: TRENDS IN IMPORT LIBERALIZATION

	Total Number Regulated	Newly-Regulated	Liberalized	No. of Regulated Items as Percent of total number of PSCC Lines 1/ (%)
1977	1892	47	--	33.5
1978	1926	34	--	34.2
1979	2031	104	--	36.0
1980	2032	1	--	36.0
1981	1771	2	263	31.4
1982	1438	277	610	25.5
1983	1988	598	48	35.3
1984	1994	6	--	35.4
1985	1924	--	70	34.1
1986	937	--	951	17.3
1987	802	--	171	14.2
1988	673	--	129	11.9
1989	579	--	94	10.2
Aug.1990	447	--	132	7.9

1/ PSSC refers to Philippines Standard Commodity Classification Code.

Source: NEDA

Table 3.5: TOTAL FACTOR PRODUCTIVITY IN SELECTED MANUFACTURING INDUSTRIES 1/

	1970-80	1981-83	1984	1985-87
All Manufacturing	-1.20	2.31	-21.95	4.51
Food		-38.4	-14.9	7.13
Apparel		-2.9	-15.7	-0.27
Paper		1.19	-29.8	5.02

1/ Indices refer to large establishments having ten or more workers.

Source: Staff calculations

3.6 Trade reforms are often resisted on the grounds that they can be disruptive to the economy. As factors are redeployed following the change in relative prices brought about by reductions in tariffs or removal of import restrictions, unemployment, capacity reductions or plant shutdowns can occur. In the case of the Philippines, there is no evidence to suggest that such

short-run consequences have been very disruptive. There is no clear link between changes in employment and/or production and episodes of trade reform.

3.7 Another concern is that liberalization leads to excessive imports of non-essential consumption goods thereby worsening the balance of payments situation. In general, there is no evidence to suggest that the import liberalization measures adopted since 1986 have led to surges of imports of unnecessary consumer goods. The Tariff Commission reports that in 1988, imports of liberalized items reached 25% of total imports. In terms of end-use categories, raw materials accounted for 1%, intermediate goods for 18% and finished goods for 6%. Non-essential consumer goods and unclassified consumer goods accounted for 2.2%, while essential producer goods accounted for 16% of total imports.

3.8 Recent Measures. The main thrust of changes in trade policy since 1986 has been liberalization of import restrictions. The number of regulated imports in terms of tariff line items declined from 1924 four years ago to 447 by August 1990. As a share in total number of PSCC lines, the regulated imports declined from 34.1% to 7.9% (see Table 3.4). During the period 1986-89, nominal tariffs have remained virtually unchanged, but there has been a slight reduction in tariff rate dispersion. Effective rates of protection have declined by about 7 percentage points overall and their dispersion has also decreased. Since nominal tariffs have remained virtually unchanged, the reduction in effective protection must be attributed mainly to the liberalization in import restrictions.

Outstanding Issues

3.9 The foregoing discussion indicates that the Philippines has made good progress on trade reform and has benefitted from the measures undertaken so far. However, its competitive position in world markets has not improved for two reasons. Firstly, the Philippines has failed to support its trade reform efforts with a consistent exchange rate policy in favor of exports. Secondly, it has lagged behind its principal competitors even in trade reform measures. For example, while the Philippines has only recently achieved a liberalization ratio of around 92%, Malaysia and Thailand have had liberalization ratios of over 95% for many years now. Similarly, average nominal tariffs in the Philippines, despite having declined since 1980, remain above those of Indonesia and Malaysia, though lower than those of Thailand. Further trade reform measures would be desirable not only because they would raise absolute efficiency in the economy, but also because they would promote its relative competitiveness. In this regard, it is encouraging to note Government's continued commitment to this process, most recently affirmed in tentative proposals for a new round of trade reforms to address several outstanding issues.

Table 3.6: COMPARATIVE TRADE REGIMES

	Average Nominal Tariff 1/	Liberalization Ratio 2/
Malaysia	14	>95
Thailand	34	>95
Indonesia	26	84
Philippines	28	92

1/ Average nominal tariffs are for various years over 1985-88 and refer to unweighted book rate data.
2/ Refers to number of unrestricted importable items to total and excludes those restricted for health, safety and security reasons.

Source: M. Noland, Pacific Area Developing Countries: Prospects for the Future, Institute for International Economics, Washington, DC, 1990.

3.10 One major issue is the continued presence of quantitative restrictions (QRs) of various kinds. The presence of QRs, still affecting more than 10% of the PSCC lines as noted above, encourages inefficient investments and production activities, and has contributed to low productivity in certain segments of the manufacturing and agriculture sectors. QRs also represent a highly inefficient instrument of trade policy, since they deprive the Government of a significant source of revenue. This is particularly important under the present circumstances of severe budgetary constraints. Moreover, QRs are not transparent instruments of protection since they do not allow an effective assessment of relative support provided by the Government policies.

3.11 Removal of QRs would, therefore, be highly desirable. It is recognized, however, that some industries could be severely affected by such a step and may require temporary assistance to allow for adjustment to the reformed trade regime. Such support would best be provided in the form of time-bound and progressively declining tariff surcharges. While Government has recently proposed a program for the elimination of QRs, the proposal has not been amplified nor has an implementation schedule been announced; it is possible that implementation could be significantly delayed.

3.12 Another remaining issue is the continuation of high protection of industry in general and of manufacturing in particular. Even though effective protection of industry has recently declined, the existing effective protection of about 50% for the industry as a whole is excessive. It implies effective rates of protection for some industries well over 100%, and in exceptional cases, even close to 200%. Clearly, with this level of protection, the benefiting industries have very limited incentives to increase efficiency.

3.13 A related issue is the scope of distortions arising from the existing structure of protection. Even though the bias has been considerably reduced over time, existing interventions continue to discriminate against exports and agriculture. Moreover, the level of protection within the manufacturing sector is highly uneven. These distortions arise because the present band of tariffs, ranging from 0% to 50%, results in a situation in which some sectors receive the excessively high level of protection noted above, whereas others are protected considerably less, and some even negatively. This pattern of protection encourages investments in relatively less efficient (high cost) activities, while discouraging activities in which the country may have a comparative advantage. The high dispersion of tariff rates also increases the administrative costs of tariff collection and, together with high tariffs, encourages muggling and misdeclaration on tariff documents (technical smuggling). This adversely affects budgetary revenues and leads to unfair competition between domestic production and imports.

3.14 The solution to these problems lies in a revision of the tariff schedule to significantly reduce the level and dispersion of tariff rates. Recently, Government has proposed the introduction of a four band system with tariffs rising in steps as follows: 3% for all goods that previously had a tariff rate of 5% or less; 10% tariff on raw materials; 20% on intermediate goods and 30% on final goods. If implemented as proposed, this would be a highly beneficial move. The revenue loss resulting from the reduction in top tariff rates should be offset by increased revenues from (a) replacement of QRs by tariffs and/or tariff surcharges, and (b) stricter compliance with simplified customs declarations, as well as by lower costs of customs administration. As of this writing, Government's tariff reform proposal is being held in abeyance pending the outcome of consultations with affected business sectors and Congress.

C. Investment Incentives and Industrial Policies

3.15 Objectives of Industrial Policy. Government has attempted to influence the size, location, composition and competitiveness of Philippine industry through a variety of industrial policy measures, ranging from fiscal incentives to capacity regulations. The major vehicle of industrial promotion under the Aquino Administration has been the Omnibus Investment Code (OIC) adopted in 1987 and administered by the Board of Investments (BOI). Among the objectives of the OIC are: domestic investment promotion, augmentation of direct foreign investment, export promotion, regional development, employment enhancement and technology upgrading. The overall industrial strategy also calls for the development of special industries, the most prominent one being the automotive industry, through capacity and import restrictions. The chief incentives available under the OIC are fiscal in nature: eligible investments are provided exemption from duties and taxes on certain inputs and expenditures, as well as a general tax holiday. The hypothetical effects of such incentives can be quite significant. A recent study shows that the

internal rate of return of a project can be doubled by utilization of the appropriate incentives.[2]

3.16 Impact of BOI Incentives. At one level, investment data could be interpreted as indicating the effectiveness of an incentives-based industrial strategy. The data reported in Table 3.7 show that the volume of investments covered by BOI approvals has risen dramatically both in nominal and real terms since 1986. These data should, however, be examined in perspective. The rise in investments need not necessarily be attributed to the inducements of the OIC. First, much of the increase in investment that has occurred since 1986 would have occurred anyhow, with or without incentives, in response to the growth of the world economy in general and to the recovery of the Philippine economy in particular. Indeed, overall investments (that is, including those not registered with the BOI) have risen sharply since 1986. Second, BOI data refer to approvals rather than to investment flows per se and are thus an overestimate of annual investment flows to the extent that not all approved projects actually get implemented and, for the ones that do get implemented, the total amount approved is not necessarily invested in one year but may be spread over time.

3.17 From the point of view of economic efficiency several other considerations must also be taken into account. Among such considerations are the effect on choice of techniques and choice of projects as well as the fiscal impact of the incentives. As far as the effect on choice of techniques is concerned, Table 3.7 indicates that the capital intensity of approved projects (measured as the investment per person employed) declined substantially from 1983 to 1987 but has since been rising. To some extent then, BOI incentives are having the perverse effect of promoting capital-intensive projects in a labor-rich economy. Recent evidence on choice of projects is also disturbing if it is accepted that export-oriented projects are more suited to the present needs of the economy: project approval data show a tendency for the share of export-oriented projects to be lower in recent years than in the earlier part of the decade. Incentives, of course, are only one of the determinants of these trends; more important determinants of both choice of techniques and choice of projects are exchange rate and tariff policy.

3.18 As far as the fiscal impact is concerned, it is generally felt that the structure of fiscal incentives leaves much to be desired and that the overall fiscal impact on the budget is considerable. The inappropriateness of some of the incentives being offered may be seen from two examples. One is that the current system offers tax holidays for the early years of a firm's operations when it is likely to be making losses. The incentives would be more useful from the firm's point of view if they applied to the first few profit-making years or if loss carry-overs were permitted for tax purposes. Similarly, tax deductions may be of little additional benefit for foreign investors if their

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2/ See R. Manasan, "A Review of Investment Incentives in ASEAN Countries", Working Paper Series No. 88-27, Philippine Institute for Development Studies, 1988.

Table 3.7: CHARACTERISTICS OF BOI-APPROVED PROJECTS 1/
(in billion Pesos except as noted)

	1983	1986	1987	1988	1989 2/
Volume of Investments					
Nominal	5.2	3.2	11.9	32.8	70.8
Real	5.2	1.8	8.4	14.0	28.7
Projected Employment					
Total (000 persons)	113	26	82	128	153
Investment per Worker (Real, 000 pesos)	46	12	15	26	46
Share of Export Projects to Total Approvals	76	72	62	50	55
BOI Share of Total Inv. (in per cent)	5.5	4.0	11.7	25.9	42.4
Fiscal Impact					
Incentives/Govt. Revenues (in per cent)			8.2	7.0	5.8

1/ Not all approved projects get incentives.
2/ Provisional estimates.

Source: Board of Investments

home countries already allow foreign taxes paid to be credited against home country tax liabilities, as is the case with the US, for example. Despite these examples of redundancy, it is sometimes argued that the present incentive system has a large budgetary impact. Such an impression is not supported by the available data. Table 3.7 shows that revenue foregone on account of various fiscal incentives amounted to 8.2% of total revenues in 1987 and has declined since then to 5.8% in 1989. As a rule, incentives involving tax exemptions, credits and deductions, result in a greater loss of potential revenue than duty exemptions on imports, but neither category involves a substantial loss.

3.19 Recent Initiatives. Measures have recently been proposed to make the investment incentives system more effective and less discretionary. If adopted and implemented as proposed, these initiatives would allow accelerated depreciation, the carry-over of business losses for tax purposes, and the automatic availment of a flat rate of 10% on imported capital equipment. The last noted measure would result in a substantial reduction of the discretionary power of the BOI since dutyexemptions on imported capital equipment constitute one of the most important incentives that the BOI

currently offers. The BOI has proposed that this measure be accompanied by a measure to provide tax credit for the use of locally manufactured capital equipment so as not to disrupt the local capital goods industry.

Direct Foreign Investment

3.20 One of the objectives of the OIC is to promote direct foreign investment (DFI). Thus it provides, in addition to the general incentives available to all eligible investors, specific incentives and guarantees for foreign investors in such matters as repatriation of profits, dividends and capital, expropriation, nationalization and so on. Furthermore, during 1988, foreign investors were permitted to avail of debt-to-equity swap facilities whereby they could purchase Philippine external debt at a discount and use it to cover their peso investment needs. On the other hand, there is a perception among foreign investors that the Philippines incentive scheme is too restrictive, especially to the extent that it restricts foreign ownership to 40% in most cases, the exceptions being investments that produce mostly for export or have pioneer status. It is difficult to isolate the impact of all these incentives on DFI since many other factors (discussed below) also affect the level and composition of such investments. Whatever the cause, DFI has risen in recent years from a level of $140 million dollars in 1986 to around $850 million dollars in 1989.

3.21 Government is aware of the concerns of potential foreign investors and is currently discussing a set of measures to make the Philippines a more attractive location for foreign investment. Of the various measures being considered perhaps the most important involves the drawing up of a narrow negative list that would contain the business areas from which foreign investment is to be prohibited. It is widely felt among the foreign investor community that the present approach, wherein DFI is approved virtually on a case-by-case basis, does not provide clear signals and gives too much discretion to the approving authority. A short list and transparent approval procedures would make a considerable difference in the attitude of foreign investors. Another area of concern is the so-called "60-40 rule" that restricts foreign ownership to 40% in many investment areas. Among the options being discussed is that of allowing foreigners to own more than 50% of the equity of a joint venture in a larger number of areas (including investments oriented entirely to the domestic market) provided they agree to divest their shares to Filipino nationals over an agreed period of time. In other words, management control will be retained by the foreign investor but only for a specified and negotiated period of time.

3.22 Other Considerations. In addition to OIC incentives, the level of DFI flows into the Philippines is determined by such factors as the before-incentives level of attractiveness, non-economic considerations and risk-spreading considerations. As far as the first factor is concerned, the attractiveness of the Philippines as an investment destination depends on the extent to which foreign investors ignore its relatively poorer infrastructure in favor of its relatively inexpensive, well-educated and English-speaking labor force, a calculation that can be strongly affected by movements in real effective exchange rates. Philippine competitiveness on this score has been

adversely affected in recent months by higher inflation and wage rate adjustments than in most ASEAN countries.

3.23 As far as non-economic considerations are concerned, there is a continuing perception that the Philippines remains politically unstable and that there remains a risk to the personal security of foreigners. These considerations must be balanced against the fact that Japan and the NICs are generating large amounts of surplus capital that must be invested abroad (in view of their loss of comparative advantage in certain areas and their loss of GSP privileges) and that, all other things being equal, they would prefer to spread their risk by diversifying among DFI destinations. In this regard, one often hears nowadays that investors are seeking to diversify away from Thailand and Malaysia. Despite its security problems, therefore, the Philippines is likely to continue to receive some DFI for this reason.

3.24 Role of Debt-Equity Swaps. A comparison of DFI incentives across ASEAN countries indicates that the relative attractiveness of individual countries is not affected by their incentive schemes because these schemes are similar in important respects and offer roughly equal inducements (see Manasan, 1988). Raising fiscal and other incentives may increase the levels of both domestic and foreign investment but will typically not increase market share in the sense of attracting potential investors away from other countries because competitor countries will offer matching incentives. The Philippines, however, possesses one instrument that can affect its market share in the prospective flow of DFI and that is the possibility of using debt-equity swaps as an investment promotion tool. Such swaps can be used to offer potential investors a rather attractive discount which cannot be matched by countries whose debt is not trading in the secondary market at a substantial discount. Thus, the Philippines can offer investors a discount that, ironically, Malaysia and Thailand, with their higher creditworthiness and better debt repayment performance, cannot match directly. [3]

Export Promotion

3.25 Accelerating and sustaining the growth of exports is fundamental to both reducing the Philippines' relative burden of debt and providing foreign exchange for debt service and for critical import needs. This is clearly one of the highest economic priorities and major challenges facing the Philippines. Compared to a historical real export growth rate of less than 3% during the past decade, it is estimated that an average of 8% export growth must be achieved in the next decade in order to attain targeted goals in the balance of payments, in debt servicing and in economic growth.

3/ Two qualifications should be noted. First, the investment promotion effect should be balanced against the monetary expansion effect of debt-equity swaps. Second, while the large jump in DFI inflows recorded in 1988 and 1989 was due in considerable part to the availability of debt-equity swap facilities, it is difficult to calculate the "true" incremental investment induced by such facilities because of the lack of a stable historical trend against which to measure policy-induced deviations.

3.26 Moreover this acceleration will need to built on a restructured export base. Little real growth is expected from traditional exports which constitute a third of merchandise exports. Thus almost all the growth burden falls on non-traditional exports. While growth of non-traditional manufactured products has been very rapid since the mid-1970s, it has been based almost entirely on exports of two products--garments and electronics--which now comprise 60% of non-traditional exports. While extending backward linkages in these products, particularly garments, could provide important source of foreign exchange earnings, other manufactured products, which presently make up only a quarter of export goods, will need to perform exceptionally well if the Philippines is to have any hope of meeting its debt and growth targets.

3.27 In addition to being based on a narrow range of products, recent export performance in the Philippines has been disappointing on two counts. First, merchandise export growth, while higher than in the early 1980s, has not been sufficient to improve the current account. Second, such growth has been slower than that of Malaysia and Thailand during 1987-89, leading to a loss of market share in developed countries.

3.28 There is increasing awareness and concern in Government, particularly the Department of Trade and Industry, on the need to address these export objectives with a much more comprehensive and forceful export strategy. In addition to maintaining a competitive exchange rate, which is possibly the single most important measure that Government can take, there are three basic areas that are critical to an effective export performance: access to inputs at competitive prices, access to finance at competitive rates and an institutional and promotional framework that addresses key supply-side constraints. These are discussed below.

3.29 Access to Inputs. The Philippines has been operating several administrative and bonded type schemes to provide exporters with duty free access to their inputs. However these schemes have critical deficiencies: coverage of exporters and export products is very limited and bureaucratic complexities and delays impose significant costs on exporters that are covered. Only about 20% of exporters and half of non-traditional exports are covered by some form of drawback/exemption scheme. Four major problems have contributed to the ineffectiveness of the schemes. First, many exporters are subject to local "non-availability" requirements restricting their access to internationally competitive inputs. Second, the "formulae of manufacture" used to reconcile imported inputs with exported outputs have not been standardized making the process time consuming and cumbersome for exporters and implementing agencies. Third, the control mechanisms and agencies are duplicated for much of the drawback/exemption administration. Fourth, indirect exporters are for the most part not covered.

3.30 Government is aware of these problems and has been trying to address them. Substantial work is underway to improve the quality and efficiency of techniques and procedures used to estimate "formula of manufacture" coefficients. Also, Government has been preparing more far-reaching measures to streamline the administration of the system and to extend coverage to all

exporters including indirect exporters. These measures merit priority consideration and enactment.

3.31 Access to Finance. Existing systems of export finance in the Philippines are very inadequate especially for a country facing an acute shortage of foreign exchange and the need to accelerate export earnings. Many exporters, especially newer and smaller ones, face great difficulty obtaining working capital finance for their export activities. Indirect exporters are even worse off. No mechanism, such as the domestic L/C, is being used that would enable them to access export finance. Traditional banking practices currently in use do not make use of streamlined disbursement mechanisms to reduce the duration and hence costs of export loans. There have developed no collateral substitutes to meet banks' formidable collateral requirements. Nor have transaction-based loan arrangements been employed to increase loan surety. The use of local currency loans for imported inputs has missed an opportunity to reduce finance costs to more competitive levels.

3.32 In this context, high priority needs to be given to implementing a system of export finance that has been effective in other successful exporting countries. Specifically, it is recommended such a scheme include: a foreign currency loan scheme to finance imported inputs, modernized disbursement mechanisms, parallel systems (such as domestic L/C) for exporters domestic purchases, and a greatly expanded preshipment guarantee facility for export loans. The Government has recently taken the first step in this direction by initiating a fundamental restructuring of Phi' ıarantee to make the creation of an effective preshipment export guarantee · ility its primary corporate objective.

3.33 Export Promotion Strategy/Institutional Support. The Government has provided a number of programs to assist exporters over the past decade. A few of these programs have been successful within their limited objectives. Others less so. However, the Government has not been able to formulate an effective national strategy and the administrative mechanisms to implement it. As such, the approach is very ad hoc with no efficient mechanism for responding to exporters' concerns in a systematic way with quick and deliberate action that cuts across interagency bureaucratic hurdles. Further, the effectiveness of Government programs has been hindered by the multiplicity of Government agencies providing services, and the minimal role the private sector has had in the design and delivery of such services.

3.34 The Government is working on an important piece of legislation--the Export Omnibus Bill--to address these shortcoming in the policy/institutional framework. This legislation, which is still being drafted, would establish an institutional framework in which exports would: be given high level priority and attention by the key policy makers; involve the private sector in a major way in formulating and fine tuning export policy and procedures and in implementing export support measures; provide an independent source of funding dedicated to export programs in such areas as marketing, design, trade fairs, product prototype development, packaging, trade information and training; and provide the legal basis for executive action to carry out program and policy decisions. The legislation would remove from Government many of the diverse and overlapping export services, consolidate them, and transfer them to a

professionally managed, private sector oriented Trade Promotion Organization. The legislation would establish the basic policy objectives in such critical areas as export finance, duty free access to imported inputs equipment and foreign exchange, and the import and export procedures. As such the proposed Omnibus Legislation could be an important vehicle to spearhead a more aggressive and comprehensive export policy and support framework.

Sectoral Policies and Programs

3.35 In addition to investment promotion policies, the industrial sector has been subject to a variety of sectoral policies. The World Bank together with the Government has recently conducted detailed studies of four subsectors--cement, textiles, pulp and paper and shipping--to assess the growth potential of these sectors, identify constraints on their performance and devise action programs, including institutional and policy reforms, to develop these sectors.

3.36 The studies suggest that the low productivity and high operating costs that characterize these sectors result from high energy intensity of production, high wastage rates of raw materials, high maintenance costs, low labor productivity, suboptimal scale of production, inadequate labor skills and lack of preventive maintenance systems. Another issue is the procurement and use of inefficient and obsolete technology. For example, second-hand plants using pre-1975 technology are being installed in the cement and paper & pulp industries, and old vessels are being purchased by shipping companies.

3.37 Underlying these problems have been deficient sectoral policies. Even though most if not all of these problems will call for new investments, the sine qua non of such investments should be elimination of the remaining policy distortions. In the cement industry, the major distortion is the existing price control by which the Government hopes to protect consumers. However, since demand for cement has been recently growing very rapidly, it has become necessary for the Government to liberalize imports of cement and permit free pricing of imported cement. The result has been a major increase of domestic prices to consumers and very slow response of the domestic cement industry to satisfy demand. Price controls have also limited the incentives to expand and modernize the cement industry. In view of these effects, it would be advisable to remove price controls on the cement industry as soon as practicable.

3.38 The pulp and paper industry suffers primarily from an irregular structure of import tariffs. Imported inputs are subject to very high tariffs, which will need to be lowered to reduce costs of production. In addition, the tariff rates are highly dispersed, which provides uneven protection to domestic producers and encourages technical smuggling. Similarly, the tariff rates on output of industry are also too high and non-uniform. These issues need to be addressed but the solution should be a part of a general tariff reform rather than a piece-meal approach in order to ensure consistency with changes of other tariffs. In its recent announcements Government seems to be moving in this direction and its efforts merit support.

3.39 In the shipping sector, the major policy issues include franchising, price control and statutory rate of return requirements. In comparison to the cement industry, the price control in shipping is more complex. The price control has been introduced to accompany franchising of routes, which in turn was justified on the grounds of protecting consumers and ensuring safety standards. However, neither of the latter objectives has been met satisfactorily over the years. The statutory requirement for rate of return on investments is a tool borrowed from public utility regulation, but it is an inappropriate tool for a potentially competitive industry and a principal reason for the poor profitability of shipping operations in the last few years. The price control should be removed, and the removal should be accompanied by measures to facilitate entry into the industry.

3.40 Car Manufacturing Program. The car manufacturing program, which seeks to promote the development of an automotive industry in the Philippines through cartels and import controls, has come under attack for producing too little at too high a cost. While production has risen significantly in the last two years, demand has risen much faster. There is a six month wait for delivery and premiums have to be paid to dealers and suppliers. The high cost of domestically-assembled vehicles and the questionable foreign exchange savings have also attracted much negative comment. To meet some of these criticisms, Government has approved a scheme whereby cars may be imported provided payments are made directly out of overseas earnings. Also, the BOI has recently decided to allow more companies to join the production program; the new-comers will be restricted to producing small cars (sub-compacts). Given the reportedly high cost of the car development program, it would be useful to assess, through a more comprehensive exercise, whether it is achieving the goals originally envisaged.

D. Interest Rates and Financial Intermediation

3.41 High Costs. Viewed in comparison with its ASEAN neighbours the Philippines has a relatively underdeveloped financial sector. This is shown in Table 3.8 by the ratio of total domestic liquidity (M3) to GNP. The Philippines also features relatively high interest rates and spreads. While measures of degree and cost of intermediation vary somewhat from year to year, it would nevertheless be fair to say that, as far as financial services are concerned, on average the Philippines produces relatively small quantities at relatively high costs.

3.42 The costs of financial intermediation are high in the Philippines for reasons related to Government policy and financial market structure. Government policy features relatively high explicit and implicit taxes on financial intermediation which add to cost. The market structure for financial services is characterised by oligopoly which also adds to cost by way of high operating and profit margins.

Table 3.8: COMPARATIVE FINANCIAL INTERMEDIATION DATA (1988)

	Indonesia	Malaysia	Singapore	Thailand	Philippines
M3/GNP (%) 1/	21.9	59.8	72.4	59.4	18.5
Real Loan Rate 2/	16.2	3.2	3.0	8.0	6.2
Nominal Loan Rate 3/	22.1	7.3	6.0	15.0	15.9
Nominal Deposit Rate 4/	17.7	3.3	2.7	9.5	9.3
Interest Rate Spread 5/	4.4	3.9	3.2	5.5	6.6

1/ Demand, savings, and time deposits.
2/ Nominal rate minus growth of GDP deflator.
3/ Bank lending rates for short- and medium-term financing needs of the private sector (IFS line 60p).
4/ Bank deposit rates include rates offered to resident customers for demand, time and savings deposits (IFS line 601).
5/ Difference between nominal loan and deposit rates.

3.43 Implicit and Explicit Taxes. Three taxes affect the cost of intermediation in the Philippines. First, an implicit tax on financial intermediation is imposed by a requirement that 25% of a commercial bank's assets be in the form of loans for agricultural purposes or to beneficiaries of agrarian reform laws (the so-called agri-agra requirement). Second, another implicit tax is imposed by monetary policy considerations in the form of reserve requirements. Third, an explicit tax (currently at 5%) is levied on gross receipts of banks (the Gross Receipts Tax or GRT). Overall, such taxes can add several points to the interest rate charged by banks.

3.44 Table 3.9 provides data on trends in financial intermediation margins in recent years. It can be seen that the intermediation cost to banks (which is due to all implicit and explicit taxes) fell from 1985 to 1987 but has since been rising. This pattern can be explained largely by changes in reserve requirements which impose by far the largest tax on financial services since they tend to relatively high in the Philippines. As reserve requirements were reduced in keeping with an easing of monetary policy in 1985 and 1986, intermediation costs fell. Since 1988, however, monetary policy has been tightened and the implied tax on intermediation has risen. This has been especially important in 1989 when all banks were required to keep 21% of most types of deposits in reserve.

Table 3.9: BANK SPREADS AND MARGINS

	1985	1986	1987	1988	1989
Banks Borrowing Rate 1/	21.3	12.6	9.0	10.6	13.5
Intermediation Cost 2/	6.9	2.7	1.1	1.7	2.8
Gross Bank Margin 3/	0.3	2.3	3.2	3.6	3.0
Banks lending Rate 4/	28.5	17.5	13.3	15.9	19.3
Gross Spread 5/	7.2	5.0	4.3	5.3	5.8
Bank Margin Rate (%) 6/	4	46	74	68	52

1/ Refers to simple average of Manila Reference Rate (MRR90).
2/ Cost due to imposition of Gross Receipts Tax, Reserve and Agri-Agra Requirements.
3/ Sum of operating costs and profits of banks.
4/ Refers to Secured Loan rate (61-90 days).
5/ Difference between bank lending and borrowing rates.
6/ Ratio of Gross Bank Margin to Gross Spread.

Sources: C.V. de Leon, "A Historical View of the Intermediation Cost of Commercial Banks," CB Review, April 1989, Central Bank of the Philippines; Philippine Financial Statistics.

3.45 Bank Margins. Table 3.9 also indicates that the bank margin is an equally important component of the gross interest rate spread. The bank margin is made up of operating costs and profits. Both of these components tend to be relatively high in the Philippines as compared to other countries. This impression is supported by the data in Table 3.10 which compares the Philippines with selected ASEAN countries in respect of, among other things, operating expenses and interest margins. It is worth noting that operating expenses are relatively high in the Philippines despite its generally lower labor costs (in nominal terms and especially compared to Thailand and Malaysia). This suggests insufficient competition within the financial system.

3.46 Bank Concentration. The Philippine banking system is made up of a few large and strong banks and numerous small and weak banks. Five large commercial banks dominate the system. Most measures of concentration indicate an increase in market share and market power for the large banks since the financial crisis of the mid-1980s. Indeed, each of the largest five banks had assets in 1988 that were greater than the assets of all rural and savings banks combined. Still, concentration is not unusually high in the Philippines; it is lower than in several of its ASEAN neighbours. The real issue in the Philippines is the high degree of control over entry into the system, control that has essentially protected the smaller, weaker banks and allowed the larger, more efficient banks to reap above-normal profits. An example of the barriers to entry into the system is provided by the fact that

only two new commercial banks have been licensed in the last twenty years, both in recent months.

Table 3.10: BANK CONCENTRATION, OPERATING EXPENSES AND INTEREST MARGINS

Country	4-Bank Concentration Ratio	Operating Expenses 1/	Interest Margin 1/
Thailand	65	2.28	2.50
Indonesia	66	2.40	2.24
Malaysia	64	2.80	3.60
Philippines	40	3.90	2.70

1/ Expressed as percentages of total assets.

Source: Staff Calculations

3.47 While it is hard to document collusive behavior among the top banks, some features of the financial system are consistent with the exercise of oligopoly power. For example, interest rates have tended to be sticky downwards; there is little interest rate competition among banks who prefer instead to compete on service and via advertisements. When interest rates were liberalized in the early 1980s, interest spreads widened as deposit rates fell and lending rates increased. Normally, competition among banks would have been expected to raise deposit rates and reduce spreads.

3.48 Capital Market Development. The capital market remains relatively underdeveloped as well. While the Philippines has long had stock exchanges, the capital market has not really developed into a significant alternative source of funds to banks. In terms of size, the market has only recently breached the 10 billion peso level. Public participation remains narrow and investor confidence remains minimal since it is generally felt that investors are not well protected from loss from irregular activities. The market is dominated by a few big issues and trading is subject to large sings in volume and price. The top ten stocks contribute almost 80% of market capitalization, a much higher level of concentration than in the stock markets of other ASEAN countries (see Table 3.11).

Table 3.11: COMPARATIVE CAPITAL MARKET DATA (1989)

	Indonesia	Malaysia	Thailand	Singapore	Philippines
Market Capitalization (billion US Dollars)	6	24	17	47	12
No. of Listed Securities	51	235	160	147	144
Capitalization of Top 10 Stocks (% of Total)	52	44	61	35	79

3.49 Private Sector Concerns. Government policy and the structure of the financial system raise two issues of concern for the private sector. One is the high cost of finance and the other is the level and pattern of credit availability. The high cost of finance has already been documented: currently, nominal interest rates applicable to collateralized lending are running at 25% (this implies real interest rates in the neighbourhood of 12%). This is a significant deterrent to both domestic and foreign investment and cannot be sustained for long, even if new investment is only modestly sensitive to interest costs. Credit availability is an issue in the sense that the loans given by commercial banks to the private sector have not yet recovered in real terms to pre-crisis levels. As Table 3.12 shows, real credit availability in 1989 was only half that of 1984.

Outstanding Issues and Suggestions for Reform

3.50 The Bank has drawn attention to the problems of the Philippines financial sector previously and has encouraged suitable reforms with the support of a sector adjustment loan. Among the reforms suggested are measures to reduce intermediation costs, to increase competition and to strengthen supervision and regulation of commercial banks. The Bank has recommended that intermediation costs be reduced by the elimination of the Gross Receipts Tax and the withholding tax on interbank deposits, and the abolition of the agri-agra requirement. Recently, Government has indicated that it may be able to eliminate the two taxes by the end of the year and to modify the agri-agra requirement so that it does not impose as heavy a burden to banks as it has till now. A far more important tax, however, is that implied by high reserve requirements. These cannot be reduced until monetary conditions are appropriate in the sense that inflation and inflationary expectations are low.

3.51 Competition in the banking system is to be enhanced through a more permissive approach to bank and branch licensing. Recently, the Central bank issued a circular announcing that there was no moratorium on either the formation of new banks or the spread of branches. In practice, however, there has been little progress on this front. The system of approving branch

Table 3.12: CREDIT AVAILABILITY 1/

	1984	1985	1986	1987	1988	1989 3/
Nominal						
Agriculture	23.7	23.9	20.9	21.2	25.6	28.4
Manufacturing	115.6	87.2	82.2	94.2	123.9	151.7
Trade	63.4	41.4	46.4	54.2	59.0	62.7
Total	322.2	264.7	320.0	359.3	366.6	357.2
Real 2/						
Agriculture	23.7	19.4	16.7	15.1	15.0	12.6
Manufacturing	115.6	70.9	65.9	66.9	72.6	67.5
Trade	63.4	33.6	37.2	38.5	34.6	27.9
Total	322.2	215.1	256.4	255.3	214.9	159.0

1/ Measured as loans granted by commercial banks in billion pesos; not revised to reflect recent changes in coverage.
2/ Adjusted by GDP deflator using 1984 constant prices.
3/ Data as of end-September 1989 (annualized).

applications relies too heavily on regulatory notions of branch-sufficiency in a given area and does not take adequate account of the benefits of branch competition. Most profitable geographical business areas are presently considered overbranched and applications for licenses are normally turned down. Similarly, despite several applications, only two new commercial bank licenses have been granted following the agreement with the Bank to stimulate competition in the banking sector. While Government is understandably concerned about the soundness of banks and the safety of the financial system, its approach has been over-cautious. A more appropriate stance would be to maintain a strict regulatory environment and relatively high capital-asset requirements for bank licensing but to leave decisions regarding the opening of a bank or the location of a branch to entrepreneurs. Finally, competition in the banking sector would be enhanced by a more open approach to the licensing of foreign banks and to their operational scope.

3.52 The lack of a significant alternative source of finance in the form of a capital market has been noted above. Government is cognizant of the need to stimulate capital market development and is considering various steps to make equity issuance more attractive for companies and stock purchases a safer form of investment for individual investors. One measure being considered is the merging of the two stock exchanges in Manila so as to achieve economies of scale in listing, trading and backroom operations, economies that could be passed on to issuing companies.

E. Labor Market Issues

3.53 Labor market developments typically affect economic efficiency to the extent that they alter the size and proportion of the labor force whose compensation is not determined by market forces. This could occur in one or more of several ways: if the size or compensation of public sector employment rises substantially, if unionization increases in either the public or the private sector, or if labor compensation in the private sector is excessively influenced by Government intervention. Recent developments in these areas in the Philippines have potentially adverse implications for economic efficiency even though, on balance, their effects to date are likely to have been rather small.

3.54 Public Sector Employment and Compensation Levels. The level of employment in the public sector has risen faster than that in the private sector in the last three years. Public sector compensation levels, especially at the lower end of the scale, rose substantially in 1989, following the enactment of the Salary Standardization Law. The personnel bill of the National Government has grown by 24% in each of the last three years. These developments should, however, be evaluated in the context of the following points. First, much of the increase in public sector employment is of an accounting nature in that it reflects the "regularization" of a large number of persons previously listed as contract or temporary workers. These workers were, for all practical purposes, part of the public sector labor force but previously not recognised as such. Some are reported to have been on temporary status for over twenty-five years. The present Government has decided to "regularize" the status of these employees in order to promote fairness (in the award of pensions and fringe benefits, for example), in the process enabling a more accurate estimate of the public sector labor force. Second, the public sector in the Philippines is relatively small despite recent growth. Total public sector employment amounts to less than 6% of the labor force. Indeed, the Philippines public sector is lean compared to some of its neighbours. For example, public consumption is the lowest relative to total consumption in the Philippines as compared to Thailand, Malaysia and Indonesia, and well below the average for Asia. As far as compensation levels are concerned, the recent upward adjustments follow several years of declining real levels of compensation and, therefore, appear relatively large. Nevertheless, recent trends are disquieting: both the share of the public sector in the labor force and the share of public consumption to total consumption have been rising. A continuation of these trends would not be in the interests of economic efficiency.

3.55 Unionization. Unionization has increased in recent years, moderately in the private sector and substantially in the public sector. This has occurred largely in response to accommodating legislation introduced by the present Government. In the public sector, union membership climbed 30% last year to a level of around 77,500 members. In the private sector, union membership is now reckoned to amount to around 2.9 million persons or 12% of the total work

Table 3.13: PUBLIC SECTOR EMPLOYMENT & COMPENSATION 1/

	1986	1987	1989
Numbers Employed by Branch of Service ('000)			
National Government	832	682	954
Government Corporations	103	134	251
Local Government	202	255	220
State Educational Institutions	511	60	51
Total	1,188	1,131	1,476
Public Employees/Total Labor Force (%)	5.4	4.8	6.0
Personnel Expenditures (Billion Pesos)			
National Government	25	33	51
Growth Rate (%)		24	24

1/ Employment data based on Civil Service Commission Surveys. No survey was done in 1988; for 1989, the data are as of June.

Table 3.14: COMPARATIVE PUBLIC CONSUMPTION RATIO 1/

	1980-86	1988
Philippines	9.4	11.3
Malaysia	24.1	22.5
Indonesia	15.8	13.7
Thailand	16.8	15.0
Asia Average	14.8	14.0

1/ Refers to rates of public to total Consumption.

Source: World Bank Data (SAVEM, 1990)

force, having risen by about 800,000 in the past year alone. Despite recent gains, however, the level of unionization in the private sector remains relatively low and the power of unions to influence the general level of wages relatively weak.

3.56 The main mechanism through which labor unions influence the wage setting process in the industries in which they are present is the collective bargaining agreement (CBA). The extent to which CBAs are successful in raising the level of real wages is unclear but unions appear to be successful

in enforcing labor policies, especially with regard to minimum wages. While average compliance has been relatively low and decreasing since 1986, according to both industry and union sources, compliance is much higher in sectors in which unionized labor has been significant.[4]

3.57 The influence of unions on effective labor costs is determined also by their attitude towards labor disputes. In 1985-86, such disputes were very prominent. There were a large number of strikes affecting a large number of establishments and involving a substantial number of workers. It is estimated that almost 3.6 million man-days were lost to strikes in 1986. To the extent that these strikes were concentrated in the manufacturing sector, their effect was disproportionately high in that sector and encouraged a move to sub-contracting and capital-intensive lines of business. The more recent picture of industrial relations is more encouraging. Since 1986, the number of industrial disputes as well as the resulting economic losses have been steadily and quite rapidly declining. The total number of new strikes declined in 1989 to 197 resulting in 955,000 man-days lost, or a decline of 74%. This remarkable decline has been achieved primarily because of the strong desire on the part of both labor and management to solve their disputes through amicable settlements and collective bargaining. The rise in unionization has, therefore, not been accompanied by an increase in industrial disputes.

3.58 Interventions in Compensation Policy. The present Government has intervened in the formulation of compensation levels for private sector employees by maintaining the practice of setting minimum wages and several elements of non-wage benefits by legislation. For example, in 1989, minimum wages were raised substantially for all groups of low-scale employees; non-agricultural workers received an increase of around 48%. Such interventions, however, may seem more distortive than they really are. First, minimum wage legislation is easily circumvented, either by outright non-compliance or by an increase in sub-contracting. Surveys routinely reveal high levels of non-compliance. In a market characterized by substantial underemployment of unskilled workers, it is unlikely that minimum wage legislation can be made to

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4/ In the most recent period, the newly filed CBAs have resulted in wage deals mainly in transport (including storage and communications), manufacturing and agriculture. These three sectors cover about 76 percent of all workers whose wages are subject to collective bargaining agreements. The compliance rates in these sectors have been higher than in sectors such as electricity (rural cooperatives), mining or construction where the union presence has been less visible. The data are shown in Tables D11 and D12 in the appendix. The compliance rates have also been higher in the National Capital Region, where unions play a more important role than in the provinces. All these indicators would suggest the positive impact of CBAs on the rate of compliance.

Table 3.15: NUMBER OF ACTUAL STRIKES, AND MAN-DAYS LOST
1985-89

	Number				
	1985	1986	1987	1988	1989
TOTAL STRIKES	413	597	484	297	206
Pending, Beginning	42	16	48	30	9
New Strikes Declared	371	581	436	267	197
Cases Disposed	397	549	454	288	194
Workers Involved (000)	111	169	90	76	57
Man-Days Lost (000)	2,458	3,638	1,908	1,525	955

Sources: Bureau of Labor and Employment Statistics. Yearbook of Labor Statistics, DOLE.

stick.[5] Second, the overall behavior of wages in the Philippine economy is determined by several other, more important factors. In recent years, one such factor has been the increasing demand for labor associated with the economic recovery. This has tightened the labor market somewhat and led to increases in both nominal and real wage rates. Between 1986 and 1989 employment has risen at around 2% a year and unemployment has fallen from around 11% to around 8.5%.

3.59 Another significant factor has been the demand for Filipino labor abroad. Despite the growing domestic demand for labor, external migration remained high throughout the period as many Filipinos were attracted by better job opportunities abroad. The total number of processed contract workers increased quite dramatically after the crisis of 1983-1985, rising by 22.9% between 1986 and 1988. This migration has affected particularly the market for skilled labor in addition to that for domestic help. The supply of labor has probably also been somewhat affected by recent changes in social security regulations permitting early retirement. Since most workers close to the retirement age are more skilled than newcomers into the labor market, this step has affected the supply and wages of skilled workers.

5/ This is not to say that minimum wage legislation has no bite in specific sectors. Mining, for example, is critically affected by such legislation because it employs a large number of unskilled, low-wage workers and the sector is made up of large companies which have limited ability to sub-contract and which are easier to monitor for compliance.

Table 3.16: LABOR COMPENSATION MEASURES 1/
(Annual Growth Rates, Percent)

	1985	1986	1987	1988	1989
1. Real Compensation Per Employee	-	-	12.8 2/	7.2	10.5 3/
2. Real Minimum Wages (1978 prices)					
A. Non-Agricultural					
NCR	-2.5	-5.0	-4.4	8.1	9.0
ONCR	-4.4	0.2	-1.0	11.7	7.9
B. Agricultural					
Plantation	-4.8	0.2	-1.1	13.2	11.1
Non-Plantation	-3.5	0.1	-0.8	19.0	5.8
3. Daily Real Wages	-	5.1	4.8	6.8	-
4. Daily Real Wages in Manuf.					
A. Skilled	-11.4	-1.8	6.6	-	-
B. Unskilled	-3.7	-5.0	-1.2	-	-

1/ Compensation includes all earnings in cash and in kind and employers' contribution to social security. Daily wages on Line 3 are based on National Wages Council definition, those on line 4 refer to Metro Manila only.
2/ Increase between first and fourth quarter.
3/ Data refers to the third quarter.

Source: Current Labor Statistics (DOLE, BLES), March 1990, Edna Reyes and Ma. Teresa C. Sanchez: An Assessment to Labor and Employment Policies in the Philippines, 1986-88, Manila: PIDS, Working Paper No. 90-09, pp. 22-23 and National Wages Council. International Labor Office, cf. in Gysbert and Papola, p. 39.

3.60 Role of Government. Thus, while nominal and real wages have grown in the Philippines in recent years, the explanation for this probably has more to do with trends in the demand and supply of labor than with induced distortions arising from Government policy or union action. Nevertheless, Government policy should be directed towards keeping the public sector trim and should be non-interventionist as far as wage-setting in the private sector is concerned. While recent interventions may have been inconsequential relative to other factors, if recent trends continue they could certainly have much more substantial effects on overall economic efficiency. In this regard, the enactment of legislation (in June 1989) to transfer the wage-recommendation decision to regional wage and productivity boards with tripartite

representation may help in depoliticising the process and linking future wage increases more firmly to productivity gains.

3.61 One area in which Government intervention could have a positive effect is that of productivity improvement. As indicated before, Philippine labor productivity is low and has not significantly increased in the last twenty years. Trade, finance and industrial policy have contributed to this state of affairs. Indeed, as far as unit labor cost comparisons are concerned, it is probably exchange rate policy that has been the most important determinant of relative competitiveness in recent years. From the point of view of labor skills, however, an important consideration is the low expenditure of the Philippines on science and technology education and R&D. This has resulted in a shortage of key skills necessary to increase value-added in the economy and to make the transition to a more sophisticated manufacturing base. Compared to the NICs as well as to some of its ASEAN neighbours, the Philippines has among the lowest number of scientists and engineers per million population and share of R&D expenditures to GNP.

F. Rationalization of Public Corporations

3.62 Background. The growth of public assets in the Philippines came about from two sources: "statism" in the 1970s and the acquisition of non-performing assets from a number of public corporations on account of default on Government guaranteed loans. Statism under Marcos led to the Government's penetration into the economic arena across a broad front. A variety of corporations were set up with public funds, some directly with Government equity and some indirectly through large Government loans. During this period, two public sector banks, the Philippines National Bank and the Development Bank of the Philippines, became the largest corporations in the banking system. Ironically, the failure of these two banks in the mid-1980s enlarged the size of the public sector by putting a large number of foreclosed and non-performing assets into Government hands. The Aquino Administration introduced a reform program with the following main features: all acquired non-performing assets were to be sold to the private sector while, from among the public corporations, some were to be privatized while others would be abolished, consolidated, or merged with existing line agencies as appeared necessary following a review of their financial and organisational role and capabilities.

3.63 Progress of Program. The rationalization program has been relatively successful in disposing of acquired assets but not so successful in meeting its objectives with respect to public enterprises. For example, as of end-June 1990, 210 of 399 non-performing assets had been sold, recovering about 20% of book value on average and raising about P12 billion pesos for the Treasury. This is widely considered to be creditable progress. On the other hand, by mid-1990, only about 26% of target public corporations had been effectively privatized (32 out of 122) and only 48% of target had been abolished. Indeed, there has been some backtracking also: 23 corporations originally identified for privatization were later reclassified for retention in the public sector. The bulk of the disposition (especially privatization)

program remains to be implemented even though more than half the time allotted in the original schedule has elapsed.

Table 3.17: STATUS OF PRIVATIZATION PROGRAM
(As of end-June 1990)

Government Corporations	
PCGR Recommendation	132
Approved by President	122
Offered for Sale	39
Number Sold	32
Sales Value	P6.34 billion
Disposition of Acquired Assets	
Number Acquired	399
Number Sold	210
Sales Value	P12.1 billion
Other Collections	P6.4 billion
Amount Remitted to Treasury	P12.0 billion

Source: Department of Finance

3.64 Impact of Program. The potential impact of the rationalization program could be significant not only for the public sector fiscal accounts but also for overall economic efficiency. The public corporations account for a significant chunk of the assets and employment in the economy. However, so far, the impact of the program has been relatively small. This is especially true of the privatization program which has yielded only about P12 billion in three years to the Treasury. While the flow of subsidies to public corporations has been reduced in recent years, several "hard" cases--involving corporations receiving large subsidies from Government and/or having substantially negative net worth--have yet to be dealt with.

3.65 The potential fiscal impact of the privatization program should be assessed in light of the fact that many of the large public corporations (excepting those in public utilities) have substantial negative net worth and will be expensive to unload. For example, a list of 14 large public corporations, including Philippines Airlines and the Manila Hotel Group, two of the best known of Government properties, would fetch only 3 billion pesos if sold at net worth. In many cases, Government may have to offer substantial cash payments or accept liabilities in order to divest these corporations to the private sector.

Table 3.18: SUMMARY DATA FOR LARGE GCs TO BE PRIVATIZED

Corporation	Total Assets	Ttl Liabilities	No. of Employees
Philippine Phosphate Fertilizer Corp.	10898.4	9716.4	1157
National Sugar Regineries Corp.	1651.1	1647.1	1613
Semirara Coal Corp.	1178.0	593.2	1169
Food Terminal, Inc.	702.8	872.2	1544
Metro Manila Transit Corp.	628.0	566.0	1891
Bicolandia Sugar Devt. Corp.	269.7	830.2	874
Philippine Airlines, inc.	10788.4	12698.9	9899
Philippine Assoc. Smelting & Refin. Corp.	8946.7	7980.5	1113
National Steel Copr.	6297.0	4018.2	3410
NDC-Guthrie Plantations, Inc.	520.8	403.5	1311
Manila Hotel Corp.	286.3	45.7	1046
NDC-Guthrie Estates, Inc.	186.4	86.4	1038
Luzon Integrated Services, Inc.	14.5	13.4	1817
National Service Corp.	11.1	9.1	3090
TOTAL	42379.2	39480.8	3097.2

3.66 Factors Affecting Privatization. Legal and technical problems have dogged the privatization program so far. The law gives substantial rights to original owners to block sales of assets even after foreclosure. Government has had to negotiate with owners and has typically given them right of first refusal. At least 50 non-performing assets are presently under litigation brought by former owners. In some cases, the litigation has continued since the first year of the program, as for example in the case of MERALCO, the Manila electricity distributor.

3.67 Bureaucratic factors have also impeded privatization. Bureaucratic interests have become entrenched since management of public enterprises brings perks and patronage opportunites. This factor was probably resposible for the reversion of some corporations from the privatization list to the retention list. There has also been a concern about timing. It has been argued that quick sales should not be attempted, that the intrinsic value of the enterprises was high and that there would be significant benefits to waiting for a better time to sell as well as to undertaking rehabilitation measures.

3.68 Private Sector Concerns. Mixed performance on privatization and the contradictory signals emanating at various times from Government on this issue have led to cynicism about the overall privatization program on the part of the private sector. There is a concern that the factors which have impeded privatization so far may become even more important in the future as the original political motivation wanes in the run-up to the next election. There are also some concerns about the distribution of the benefits of privatization. Much of the buying activity so far has been confined to local

business elites and their foreign partners; the broad business class has not participated largely because of resource considerations. Furthermore, privatization has mostly involved direct sale of assets to a single buyer rather than a sale of stocks to a large number of shareholders or employees. As a result it has not had much of an effect on capital market development. A prominent exception to this is the partial privatization of the Philippine National Bank, 30% of the shares of which were sold to the public to considerable oversubscription and a spectacular run-up in the post-offering price. This sale generated much interest and activity in the local stock market and there is clamor for a further and similar divestment. Finally, there is a concern that privatization has not improved competition in key areas. Most of the units so far privatized were in competitive sectors to begin with whereas the corporations that effectively enjoy monopoly or oligopoly positions have not yet been privatized. As a result, one cannot say that privatization has resulted in a better market structure overall.

3.69 Some Recommendations. In the current context of pressing fiscal need privatization could play a very important role not only by providing some cash up front to the Government, but also by stopping the drain on fiscal resources entailed by many public corporations. Towards this end Government has recently made the following proposals: to accelerate its privatization program, to reduce tax exemptions and subsidies presently enjoyed by some public corporations, and to reduce the deficits of public corporations through better management.

3.70 Under the accelerated privatization program it is envisaged that up to 50% of the total assets marked for privatization will be offered for sale by the end of 1990. It is expected that several Government financial institutions will also be partiallly or fully divested. In particular, it is expected that there will be a further divestment of PNB as well as public offerings of the stocks of Republic Bank and Union Bank.

3.71 As far as budgetary support of public corporations are concerned, there has been significant progress under the present Government. Since 1986-87, most tax exemptions have been eliminated, the level of capital equity infusion reduced significantly, and public corporations have been made to pay market interest rates on their borrowings from the Government. However, some public corporations still enjoy tax exemptions and subsidies on the grounds that they provide goods or services of considerable social merit. Government proposes to review the justification of these exemptions to see if further pruning is possible.

3.72 While the deficits of public corporations are lower now than only a few years ago, there remains room for improvement. Government has taken steps to improve the management of public corporations by introducing a number of innovations such as monitoring, corporate planning and performance evaluation systems. Such systems were implemented in four public corporations in 1989 and it is expected that they will be extended to several others by the end of the year. Together with these measures, it will be important to continue to improve the collection performance of major public utilities by raising user charges in line with costs and by resolving delinquent accounts speedily.

G. Taxation and Efficiency

3.73 Several aspects of the tax system affect economic efficiency. Among these are tax rates, tax structure, and collection efficiency. Tax rates are not a major source of concern in the Philippines since they are low as well as comparable to those levied in competitor countries. Following the tax reform of 1986, the highest tax rate on corporations was lowered to 35%. More significant sources of concern are the tax structure and tax collection performance.

3.74 Tax Structure. The tax structure shows an excessive reliance on indirect taxes, a reliance which has not decreased over time despite increases in per capita income. A high proportion of indirect taxes indicates a higher distortionary effect for a given level of taxes. Table 3.19 shows that the ratio of indirect taxes to total taxes has remained constant at around 70% on average during the last five years. Direct taxes form a low proportion of total taxes as well as of GNP. In this respect, the Philippines compares unfavorably with such countries as Indonesia and Malaysia (see Table 3.20). The comparison with Indonesia is particularly interesting since the Philippines has a higher level of per capita income and yet shows a much higher reliance on indirect taxes. In particular, the Philippines derives a comparatively larger share of its revenues from import duties, a feature which could affect the relative competitiveness of Philippine business.

Table 3.19: STRUCTURE OF TAXES

	1985	1986	1987	1988	1989
Direct Taxes 1/	30	29	25	29	30
Indirect Taxes 2/	70	71	75	71	70
Import Duties	26	26	30	28	32
Others	44	45	45	43	38
Total	100	100	100	100	100

1/ Refers essentially to direct income taxes.
2/ Refers to sales, excise, VAT, tariffs, etc.

Source: Department of Finance

3.75 Despite the constancy of some elements of the tax structure, there have been some improvements in recent years. In particular, tax reforms in recent years have resulted in the replacement of a variety of sales taxes by a VAT, in the removal of export taxes, and in a shift away from commodity taxation. Together with the reduction in marginal tax rates, these constitute a significant reform effort. The scope for further improvement lies not in

further fiddling with tax rates and types but in improving collections. Improved direct tax collections will improve the tax structure.

Table 3.20: COMPARATIVE TAX STRUCTURES AND COLLECTIONS (1988)

	Indonesia	Malaysia	Thailand 4/	Philippines
Direct Taxes 1/	10.5	8.8	3.0	3.2
Indirect Taxes 1/	5.7	8.4	11.0	7.6
Import Duties 1/	0.9	2.8	0.3	3.0
Tax Effort 2/	16.2	17.2	14.0	10.8
Revenue Effort 3/	18.6	25.8	17.4	13.7

1/ Ratio to GNP.
2/ Ratio of tax collections to GNP.
3/ Ratio of total revenue collections to GNP.
4/ Budget figures.

3.76 Tax Effort. As Table 3.21 shows, tax revenue rose during 1985-89. The increase in 1989 was especially large and significant in that it represented the highest tax effort achieved in the last decade. Collections by both the Board of Internal Revenue (BIR) and the Bureau of Customs (BOC) reached record levels in 1989. If improvements in the tax effort are maintained at this level, the Philippines could reach the levels normally achieved by its ASEAN neighbours.

Table 3.21: REVENUE COLLECTION TRENDS
(Shares of GNP, Percent)

	1985	1986	1987	1988	1989
Tax Revenues	10.2	10.6	12.2	10.8	12.6
BIR	7.4	7.8	8.5	7.8	8.6
BOC	2.8	2.8	3.7	3.0	4.0
Non Tax Revenues	1.3	2.2	2.2	2.9	3.2
Total	11.5	12.8	14.4	13.7	15.8

3.77 Recent increases in tax collections, however, have come from increases in the relevant bases rather than from improvements in collection efficiency. For example, while customs collections rose to a record 4% of GNP in 1989, this was mostly due to an increase in the value of imports. Indeed, measured as a ratio of imports, customs collections in 1989 were about the same as the average for the last five years.

3.78 A similar case might be made with respect to the improved collections of the BIR. While the ratio of BIR collections to GNP has improved, the 1989 performance was due largely to special factors that may not be repeated in later years and that, in any case, have a somewhat mixed fiscal impact. For example, much of the increase in BIR collections in 1989 came from taxes on bank deposits placed by the Treasury with the Central Bank. This constitutes a transfer from one Government agency to another and its fiscal impact is neutral. Some of the increase in collections also came in the form of interest withheld on Treasury Bill transactions arising from both an increase in the volume of such transactions and in average interest rates. This too represents a transfer from one agency to another since the Treasury is the issuer of such liabilities and the incidence of the withholding tax in this case is probably all on the issuer. Finally, it should be noted that corporate and individual tax collections fell below target in 1989.

3.79 Collection Efficiency. Collection efficiency might be measured by the ratio of amounts collected to resources spent on collection efforts. Data from the Board of Internal Revenue show conflicting trends depending on how collection effort is measured. If collection effort is measured by the enforcement budget, it would appear that there has been a sharp drop in efficiency between 1985 and 1989; a peso spent on the enforcement budget gathered around 358 pesos in 1985 as compared to only 228 pesos in 1989. On the other hand, if collection effort is measured by the total administrative budget of the BIR, it would appear that there has been a modest improvement in collection efficiency (see Table 3.22).

Table 3.22: SELECTED MEASURES OF TAX COLLECTION EFFICIENCY

	1985	1986	1987	1988	1989
Customs Collections/Imports	15.5	15.0	16.5	12.6	15.1
BIR Collection Efficiency					
Relative to Enforcement Budget	358	470	211	229	228
Relative to Admin. Expenditures	110	118	131	125	128
VAT Collection					
Relative to Potential				0.38	

3.80 Recent VAT Performance. The VAT system is clearly improving. The number of registrants and filers have increased and the ratio of filers to

registrants has also increased. There also seems to be increasing understanding and acceptance of the VAT concept among the tax-paying public. Nevertheless, VAT collections, while rising, continue to fall below target. In 1988, the first year of the program, the shortfall in collections was blamed on a late start of the program (in April); in 1989, the shortfall was blamed on an inadequate collection budget (reflected in fewer personnel hired to collect VAT than thought necessary). Whatever the reasons, performance has not only been below targets but also consideraby below potential. The potential collection from VAT, based on national accounts estimates of value-added, is huge and at present less than half the potential tax is being collected. Indeed, this is one of the main criticisms of attempts to raise tax rates: much more can be done by simply improving collection.

3.81 In this regard, recent measures announced by Government to improve tax administration are steps in the right direction. These measures include, for the Bureau of Customs, the voluntary acceptance of payments on delinquent accounts, the expansion in the scope of pre-shipment inspections, the increased computerization of operations, and the intensification of anti-smuggling operations. For the BIR, such measures include the stamping and registration of receipts, the affixing of strip stamps to cigarette and liquor packages, and the creation of special tax courts. It is hoped that such measures will yield a total of P2.1 billion in additional revenue in 1990 and P7.4 billion in 1991.

H. Infrastructure and Efficiency

3.82 The main infrastructure issues which affect efficiency and competitiveness in the Philippines relate to the reliability of electricity, the adequacy of transportation infrastructure and the anti-competition nature of the regulations governing the supply of transportation.

Power

3.83 Reliability of Power Supply. The power sector was severely affected by the investment cuts of the macroeconomic stabilization program of the mid-1980s. Virtually no new investments were made in power generating capacity then and, in addition, a major product of earlier investments--a 620 MW nuclear power station--was mothballed in 1986 for safety and financial considerations. The economic recovery experienced since 1986 has exposed the true cost of underinvestment in the power sector. Power demand has soared at the rate of 10% per annum while supply has grown slowly, and that too from operating existing power plants at above capacity from a maintenance point of view. During 1989 and 1990 periodic shutoffs of power have been a major problem for the industrial sector in particular.

3.84 The power crisis that gripped the Metro Manila area in the first half of 1990 exposed several deficiencies in the performance of the power sector. First, it revealed a lack of planning and coordination among the key agencies that operate in this sector. There has been slow implementation of alternatives to the nuclear power program that was abandoned in 1986. Second, it exposed the vulnerability of the generation system to low reserves and to

drought. The drought reduced water levels in key reservoirs and led to a reduction in the output of hydroelectric power plants. Third, it reflected the effects of inadequate maintenance in that there was a high frequency of breakdowns of some of the older power plants.

3.85 In the short run, the availability and reliability of power can be improved by permitting the private sector to import and use generators. This has been Government policy in recent years and has no doubt lessened the impact of rising power outages in recent months. Another short-run solution is the installation of oil-based combustion turbines. The commissioning of 400MW of such turbines was to be accomplished in 1989 but was delayed due to implementation problems; this delay has featured prominently in the power crisis experienced in 1990. An idea of the growing reliance on imported energy to balance domestic demand and supply may be gained from Table 3.24 which shows the proportion of oil-based generation (most oil is imported) to rise from around 42% in 1989 to around 50% by 1992.[6]

3.86 In the long run, the solution lies in further investments in generation and distribution capacity. A promising beginning towards this was made in 1988 when a new power development program was formulated with the aid of the World Bank Energy Sector Study. Under this program, the National Power Corporation will install 1805MW of generating capacity during 1993-96, utilizing geothermal energy as much as possible and coal-fired or hydroelectric plants as a second-best option. It is anticipated that the private sector will be given a large role in energy exploration and processing under this program. If the present program is implemented on schedule, the country will acquire sufficient domestic generating capacity by 1996 to support its industrial and residential needs on a sustained basis; its reliance on imported feedstock (oil) will also stabilize at a level of around 40% by then.

3.87 Electricity Costs. Despite recent improvements in electricity tariff policy and in the operating efficiency of the principal electricity suppliers, the business sector in the Philippines faces high electricity costs. This is partly because of reliance on imported feedstock (mostly oil and coal) to generate electricity and partly because of high, albeit recently declining, levels of technical and nontechnical (pilferage) losses. Under local regulations, the cost of such losses can be passed along to consumers and electricity companies have little incentive to reduce such losses.

6/ The power supply situation has eased considerably in the last few months as heavy rains have increased hydroelectric capacity and a rehabilitated plant has been brought on line. With the imminent commissioning of a 200MW combustion turbine, the likelihood of further power problems in 1990 is considerably reduced.

Table 3.23: COMPARATIVE ELECTRICITY COSTS (1989)
(Pesos per KWH)

	Residental	Industrial	Overall
Thailand	1.50	1.32	1.51
Hong Kong	1.64	1.43	1.46
Korea	2.06	1.48	1.71
Singapore	1.49	1.13	1.26
Japan	3.34	2.45	2.66
Indonesia	1.52	1.12	1.42
Malaysia	1.71	1.15	1.48
Philippines	1.43	1.50	1.48

3.88 The cost of generating power will rise during the next two years since the only additions to capacity in the energy-short Luzon area are to come from oil-fired combustion turbines which are the most expensive source of generation. The earliest contribution to power supply from a non-gas turbine source will be in 1992. The proportion of oil-based capacity to total capacity in the Luzon grid (which supplies Metro Manila and a sizable chunk of Philippine industry) will rise from 50% in 1989 to about 63% in 1992 (see Table 3.24).

Table 3.24: POWER GENERATION PLANS
(in GWH)

	1989	1990	1991	1992
Total Generation	24088	26464	28217	30713
of which				
Oil Based	10078	12879	13943	15388
% Share	42	49	49	50
Luzon Grid Generation	18223	19779	20996	22597
of which				
Oil Based	9150	11490	12989	14292
% Share	50	58	62	63

3.89 The pressure of costs on industrial users can be reduced somewhat by further reduction of the cross-subsidy presently provided to residential and other users. The structure of power tariffs has been improving over the past few years as residential rates have risen while industrial rates have fallen (see Table 3.25). There remains room for further adjustment, however, since

the cost of service to the industrial sector is about 25% less than the cost of service to the residential sector whereas the present rates are still slightly in favor of residential users.

Table 3.25: TRENDS IN ELECTRICITY COSTS
(Pesos per KWH)

	1986	1987	1988	1989
Residential	0.98	1.14	1.33	1.43
Industrial	2.18	2.10	1.76	1.50
Overall	1.72	1.73	1.61	1.48

Source: NEDA

3.90 Costs can also be reduced by improvements in efficiency. There have been positive developments in this aspect in recent years. For example, electricity losses of the National Power Company (NPC) declined from 8.6% (as a percentage of available energy) in 1985 to 7.7% in 1988. The losses of MERALCO, the major electricity distributor for Metro Manila, declined from 22.6% in 1986 to around 17% in 1988 and an estimated 16% in 1989.

3.91 In addition to technical and nontechnical losses, the business performance of electricity companies, especially with respect to the recovery of receivables, can also affect costs. There has been some improvement here also. NPC's collection rate (measured as year-end receivables for supply in terms of average weeks sales) declined from 15.3 in 1986 to 6.1 in 1988 while MERALCO's declined from 9.1 in 1986 to 6.1 in 1988.

Table 3.26: INFRASTRUCTURE INDICATORS

1989	1985	1986	1987	1988
Number of Operational Ports				
Total	592	607	606	392
Ports of Entry	38	38	24	19
Municipal	231	237	231	85
Number and Length of Bridges				
Total	19738	11740	11572	11289
National	9308	7379	7211	6928
Total Length (000 metres)	438	308	304	314
National Bridges Length	225	230	225	235
Length of Roads (000 km)				
Total	9.3	9.4	9.6	9.8
National	6.1	6.2	6.2	6.2
Local	3.2	3.2	3.4	3.6
Gross Shipping Tonnage (million tons)				
Cargo Ships	4.2	4.1	5.8	4.3

Source: Philippine Statistical Yearbook, 1989

Transportation Infrastructure and Regulations

3.92 Trends in transportation infrastructure are shown in Table 3.26. It is quite clear from this table that there has been little improvement in recent years despite substantial growth in infrastructure demand arising from economic and demographic growth. The table shows all principal transportation infrastructure items to be either declining in quantity or showing minimal growth: the number of operational ports has shrunk from 607 in 1985 to 392 in 1988, while the number of bridges has shrunk from 11740 to 11289 over the same period. The road network has increased only marginally, from 9400 km in 1986 to 9800 km in 1988.

3.93 The above trends are related to fiscal stringency exercised by Government since 1986. Infrastructure expenditures have recently been kept on a tight leash: they have averaged less than 1.5% of GNP and less than 8% of total budget expenditures in recent years, considerably below historical levels. Furthermore, capital expenditures have been lower in real terms in the last few years when compared to the early 1980s. Similar patterns can be

detected in expenditures on operations and maintenance. It is no surprise then that the state of transportation infrastructure leaves much to be desired.

Table 3.27: TRENDS IN INFRASTRUCTURE EXPENDITURE

	1980	1986	1987	1988	1989
Percent of Total Expenditures					
Operations & Maintenance	28.2	13.6	15.6	14.4	15.5
Infrastructure Outlays	19.2	7.1	6.0	6.2	7.6
Levels (in billion Pesos)					
Operations & Maintenance	10.8	15.0	18.9	19.6	26.6
Infrastructure Outlays	7.3	7.8	7.3	8.4	13.1
Real Levels (in 1980 Prices)					
Operations & Maintenance	10.8	6.2	8.1	6.8	8.4
Infrastructure Outlays	7.3	3.2	2.8	2.9	4.1

Source: Department of Budget and Management

3.94 For example, a survey done by DPWH in 1988 revealed that only 18% of highways were in good condition, about 48% in fair condition and 34% in poor condition. The railways are almost non-operational and average speeds are less than 20 km/hr. Ports and navigational aids are generally also in poor condition.

3.95 Constraints on Sector Development. Over time, a number of contradictory, discriminatory and anti-competition regulations have accumulated in the transport sector that by now impede rather than enhance the growth of the sector as well as that of the economy (especially through exports). Among the most damaging regulations are the franchising requirements for passenger and freight services, single operator rules in some areas, measured capacity criteria to control entry into road and maritime transport services, and restrictions on the import of transportation equipment. These constraints on the development of the sector are well illustrated by the following discussion of interisland shipping and road transport.

Interisland Shipping

3.96 Cost of Service. Inter-island shipping is a major mode of freight and passenger transport in the Philippines. As such it affects costs across a

wide spectrum of Philippine industry. For various reasons the cost of inter-island shipping in the Philippines is relatively high, a feature that has kept the domestic market limited in size and has permitted fewer economies of scale to be achieved. By some measures, the economies of Mindanao and Luzon are less integrated between themselves than that of Luzon is with foreign countries. For example, it is reported that the cost of sea freight from Mindanao to Manila is higher than that from Bangkok to Manila, a considerably longer distance.

3.97 There are several reasons why costs are relatively high. First, there exist strict route regulations for both cargo and passenger scheduled liners and, on some routes, no more than one company is allowed to ply. Second, the liner industry is dominated by a cartel which negotiates rates with Government. While rates of return on investments are subject to ceilings imposed by Government, it is widely thought that the cartel is able to negotiate comfortable cost margins and adjustments. The regulations in place and the structure of the industry together tend to keep costs at the level of the least efficient member of the cartel.

3.98 Costs are also affected by the fact that the fleets in operation are made up of relatively old and energy-inefficient ships. The average age of cargo liners and trampers is around 20 years and has been rising over the last two decades. The number of ships in operation has also been declining. As a result, service is not only high-cost but also involves long waiting periods. The main reason why fleets are aging and declining is Government control over rates of return to investment and import restrictions on vessels and spare parts. The import restrictions make new vessel purchases very expensive while rate of return and route regulations discourage entrepreneurs from making the necessary large capital investments.

3.99 Finally, port handling charges and turnaround time are relatively high in the Philippines as compared to international norms; both of these aspects add significantly to shipping costs. For example, port productivity is only about 8 tons per ship hour in port while ship port times are as high as 70% of total turnaround time. Port handling is characterized by single operator arrangements in many locations and by the imposition of charges even when no services are actually needed or received by ships.

3.100 Recommendations. Shipping is a potentially competitive industry. There is little justification for having route regulations; at present they are simply bolstering the position of the cartel that dominates the liner trade. There is also little justification for having rate of return regulations once routes are opened to free entry. Such regulations are only keeping costs up at the level of the least efficient shippers and discouraging capital investment in the industry. Consequently, the most important step that Government could take to reduce costs and increase efficiency in inter-island shipping would be to deregulate entry, routes and rates. Regulations should only be imposed and kept in areas where safety is involved. Indeed, the "economic" regulations in place now might be compromising safety to the extent that they have led to underinvestment in fleet improvements.

3.101 Port operations should be improved and charges reduced. The practice of having only a few operators (stevedorers and arrastre companies) per port should be discontinued and efforts should be made to increase competition for port services by allowing any number to operate and letting ship agents decide who to use. Fees should be charged only for services received and should be based on the economic cost of the services rendered. If a vessel does not require port handling services, no charges should apply. The port privatization program should be accelerated and port development charges should not apply to private ports if Government has not actually invested in the facilities.

Road Transport

3.102 The Philippine road transport industry (comprising both interurban and urban passenger and freight services) is heavily regulated. As in the case of shipping, these regulations have succeeded in increasing costs and decreasing operator profits without achieving corresponding benefits in terms of safety or service. Regulations limit entry to the industry as well as operations within it (through route restrictions, for example). There are restrictions on vehicle ownership (import bans on vehicles below 18 ton GVW) as well as on fare levels. High import taxes apply to most vehicle classes and to spare parts. In addition, the road transport business is subject to a special surcharge tax, called the Common Carrier Tax. All of these restrictions make the industry relatively unattractive for existing as well as potential investors and have resulted in an industry characterized by declining, deteriorating and aging fleets. Over the last few years, the number of buses in the country, and in Metro Manila in particular, has decreased in absolute terms, and the fleet of utility vehicles and trucks has increased at less than the rate of population growth.

3.103 Improvements in road transport must combine thorough deregulation with a fleet expansion and modernization program. The supply of vehicles could be increased by lifting import restrictions; there is little hope of meeting requirements in a timely and cost-effective fashion through higher domestic production. Route and rate regulations should be progressively abolished and regulatory emphasis should be diverted instead to safety considerations. Taxation of the industry should be rationalized so as to be consistent with principles of user-charges, congestion avoidance and pollution abatement.

IV. PROJECTIONS AND FINANCING REQUIREMENTS

A. Introduction

4.1 The discussion in the previous chapters indicates that the Philippines needs to direct its economic strategy, first, at restoring macroeconomic balances by reducing domestic debt accumulation and, second, at enhancing economic efficiency and international competitiveness to support growth in the traded sector. These priorities are clearly established by the domestic developments in 1989-90, as discussed in the previous chapters. Most recently, external shocks caused by the Middle East crisis make the implementation of this strategy even more urgent, in order to avoid a replay of the 1983-86 crisis. The major difference under the current circumstances is that the Philippines is now burdened not only by high external indebtedness but also by a high level of domestic debt.

4.2 The necessary ingredients for this strategy include consistent macroeconomic policy and a strong structural reform package. The former is needed to effect the necessary fiscal adjustment with the lowest costs--in terms of current and future growth; the latter is needed to remove the sources of inefficiency that most directly affect those costs and to realize the country's economic potential. In addition, as a consequence of the Middle East crisis, the strategy will need a stronger fiscal effort and a higher level of external support in order to be implementable.

4.3 Strong emphasis is to be placed on the consistency of the adjustment strategy, as an indispensable condition for its success. Slippage in the fiscal area can be offset temporarily by tightening the money supply, but at the cost of a larger fiscal adjustment or higher inflation in the future. Furthermore, when the real interest rate is higher than GDP growth, the necessary fiscal adjustment cannot be postponed without incurring high--and increasing--costs, as the interest bill on the stock of domestic debt grows faster than the economy's ability to finance it.

4.4 Remaining structural constraints, identified and discussed in Chapter 3, need to be removed, in order to decrease the costs of the adjustment process and realize the economy's potential. A clear lesson from the experience of successful adjusters is that external borrowing constraints and limited domestic savings inevitably lead to high real interest rates during the adjustment process. Thus, increasing competitiveness and efficiency of financial markets is crucial to reducing the cost of adjustment. Furthermore, a clear lesson from Philippines' closest trade competitors is that a outward-oriented strategy is vital to growth for a labor rich-capital poor country. The Philippines needs to recover, in terms of international competitiveness, the ground lost in 1988 and 1989, when the real exchange rate appreciated both relative to trade partners and competitors. The fact that the performance of Philippine exports has been remarkable in spite of these unfavorable developments underscores the export potential of the country but also suggests that their adverse effect may show with a lag. These considerations indicate the urgent need for a more aggressive exchange rate policy, the removal of remaining anti-export bias to effectively support exporters and promote the

development of efficient backward linkages, and the establishment of a regulatory framework that does not discourage foreign investment.

4.5 While projection exercises are necessarily indicative, they are useful to assess consistency, identify potential sources of instability, and quantify trade-offs. The scenarios presented in this chapter are obtained from a consistency framework, not from a comprehensive predictive model. They are not meant to represent complete stabilization packages, but rather to illustrate how the burden imposed on the economy by the growing domestic debt can be contained and even reduced, by means of decisive fiscal action. These results are obtained under the assumption that policy variables other than fiscal do not exacerbate the fiscal situation. In addition, the scenarios presented here estimate additional financing required to sustain moderate consumption growth--about 1% per capita per year in 1990-1992, gradually reaching 2%--and investment growth--from 19% to 24% of GDP.

4.6 This report has been less preoccupied with foreign debt than previous ones not because of a disregard of the burden it places on the Philippine economy, but rather because much was accomplished in the last few years in rescheduling and reducing foreign debt, with the recent Paris Club agreement and with the buyback of US$1.337 billion of commercial debt. The former agreement rescheduled the bulk of amortizations and a large portion of the interest payments due to bilateral lenders in the period 1989-92, or approximately US$2 billion. The latter retired, at a 50% discount, over one fifth of the debt eligible for DDSR under the Commercial Bank Financing Package of October 1989--which also defined the terms for future DDSR and contributed US$710 million in new money.

4.7 Although these agreements were major accomplishments, external debt still stands at approximately 68% of GDP, and interest payments alone on foreign debt continue to be approximately 20% of export revenues. Thus, the Philippines should continue to explore all avenues to further reduce foreign debt and debt service in a cooperative fashion, with a view to both alleviating its burden and ultimately regaining creditworthiness. To this aim must be added the more immediate problem of financing the new balance of payments deficit. It should be stressed that the domestic fiscal deficit in part results from the public sector servicing foreign debt while failing to raise sufficient revenues to finance it, and future foreign debt settlements should continue to be structured as to relieve, or at the least not exacerbate, the domestic fiscal situation.

B. The Policy Scenarios

4.8 In this chapter two policy scenarios, which represent adjustment efforts of different intensities, are discussed. In the first scenario, the Government introduces a basic revenue-enhancing package that gradually stabilizes the ratio of domestic public debt to GDP. In this case, the country continues to grow but fails to achieve its full potential, as the fiscal adjustment is not accompanied by the stimulus of increased efficiency and competition. In the second scenario, in addition to introducing stronger fiscal measures, the Government undertakes vigorous structural reforms in the

areas of taxation, trade, financial intermediation, and investment regulation. The rationale for distinguishing between these two cases follows from considerations regarding both implementation capacity and phasing of the adjustment effort.

4.9 In both scenarios, the macroeconomic strategy followed by the Government comprises strong fiscal measures complemented by prudent monetary policy, more active exchange rate management than in recent experience, and cautious foreign debt management. The fiscal measures combine a moderate increase in operation and maintenance (O&M) and capital expenditures with a strong revenue effort on both indirect and direct taxes, and includes acceleration of the privatization program. Monetary policy allows base money to accommodate current real GDP growth and inflation at about 10% per year. This inflation rate is higher than optimal; it is assumed here to emphasize that efforts need to be concentrated on reducing fiscal imbalances first. Finally, the Government continues to take advantage of the current market opportunities to reduce its commercial foreign debt through debt equity swaps of about US$1.5 billion in 1990-93.

4.10 There is uncertainty concerning the effect on official financing of the intensity of the policy effort by the Philippine Government. While lack of necessary macroeconomic adjustment would likely result in a drop in multilateral and bilateral aid, the additional effort on the structural reform agenda will probably not be rewarded by increased lending, at least in the short term. This is partly because the country has already accumulated a sizeable pipeline of official assistance and partly because the total ODA available to developing countries is not expected to grow in real terms. For these reasons, the two scenarios examined in this chapter have identical assumptions concerning official financing and incorporate the expected--and already discernible--improvements in disbursements. In the light of the events following the Middle East crisis, some additional assistance to the Philippines is possible; it appears however impractical to alter the outlook for foreign financing until new commitments are actually forthcoming.

4.11 Finally, there is much uncertainty concerning international economic prospects, in the light of the recent increase in oil prices. If this increase is sustained, it will likely be reflected in higher interest rates and lower world trade growth than has been expected. The two scenarios presented here assume continuing instability in the Middle East leading to oil prices averaging US$30 per barrel in the second half of 1990, US$29 in 1991, and gradually declining to US$20 thereafter. World inflation and nominal international interest rates increase in the same period, while world trade is projected to be affected only moderately.

4.12 This international economic outlook is very different from that prevailing before the outbreak of the Middle East crisis, and has dramatic implications for the Philippines. Prior estimates of financing requirements indicated a manageable external payments situation, with very small unidentified financing requirements until 1992; after the Middle East crisis, a cumulative financing gap of US$1.8 billion is projected for 1990-1991 alone. The Philippines is very exposed to an oil shock, as it imports its entire oil needs and is heavily dependent on oil-fired power plants. In addition, the

Philippines had approximately 28,000 registered contract workers in Kuwait and Iraq at the outbreak of the crisis, remitting an estimated US$50-75 million per year. (The total number of Filipino workers in the area, including unregistered "service" workers, is estimated at 50,000.) The impact of the Middle East crisis on world prices, interest rates and trade would also affect the Philippines substantially: one third of its total external debt is at variable rates, and exports of non traditional goods, electronics in particular, are very sensitive to world trade developments.

C. Case I: Restoring Macroeconomic Balances

Policy Assumptions

4.13 We first consider a scenario where adjustment is focussed on the fiscal side; progress on the structural reform front is limited to improvements in the regulatory framework for investment. The strategy is implemented as follows. The fiscal adjustment combines a conservative expenditure policy and a strong revenue effort. Non-interest current expenditures of the consolidated public sector[1] are maintained at their 1989 level, as a share of GDP, with the exception of O&M expenditures, which rise moderately. Investment expenditure increases gradually from 4 to 6% of GDP by 1992, as a consequence of the reconstruction effort after the July earthquake and pre-existing deficiencies in infrastructure. On the revenue side, improved tax administration as well as new tax measures raise total tax revenues from 12.7 to about 15% of GDP by 1992. In addition, revenue generation by public corporations improves moderately, by about 0.5% of GDP. These developments lead to an improvement of the primary balance of the consolidated public sector, whose surplus increases from 3% to 3.8% of GDP between 1989 and 1992.

4.14 Other fiscal developments, incorporated in the policy scenario for the shorter term, include the acceleration of the Government privatization program and the disposition of APT assets, estimated to yield P5 billion in revenues on average in 1990-92; the elimination of the deficit accumulated by the Oil Price Stabilization Fund through mid-1990, in 1990 and 1991; and subsequent regulation of the Fund to maintain it in flow equilibrium.

4.15 In the projection period, in spite of the continuing growth of domestic debt in the earlier years, domestic interest rates are projected to stabilize at approximately 10% in real terms, or approximately their current level. The stabilization of real rates is assumed to follow, in the first place, from the real exchange rate devaluation, which is expected to reduce the premium required by investors for holding financial assets in local currency; and secondly, from the improvement in the primary surplus of the public sector which eventually reduces borrowing requirements. As a result of the improvement of the primary balance and the stabilization of real rates, the interest bill on domestic debt stabilizes around its 1989 level--

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[1] The definition of consolidated public sector used here includes National Government, Local Government Units, Central Bank, and Non-Financial Public Corporations, but does not include Public Financial Corporations.

approximately 4% of GDP. The consolidated public sector deficit peaks in 1990 and 1991, as a result of the increase in investment expenditures, and then declines gradually to 4.3% of GDP in 1995.[2]

4.16 Exchange rate policy is characterized by a gradual devaluation, which entails a cumulative real depreciation of 10% between 1990 and 1991. The effects of the devaluation on the consolidated public sector deficit are incorporated in our projections: interest payments on foreign debt in local currency increase proportionately to the nominal exchange rate; trade and indirect taxes on imports are assumed to have unitary elasticity, in local currency at current prices, with respect to a nominal devaluation vis-a-vis the US$ and with respect to the value of imports; and the investment deflator is assumed to have an elasticity of .3 with respect to the same variable, so that investment becomes more expensive, relative to other expenditures, when the exchange rate depreciates.

4.17 Concerning the composition of financing of the consolidated public sector deficit, as discussed above, monetary policy is accommodating in the sense that it does not increase the current rate of inflation. Domestic inflation is assumed to reach 13% in 1990, as a result of the gradual absorption of excess liquidity created in late 1989, the effects of the recent earthquake, and the increase in oil prices; inflation gradually stabilizes at 10% for the rest of the period. The expansion in monetary base is thus equal to the rate of growth of nominal GDP, and the revenues from money creation are projected at 1.3-1.4% of GDP. This level of seignorage plus inflation revenues is not sufficient to finance the operating losses of the Central Bank and additional financing requirements for foreign reserve accumulation and debt equity swaps; the National Government is thus projected to continue the be a net lender to the Central Bank.

4.18 Concerning the assumptions underlying foreign financing, the consolidated public sector is projected to receive most of the long term foreign capital inflows in the country, including both identified and unidentified financing. As a result, projected net foreign borrowing accounts for about 2.5% of GDP on average between 1990 and 1992, and about 1% afterwards. Projected net flows of long term foreign capital are discussed below.

4.19 To summarize the policy assumptions underlying this scenario, the key actions on the part of the Government are:

- strong fiscal effort, comprising indirect tax rates increases and improved direct tax administration, yielding additional tax revenues of over 2% of GDP by 1992;

- increased privatization effort, raising cumulatively P15 billion in revenues during 1990-92;

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[2]If Public Financial Institutions are included, the consolidated public sector deficit in 1989 is 4.2 per cent of GDP instead of 5.1.

- modest increase in O&M expenditures (0.7% of GDP) and investment (2% of GDP), while other non-interest expenditures remain constant as shares of GDP;

- gradual devaluation of the real exchange rate in 1990-91, by about 10% cumulatively;

- prudent monetary policy, accompanying real GDP growth and maintaining inflation at 10% annually; and

- foreign debt management leading to a reduction of US$1.5 billion by the end of the period.

External Economic and Financing Assumptions

4.20 The world economic developments underlying the projection exercise assume short term uncertainty related to the Middle East crisis. Oil prices are assumed to average US$33 per barrel in the second half of 1990 and then to decline to US$29 in 1991 and US$25 in 1992. As a consequence, international inflation and interest rates increase in 1990 and 1991, while the growth rate on world trade in real terms decelerates moderately. Developments after 1992, as instability in the Middle East is assumed to subside and oil prices to stabilize in the US$20-22 range, have world trade growing in excess of 6% per year, in real terms, manufacture unit value index growing at about 5% until 1995 and then stabilizing at about 3.5%, and LIBOR declining to about 8%.

4.21 The trends in foreign financing observed in the most recent years are expected to continue in the forecast period: official lenders are expected to be the largest source of capital inflows throughout the projection period, while only limited commercial lending--in the form of short-term trade credit--is expected to be offered. The continued role played by official lenders implies a substantial increase in the absorption capacity of the Government, resulting from the various measures introduced in 1989 to improve project preparation and implementation. Disbursements by official lenders are assumed to increase from US$1.6 billion in 1989 to US$3.0 billion by 1998--an average 7% per year or about 2.5% in real terms. There is a sharp increase in disbursements by official lenders in 1990, due both the financing of the DDSR operation of January 1990 (approximately US$480) and the disbursement of US$85 million out of the projected US$500 million in emergency assistance following the July 1990 earthquake. Concerning IBRD flows, disbursements are projected to peak in 1990 at US$800; they later average US$600 million during 1991-94, and US$750 during 1995-98. Concerning private sources, financing of about US$900 million is projected in 1990--of this, US$710 million from the Commercial Banks Financing Package concluded in October 1989. Foreign investment--direct and equity--is expected to provide substantial financing for about US$0.8 - 1.0 billion per year, stimulated by real depreciation and the resumption of debt-equity swaps.

4.22 On the requirements side, repayments of foreign loans are projected to average about US$1.5 billion per year in 1990-92, rising above US$3.0 billion per year in 1993-98. The time profile of principal repayments results from several rescheduling and DDSR operations. First, the buyback of US$1,337

million of commercial bank debt in January 1990 is estimated to reduce interest payments by about US$140 million a year and to reduce amortizations--starting in 1994--by about US$100 million. Second, the Paris Club rescheduling agreement of May 1989 is projected to postpone to 1994-2000 the bulk of principal repayments and interest payments to bilateral lenders that fall due in 1989-92. Third, the conversion of 50% of outstanding "1985 New Money" loans (about US$300 million) into new bonds--according to the terms of the 1989-90 Commercial Bank Financing Package of October 1989--is to postpone repayments in 1998-2004 and slightly reduce interest rates. Finally, the projections incorporate a gradual accumulation of official reserves from a level equivalent to 1.6 months of imports of goods and services at end-89 to about 2 months by 1993.

Outcomes

4.23 Fiscal Adjustment. Table 4.1 reports the evolution of the consolidated public sector deficit, its financing, and the resulting accumulation of domestic and foreign debt in the scenario. As the real interest rate is larger than GDP growth, the primary surplus needs to continue to increase while the consolidated public sector deficit declines slowly over the period, as the share of interest payments declines. Given our assumptions on the other borrowing requirements of the public sector and foreign financing and money creation, the fiscal adjustment stabilizes the domestic debt-to-GDP ratio at about 24.5%, or 2 percentage points higher than at end-89.

4.24 GDP Growth. The projections are characterized by a substantial slowdown of economic activity in 1990-91: GDP is forecast to grow at 3.5 and 4.5% respectively in 1990 and 1991. This follows from several factors. In the first place, in the first semester of this year economic performance has been disappointing, mostly as a consequence of supply constraints--drought and power shortages. Secondly, the earthquake of July 1990 is expected to affect output through the disruption of transport and power distribution in Northern Luzon, and to affect exports directly as the Baguio Export Processing Zone has been damaged. Thirdly, while the impact of these factors is expected to subside in 1991, the increase in oil prices will necessarily have negative repercussions on economic activity. Finally, continuing high domestic interest rates will dampen demand growth domestically at the same time as world trade growth, while positive, is expected to decelerate.

4.25 The long-term growth trend of GDP is projected at about 5.3%, lower than observed in 1988 and 1989, partly as a consequence of the structural and macroeconomic factors discussed in the previous chapters--above all, infrastructure constraints and high real interest rates--and partly because of the additional adjustment effort necessitated by the new oil shock. Growth is expected to continue to stem mostly from investment and export. The increase in investment is supported by the increase in savings, which rise from about 15 to 22% of GDP between 1989 and 1998. The public sector contributes substantially to the increase in savings: savings by the consolidated public sector increase from -1 to 2% of GDP, as a result of the fiscal adjustment. The impressive increase in national savings nevertheless fails to raise the savings-to-GDP ratio to the average level of 25% observed in the 1970s. A

Table 4.1: Case I: Consolidated Public Sector

CASE I	1988	1989	1990	1991	1992	1993	1994	1995
ASSUMPTIONS _1/								
MUV Index _2/	7.5	0.9	6.2	9.5	5.0	5.0	5.0	5.0
LIBOR _3/	8.1	9.4	9.1	10.6	9.5	8.4	8.2	8.0
World Trade _4/	5.6	7.4	5.1	5.7	6.4	6.4	6.4	6.4
Oil Price _5/	13.3	16.4	24.8	29.0	25.4	22.0	20.0	20.0
Real Exchange Rate Depreciation	-0.5	-5.9	4.0	5.2	0.0	0.0	0.0	0.0
Domestic Interest Rate	14.7	17.5	24.3	23.2	21.0	21.0	21.0	21.0
GDP Deflator Growth Rate	9.8	10.1	13.0	12.0	10.0	10.0	10.0	10.0
GDP Growth in constant terms	6.3	6.1	3.5	4.5	4.7	5.0	5.3	5.3
CONSOLIDATED PUBLIC SECTOR _6/ _7/								
Total Revenues	19.6	20.8	22.0	23.4	23.7	23.7	23.7	23.8
Revenues excld. Interest	19.1	20.2	21.3	22.7	23.1	23.2	23.2	23.3
Interest Revenues	0.5	0.5	0.7	0.6	0.6	0.5	0.5	0.5
Total Current Expenditures	19.6	21.7	22.8	23.5	22.6	22.2	22.1	21.8
Expenditures excld. Interest	11.2	13.1	13.5	13.8	13.4	13.4	13.4	13.4
Interest Payments	8.4	8.6	9.2	9.7	9.2	8.8	8.7	8.5
Domestic Debt	4.2	4.5	4.7	4.7	4.3	4.3	4.4	4.5
Foreign Debt	4.1	4.1	4.5	5.0	4.9	4.5	4.3	4.0
Capital Expenditures	3.0	4.1	5.0	5.6	6.0	6.2	6.2	6.3
Consolidated Public Sector Deficit	-3.0	-5.1	-5.8	-5.7	-4.8	-4.7	-4.6	-4.3
Primary Balance	4.9	3.0	2.8	3.4	3.8	3.6	3.6	3.7
Net Interest Bills	-7.9	-8.1	-8.6	-9.1	-8.6	-8.3	-8.2	-8.0
Domestic Debt	-3.8	-4.1	-4.2	-4.2	-3.9	-3.9	-4.1	-4.1
Foreign Debt	-4.0	-4.0	-4.4	-4.9	-4.7	-4.4	-4.1	-3.8
FINANCING REQUIREMENTS _6/	3.3	5.8	6.9	7.4	6.1	6.0	5.7	5.4
Consolidated Public Sector Deficit	-3.0	-5.1	-5.8	-5.7	-4.8	-4.7	-4.6	-4.3
Official Reserve Accumulation	0.3	0.6	0.9	1.6	1.2	1.2	1.0	0.9
CB Credit to Private Sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other Requirements _8/	-0.2	-1.1	-2.1	-0.6	-0.5	-0.4	0.0	0.0
SOURCES OF FINANCING _6/	3.3	5.8	6.9	7.4	6.1	6.0	5.7	5.4
Monetary Base Creation	1.2	2.5	1.4	1.4	1.3	1.3	1.3	1.3
Domestic Borrowing	2.2	3.1	4.3	3.4	3.2	3.9	3.5	3.1
Foreign Borrowing (net)	0.1	1.3	3.2	3.2	2.2	1.3	0.9	1.0
DEBT STOCKS _6/								
Domestic Public Debt	22.8	22.6	23.7	23.6	23.7	24.4	24.6	24.3
Foreign Public Debt	63.3	59.1	60.5	62.6	62.3	58.9	55.6	51.9

_1/ Annual percentage change.
_2/ Philippines manufacture imports weights.
_3/ Six-month US$ rate.
_4/ OECD manufacture imports.
_5/ US$ per barrel.
_6/ Share of GDP, percent.
_7/ Including National Government, Local Government Units, Central Bank, and Non-Financial Public Corporations.
_8/ Including statistical discrepancy, in history, and requirements for debt restructuring operations.

more aggressive exchange rate policy leads to an improvement in competitiveness, gradually obtaining a cumulative real devaluation of 10% in 1990-91. The exchange rate is subsequently managed so as to maintain competitiveness constant, given the assumed international and domestic inflation rates. The improvement in international competitiveness results in a moderate inflow of foreign investment; these stimulate investment and production in the tradeables sector, which continue to sustain economic growth, though at more moderate rates than in 1988-89. As a result, after 1992 real GDP growth averages more than 5% and real per capita consumption 2%. Table 4.2 summarizes the main economic indicators in the scenario.

Table 4.2: Case I: Selected Economic Indicators
(percent; annual averages)

Key Indicators	1989	1990	1991-2	1993-5	1996-8
Growth Rates					
GDP Growth Rate	6.1	3.5	4.6	5.2	5.4
Consumption/Capita Growth Rate	4.5	0.7	1.0	1.8	2.6
Domestic Inflation Rate	10.1	13.0	11.0	10.0	10.0
Real Exchange Rate Depreciation	-5.9	4.0	2.6	0.0	0.0
Ratios to GDP					
Gross Investment	18.8	19.3	20.2	22.7	23.7
National Savings	15.4	14.7	15.8	19.6	21.4
Current Account	-3.3	-5.0	-4.8	-3.4	-2.4
Exports of GNFS	24.4	25.6	27.2	28.4	29.7
Imports of GNFS	27.0	28.3	29.2	30.7	31.5
Non-interest Current Account	2.2	0.3	0.9	1.6	1.9
Interest Payments	5.5	5.3	5.7	5.0	4.3
Debt Service	8.4	8.8	9.2	9.7	8.4
DOD	68.5	70.0	70.5	63.8	53.1
Foreign Official Reserves	5.2	5.9	7.1	7.9	8.2

4.26 Trade and Payments. The oil price increase and the consequent deterioration in the terms of trade are the most dramatic events affecting international trade in 1990-92. Imports of crude oil and other fuels are projected to increase from US$1.4 billion in 1989 to US$2.2 billion in 1990 and US$2.6 billion in 1991. Volume growth underlying these projections is approximately 3% per year in 1990-91, down from an average 20% in 1988-89. The sharp decline in volume growth is expected to result from the slowdown in economic activity and the increase in prices. Concerning other imports, reconstruction needs following the July earthquake lead to larger imports of intermediate inputs in the period 1990-92, while the deceleration of growth moderates the aggregate impact on imports. In the remainder of the period, import growth continues to be dominated by capital goods, intermediate inputs for manufactured exports, and oil; food and other consumer goods account for 10 to 15% of merchandise imports. Export growth is led by the manufacturing

and other non-traditional goods (mostly agro-processing), while exports of traditional commodities (coconut oil, sugar, copper) are affected by the depressed world demand for these products. In real terms, the growth rate of exports of goods and non-factor services averages 9% per year in 1990-91 (down from almost 14% in 1988-89) and later stabilizes at about 7%.

Table 4.8: Case I: Financing Requirements
(US$ Million; Annual Average)

	1989	1990	1991-2	1993-5	1996-8
Exports of Goods & NFS	10829	12368	15771	21145	29129
Imports of Goods & NFS	11983	14318	17462	22365	29984
Net Factor Income _1/	-1141	-1265	-1822	-2110	-2440
(interest payments) _1/	2420	2498	3019	3347	3767
Net Current Transfers	830	878	967	1094	1250
Current Account Balance _1/	-1465	-2337	-2546	-2237	-2044
Direct Foreign Investment	854	762	828	880	956
Disbursements of MLT Loans	1837	3372	2535	2844	3117
Multilateral	749	1237	1056	1184	1276
Bilateral	884	1199	1293	1500	1689
Private	205	936	186	159	152
Repayments of MLT Loans	1118	1281	1625	3100	2916
Multilateral	346	378	398	495	654
Bilateral	37	54	400	959	1047
Private	617	728	705	1531	1159
Short-term and other flows	30	-535	240	662	948
Changes in Net Reserves	-139	-556	-626	-731	-834
IMF, net credit	126	-137	49	-92	-149
Official Reserves	-265	-419	-674	-639	-686
Gap, net	0	575	1194	1682	773
Amortization, gap	0	0	0	38	635
Gap, gross	0	575	1194	1720	1408

_1/ Including interest payments on gap.

4.27 Net factor incomes continue to be negative throughout the projections period, as a result of the continuing burden of interest payments on foreign debt. This increases in 1991-92, both because of the increase in LIBOR and the increase in external debt--following a sharp rise in external financing needs due to the earthquake and the oil shock--and later declines. The decrease of the interest burden is even more apparent as a share of total exports, as it declines by 8 percentage points--from 19 to 11--between 1989 and 1998. Profit remittances rise during the projection period as a consequence of foreign direct investment inflows, increasing at an average 2% per year. Factor receipts are expected to be negatively affected by the Middle East crisis in 1990-92; personal income receipts are projected to be US$50-75 than originally expected in that period, due to the loss of

remittances from approximately 28,000 Filipino contract workers that were located in Iraq and Kuwait at the outbreak of the crisis. Current transfers are projected constant in real terms, to reflect fluctuations in worker remittances in recent years. As a result of these developments, the current account deficit rises from 3.3% of GDP in 1989 to about 5% in 1990-2, and then declines slowly to about 2% at the end of the period.

4.28 External Financing. Unlike forecasts prior to the outbreak of the Middle East crisis, which predicted no financing gap in 1990 and 1991, a large financing gap arises starting in 1990. In the period 1990-92 the major determinant of the gap is the increased oil bill; in 1993-95, the major determinant is the "bunching" of maturities of previously rescheduled debt, as repayments of medium and long-term loans average US$3.1 billion per year in 1993-5--twice the average for 1990-92--and net transfers on medium and long-term loans are negative. These developments clearly indicate, on the one hand, the need for exceptional additional financing in the short term to cope with the oil shock, and, on the other, the continuing need to pursue a cooperative and innovative approach to reducing the debt burden.[3]

Implications

4.29 In this scenario, the drag imposed on the economy by the growing domestic debt is contained. The projections show the size of the fiscal adjustment that is required to stabilize the ratio of domestic public debt to GDP at approximately 24.5%. This outcome depends crucially on the ability of policy makers to effect swiftly the required fiscal adjustment--both generating additional revenues and keeping current expenditures under control--and to contain inflation at the same time as a severe external shock is changing substantially the international economic outlook. The severe strain placed on the economy by high domestic interest rates and the oil shock needs to be offset by stimulating domestic and foreign investment, restoring international competitiveness, improving the regulatory framework and increasing public investment in crucial infrastructure.

4.30 In order to support moderate growth, this strategy will require a higher level of external support than originally envisaged. Donors will inevitably be asked to act on an emergency basis to help smooth out the adjustment necessitated by precipitous world events. The problem of the debt overhang and the financing requirements associated with debt service will need to be addressed jointly and comprehensively. The magnitude of the unidentified financing needs in the immediate future require concerted and decisive action by the international community.

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[3]The projections do not incorporate a "second stage" DDSR operation. While such operation is allowed for by the agreement of October 1989 with the commercial banks, its timing, size and terms are still uncertain.

D. Case II: Furthering Structural Reform

Policy Assumptions

4.31 In this scenario, a more ambitious macroeconomic policy than in Case I is implemented, and is complemented by a structural reform package aimed at lowering the costs of adjustment. These structural reforms include the measures discussed in Chapter 3 to enhance competition and efficiency in the financial sector; to further reduce trade restrictions and broaden the revenue base for tariffs and VAT on imports; to improve the environment for domestic and foreign investment by improving the regulatory framework and to improve the quantity and quality of infrastructure, especially through deregulation of transportation. The macroeconomic measures include accommodating monetary policy as in Case I, a more aggressive exchange rate management, and fiscal measures yielding a larger revenue effort as in the previous scenario. Exchange rate policy leads to a cumulative real depreciation of about 20% between 1989 and 1998.

4.32 The fiscal package implemented in this scenario results in an increase in revenues of about 2% of GDP in 1991--i.e., as much as obtained over two years in Case I. Bringing about a revenue increase of this magnitude and at the same time increasing the efficiency and equity of the taxation system will require considerable resolve from policy makers. Measures aimed at increasing the overall efficiency and equity of the taxation system--such as the rationalization of income taxes, international trade tariffs, and taxes bearing on financial intermediation costs--will lead to some revenue loss and will thus need to be accompanied by additional revenue increasing measures.

4.33 The structural reform package is expected increase the level and efficiency of private investment and to attract larger foreign investment flows than in Case I. While a decrease in real interest rates is not built into the scenario--the effect on interest rates of structural changes cannot be estimated and the adjustment experience of other highly indebted countries shows consistently high interest rates--the magnitude of the fiscal adjustment is likely to lead to a decline in real interest rates. In addition to the improvement in the primary surplus of the consolidated public sector, other factors would contribute to this outcome in this scenario: lower intermediation costs as well as reduced rents in the banking sector; larger real exchange rate depreciation; and increased availability of funds, as foreign investors respond to improved investment and ownership regulations.

External Financing Assumptions

4.34 As argued above, it is not certain whether the more decisive policy effort of the Philippines would lead to higher official financing. Consequently, it is assumed here that official and private lending and DDSR operations are as in Case I. Direct foreign investment is however projected to be larger, growing about 5.5% per year, as a result of the improved competitiveness and regulatory framework.

Outcomes

4.35 Fiscal Adjustment. Table 4.4 reports the evolution of the consolidated public sector deficit, its financing, and the resulting accumulation of domestic and foreign debt. In this scenario, the stronger fiscal effort leads to a decline in domestic debt-to-GDP starting in 1991. First, the primary surplus of the consolidated public sector increases by one percentage point of GDP between 1990 and 1991. Second, the investment and export-led increase in real GDP growth affect beneficially the process of domestic debt accumulation. The interest bill on domestic debt, as a ratio to GDP, declines faster than in Case I, and by 1995 it is .5% smaller than in Case I. Third, the effect of the larger devaluation on the consolidated public sector financing requirements is small: the interest bill on foreign debt and the foreign currency component of public investment, denominated in local currency, are approximately .2% of GDP higher in Case II than in Case I. The higher exchange rate also affects the revenues from indirect taxes on international trade, interest receipts on the Central Bank's foreign exchange reserves and the cost of foreign reserve accumulation. As a result of these developments, by 1995 the consolidated public sector deficit is 1.2 percentage point of GDP smaller in this scenario than in Case I, or 2.7 percentage points of GDP smaller than in 1990.

4.36 GDP Growth. As in the previous scenario, growth decelerates to 3.5 and 4.5% in 1990 and 1991, as a consequence of the weakening of the economy in the first semester of 1990, the recent earthquake and the oil shock. In the later years, increased level and efficiency of investment and higher international competitiveness--leading to an increase in manufacturing and other non-traditional exports--result, in comparison with the previous scenario, in higher real growth and higher per capita consumption growth. Table 4.5 summarizes the main economic indicators in the scenario.

Table 4.4: Case II: Consolidated Public Sector

CASE II	1988	1989	1990	1991	1992	1993	1994	1995
ASSUMPTIONS _1/								
MUV Index _2/	7.5	0.9	6.2	9.5	5.0	5.0	5.0	5.0
LIBOR _3/	8.1	9.4	9.1	10.6	9.5	8.4	8.2	8.0
World Trade _4/	5.6	7.4	5.1	5.7	6.4	6.4	6.4	6.4
Oil Price _5/	13.3	16.4	24.8	29.0	25.4	22.0	20.0	20.0
Real Exchange Rate Depreciation	-0.5	-5.9	4.0	5.2	2.0	1.5	1.5	1.5
Domestic Interest Rate	14.7	17.5	24.3	23.2	21.0	21.0	21.0	21.0
GDP Deflator Growth Rate	9.8	10.1	13.0	12.0	10.0	10.0	10.0	10.0
GDP Growth in constant terms	6.3	6.1	3.5	4.5	5.0	6.0	6.5	6.5
CONSOLIDATED PUBLIC SECTOR _6/ _7/								
Total Revenues	19.6	20.8	22.0	23.9	24.1	24.3	24.4	24.6
Revenues excld. Interest	19.1	20.2	21.3	23.2	23.6	23.8	23.9	24.1
Interest Revenues	0.5	0.5	0.7	0.6	0.6	0.5	0.5	0.5
Total Current Expenditures	19.5	21.7	22.8	23.5	22.5	22.1	21.8	21.4
Expenditures excld. Interest	11.2	13.1	13.5	13.8	13.4	13.4	13.4	13.4
Interest Payments	8.4	8.6	9.2	9.7	9.2	8.7	8.4	8.0
Domestic Debt	4.2	4.5	4.7	4.7	4.2	4.1	4.1	3.9
Foreign Debt	4.1	4.1	4.5	5.0	5.0	4.6	4.4	4.1
Capital Expenditures	3.0	4.1	5.0	5.6	6.0	6.3	6.3	6.3
Consolidated Public Sector Deficit	-3.0	-5.1	-5.8	-5.2	-4.4	-4.0	-3.7	-3.1
Primary Balance	4.9	3.0	2.8	3.9	4.2	4.2	4.3	4.4
Net Interest Bills	-7.9	-8.1	-8.6	-9.1	-8.6	-8.2	-7.9	-7.6
Domestic Debt	-3.8	-4.1	-4.2	-4.2	-3.8	-3.7	-3.7	-3.6
Foreign Debt	-4.0	-4.0	-4.4	-4.9	-4.8	-4.4	-4.2	-4.0
FINANCING REQUIREMENTS _6/	3.3	5.8	6.9	6.9	5.8	5.5	5.1	4.4
Consolidated Public Sector Deficit	-3.0	-5.1	-5.8	-5.2	-4.4	-4.0	-3.7	-3.1
Official Reserve Accumulation	0.3	0.6	0.9	1.6	1.3	1.4	1.2	1.1
CB Credit to Private Sector	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other Requirements _8/	-0.2	-1.1	-2.1	-0.6	-0.5	-0.4	0.0	0.0
SOURCES OF FINANCING _6/	3.3	5.8	6.9	6.9	5.8	5.5	5.1	4.4
Monetary Base Creation	1.2	2.5	1.4	1.4	1.3	1.4	1.4	1.4
Domestic Borrowing	2.2	3.1	4.3	2.9	2.8	3.2	2.3	1.8
Foreign Borrowing (net)	0.1	1.3	3.2	3.2	2.3	1.4	1.3	1.1
DEBT STOCKS _6/								
Domestic Public Debt	22.8	22.6	23.7	23.1	22.8	22.8	21.7	20.4
Foreign Public Debt	63.3	59.1	60.5	62.6	63.3	60.2	57.4	53.8

_1/ Annual percentage change.
_2/ Philippines manufacture imports weights.
_3/ Six-month US$ rate.
_4/ OECD manufacture imports.
_5/ US$ per barrel.
_6/ Share of GDP, percent.
_7/ Including National Government, Local Government Units, Central Bank, and Non-Financial Public Corporations.
_8/ Including statistical discrepancy, in history, and requirements for debt restructuring operations.

Table 4.5: Case II: Selected Economic Indicators
(percent; annual averages)

Key Indicators	1989	1990	1991-2	1993-5	1996-8
Growth Rates					
GDP Growth Rate	6.1	3.5	4.8	6.3	6.6
Consumption/Capita Growth Rate	4.5	0.7	0.7	2.3	3.6
Domestic Inflation Rate	10.1	13.0	11.0	10.0	10.0
Real Exchange Rate Depreciation	-5.9	4.0	3.6	1.5	1.5
Ratios to GDP					
Gross Investment	18.8	19.3	20.4	24.4	25.8
National Savings	15.4	14.7	16.2	21.3	23.7
Current Account	-3.3	-5.0	-4.8	-3.5	-2.5
Exports of GNFS	24.4	25.6	27.4	29.1	30.8
Imports of GNFS	27.0	28.3	29.3	31.4	32.6
Non-Interest Current Account	2.2	0.3	1.0	1.6	1.9
Interest Payments	5.5	5.3	5.8	5.1	4.5
Debt Service	8.4	8.8	9.2	10.0	8.8
DOD	68.5	70.0	71.0	65.6	55.3
Foreign Official Reserves	5.2	5.9	7.2	8.5	9.3

4.37 Trade and Payments. Export and import growth rates are higher in this scenario: exports are affected by real exchange depreciation; imports, by real GDP growth and in particular investment and manufacturing exports, which are the most import-intensive demand components and are also the most dynamic in this scenario. As a result, until 1996 the current account deficit is larger in this scenario than in Case I; the increase in investment leads to an increase in imports that more than compensates for the increase in exports; higher factor income payments result from larger foreign borrowing requirements and direct foreign investment--and thus higher interest payments and profit remittances. The current account deficit, however, steadily improves, after peaking at 5.3% of GDP in 1991.

4.38 External Financing. Table 4.6 reports external financing and financing requirements in Case II. As discussed above, official and private lending and DDSR operations are assumed to be as in Case I, while direct foreign investment is larger. The larger inflow of foreign investment does not completely offset the larger financing requirements and, as a result, until 1996 larger unidentified financing requirements emerge in Case II.

Table 4.6: Case II: Financing Requirements
(US$ Million; Annual Average)

	1989	1990	1991-2	1993-5	1996-8
Exports of Goods & NFS	10829	12368	15890	22110	32229
Imports of Goods & NFS	11988	14318	17556	23477	32947
Net Factor Income _1/	-1141	-1265	-1822	-2128	-2502
(interest payments) _1/	2420	2498	3018	3355	3805
Net Current Transfers	830	878	967	1094	1250
Current Account Balance _1/	-1465	-2337	-2520	-2395	-1970
Direct Foreign Investment	854	762	856	978	1242
Disbursements of MLT Loans	1837	3372	2535	2844	3117
Multilateral	749	1237	1056	1184	1276
Bilateral	884	1199	1293	1500	1689
Private	205	936	186	159	152
Repayments of MLT Loans	1118	1281	1625	3100	2916
Multilateral	346	378	398	495	654
Bilateral	37	54	400	959	1047
Private	617	728	705	1531	1159
Short-term and other flows	30	-535	240	662	948
Changes in Net Reserves	-139	-556	-647	-843	-1013
IMF, net credit	126	-137	49	-92	-149
Official Reserves	-265	-419	-695	-751	-865
Gap, net	0	575	1161	1854	592
Amortization, gap	0	0	0	38	632
Gap, gross	0	575	1161	1893	1224

_1/ Including interest payments on gap.

Implications

4.39 In this scenario, the stock of domestic public debt decreases, as fraction of GDP, below its current level, and at the same time the economy is placed on a higher growth trajectory as overall economic efficiency is improved. In addition to sound macroeconomic management, this outcome will require a major push towards structural reforms that will increase efficiency and competition in the financial sector, improve the effectiveness of investment incentives, and stimulate the transfer of resources to the tradeables sector. While major steps in these areas have been taken since the mid-1980s--with positive results in terms of growth--more needs to be done for the country to fully realize its potential, as extensively discussed in Chapter 3.

4.40 As in Case I, implementing this strategy will require a higher level of external support than envisaged prior to the outbreak of the Middle East crisis; this, in turn, will require concerted and decisive action by the international community to address the problem of financing requirements and debt overhang in a comprehensive fashion. In addition, the strategy outlined in this scenario needs a stronger determination to free the Philippines from

its remaining structural constraints to develop a more open, market-based economy. The most recent developments indicate clearly that the progress achieved by the Philippines in this direction, while impressive, can too easily be threatened by exogenous shocks. The solution to reduce the vulnerability of the economy to adverse external developments is to be found in the comprehensive and bold economic strategy that has been outlined. Considerable political will is necessary to reverse the trends that have emerged in the economy during the past eighteen months, in order to position it to withstand future shocks and achieve meaningful progress in reducing the drag of domestic debt on the country's growth potential.

STATISTICAL APPENDIX
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PHILIPPINES
TABLE 1:
National Accounts Summary at Current Prices
(In billions of national currency units)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
ORIGIN AND USE OF RESOURCES:											
A.1. GDP at market prices	217.5	264.7	305.3	340.6	384.1	540.5	612.684	627.129	708.368	825.707	963.171
2. Net indirect taxes	22.379	25.759	25.928	28.665	34.722	43.92	49.346	52.309	70.231	64.16	80.278
3. GDP at factor cost	195.121	238.941	279.372	311.935	349.378	496.58	563.338	574.82	638.137	761.547	882.893
4. Agriculture	55.5	61.8	69.4	76.7	84.6	139.5	162.519	155.989	170.77	189.988	225.872
5. Industry	76.9	96.8	111.6	122.5	138.2	186.2	200.554	204.98	232.585	277.175	320.436
a. Manufacturing	52.1	64.6	75.2	83.1	95.2	137.3	150.533	155.172	173.539	207.447	240.377
b. Mining and quarrying	5.8	8.1	6.8	6.1	7	9.7	11.529	12.445	13.6	15.996	16.462
c. Other	19	24.1	29.6	33.3	36	39.2	38.492	37.363	45.446	53.732	63.597
6. Services	85.1	106.1	124.3	141.4	161.3	214.8	249.611	266.16	305.013	358.544	416.863
B.1. Resource balance	-12.1	-15.1	-16.6	-23.1	-26.2	-0.7	18.065	38.916	6.075	4.799	-12.917
2. Exports of GNFS	41.5	53.6	57.8	56.2	75.3	117.7	126.571	155.104	163.472	202.936	239.337
3. Imports of GNFS	53.6	68.7	74.4	79.3	101.5	118.4	108.506	116.188	157.397	198.137	252.254
C.1. Domestic absorption	229.6	279.8	321.9	363.7	410.3	541.2	594.619	588.213	702.293	820.908	976.088
D.1. Total consumption	161.9	198.6	228.6	267.2	307.7	449.2	509.217	507.107	591.899	677.652	795.489
2. Private	143.6	177.4	203.8	238	278.2	413.6	465.173	458.666	533.427	604.581	706.625
a. Statistical discrepancy	-2.9	-0.7	-3.1	3.5	10	10.2	-3.96	-16.325	7.346	1.3	-0.267
3. General government	18.3	21.2	24.8	29.2	29.5	35.6	44.044	48.441	58.472	73.071	88.864
E.1. Gross domestic investment	67.7	81.2	93.3	96.5	102.6	92	85.402	81.106	110.394	143.256	180.599
2. Fixed investment	56.3	68	79.3	86	95.3	100.1	89.974	80.817	99.588	126.413	164.609
3. Increase in stocks	11.4	13.2	14	10.5	7.3	-8.1	-4.572	0.289	11.806	16.843	15.99
MEMORANDUM ITEMS:											
G.1. Net factor income	0.5	-0.2	-1.7	-5.2	-5.3	-13.1	-14.941	-12.426	-5.007	-2.982	-7.598
2. Net current transfers	1.689	2.246	2.567	2.75	2.634	1.97	3.2	4.791	7.734	10.548	10.282
3. Gross national product	218	264.5	303.6	335.4	378.8	527.4	597.743	614.703	703.361	822.725	955.573
H.1. Gross domestic saving	55.6	66.1	76.7	73.4	76.4	91.3	103.467	120.022	116.469	148.055	167.682
2. Gross national saving	57.789	68.146	77.567	70.95	73.734	80.17	91.726	112.387	119.196	155.621	170.366
I.1. GDP at mp (curr. mill. US)	29481.1	35239.8	38647	39882.9	34563.1	32367.2	32940	30741.6	34440.0	39142.0	44310.0

Source: Philippines Standard Tables, IEC, World Bank

TABLE 2:
National Accounts Summary at Constant 1972 Prices
(In billions of national currency units)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
ORIGIN AND USE OF RESOURCES:											
A.1. GDP at market prices	88	92.637	96.2	99	100	93.9	89.904	91.18	95.481	101.398	107.466
2. Net indirect taxes	9.053	9.016	8.169	8.333	9.13	7.354	7.241	7.569	9.466	7.879	8.957
3. GDP at factor cost	78.947	83.621	88.031	90.667	90.87	86.546	82.663	83.611	86.015	93.519	98.509
4. Agriculture	22.6	23.7	24.6	25.4	24.9	25.4	26.252	27.11	26.834	27.771	28.887
5. Industry	31.9	33.4	35	35.7	36	32.3	29	28.396	30.608	33.205	35.562
a. Manufacturing	22.2	23.2	24	24.5	25.1	23.3	21.541	21.717	23.186	25.251	26.99
b. Mining and quarrying	2.1	2.2	2.2	2	2	1.8	1.768	1.574	1.547	1.615	1.571
c. Other	7.6	8	8.8	9.2	8.9	7.2	5.691	5.105	5.875	6.339	7.001
6. Services	33.5	35.537	36.6	37.9	39.1	36.2	34.652	35.674	38.039	40.422	43.017
B.1. Resource balance	-3.1	-1.7	-1	-1.8	-2.5	2.7	5.356	7.758	3.258	0.251	-2.576
2. Exports of GNFS	15.7	17.7	17.9	17.7	19.3	20.9	19.351	23.56	23.245	26.931	30.091
3. Imports of GNFS	18.8	19.4	18.9	19.5	21.8	18.2	13.995	15.802	19.987	26.68	32.667
C.1. Domestic absorption	91.1	94.337	97.2	100.8	102.5	91.2	84.548	83.422	92.74	99.981	107.329
D.1. Total consumption	65.6	67.737	70	74.5	77.5	77	73.424	73.311	79.183	84.055	88.925
2. Private	57.6	59.437	61.4	65.4	68.8	68.7	65.203	65.124	70.409	74.646	78.791
a. Statistical discrepancy	0.9	0.137	-0.2	1.9	3.4	2.7	-0.774	-1.473	-0.517	1.156	1.156
3. General government	8	8.3	8.6	9.1	8.7	8.3	8.221	8.187	8.774	9.409	10.134
E.1. Gross domestic investment	25.5	26.6	27.2	26.3	25	14.2	11.124	10.111	13.557	15.926	18.404
2. Fixed investment	21.3	22.7	23.5	23.7	23	15.6	11.826	10.057	12.017	13.874	16.616
3. Increase in stocks	4.2	3.9	3.7	2.6	2	-1.4	-0.702	0.054	1.54	2.052	1.788
MEMORANDUM ITEMS:											
G.1. Net factor income	0.2	-0.036	-0.5	-1.5	-1.3	-2.3	-2.037	-1.676	-0.666	-0.348	-0.807
2. Net current transfers	0.67	0.757	0.775	0.762	0.658	0.332	0.455	0.679	0.862	1.268	
3. Gross national product	88.2	92.601	95.7	97.5	98.7	91.6	87.867	89.504	94.815	101.05	106.659
H.1. Gross domestic saving	21.256	22.336	22.983	20.62	19.373	14.092	13.454	15.404	16.298	17.343	18.541
2. Gross national saving	22.126	23.057	23.258	19.882	18.731	12.124	11.872	14.407	16.494	18.263	17.734
I.1. Capacity to import	14.556	15.136	14.683	13.82	16.173	18.092	16.325	21.095	20.758	26.256	29.961
2. Terms of trade adjustment	-1.144	-2.564	-3.217	-3.88	-3.127	-2.808	-3.026	-2.465	-2.487	-0.644	NA
3. Gross domestic income	86.856	90.073	92.983	95.12	96.873	91.092	86.878	88.715	92.976	100.956	108.025
4. Gross national income	87.056	90.037	92.483	93.62	95.573	88.792	84.841	87.039	92.31	100.556	105.146
J.1. GDP at current mp	217.5	264.7	305.3	340.6	384.1	540.5	612.684	627.129	708.368	825.707	963.171

Source: Philippines Standard Tables, IEC, World Bank

TABLE 8:
Balance of Payments Summary at Current Prices
(In millions of US dollars)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
A.1. Exports of GNFS	5678	7236	7513	6825	6813	7033	6864	7702	8065	9479	10829
2. Merchandise (FOB)	4601	5788	5722	5021	5005	5391	4629	4842	5720	7074	7821
a. of which: Manufacture	1622.9	2141.2	2560.4	2491.9	2533.6	2978.7	2643.9	2808	3486.1	4338	5192
3. Non-factor services	1077	1448	1791	1804	1808	1642	2235	2860	2345	2405	3008
B.1. Imports of GNFS	7305	9147	9554	9467	9174	7212	5944	5868	7861	9467	11983
2. Merchandise (FOB)	6142	7727	7946	7667	7487	6070	5111	5044	6737	8159	10419
a. of which: Manufacture	4239	4862.8	4896.6	4903.1	4771	3956.9	3144.6	3608.9	4866.3	4020	4910
3. Non-factor services	1163	1420	1608	1800	1687	1142	833	824	1124	1308	1564
C.1. Resource balance	-1627	-1911	-2041	-2642	-2361	-179	920	1834	204	12	-1154
D.1. Net factor income	-223	-439	-527	-1044	-859	-1475	-1317	-1321	-1221	-1210	-1141
2. Factor receipts	578	762	1070	1179	1319	984	1053	931	1109	1187	1578
a. of which labor income	365	421	546	810	944	659	694	696	809	874	1002
3. Factor payments	801	1201	1597	2223	2178	2459	2370	2252	2330	2397	2719
a. of wh. LT interest (DRS)	490.4	573.9	820.5	920.5	940.6	923.7	937	1138.1	1434.2	1638.1	1910.2
E.1. Net current transfers (prv)	229	299	325	322	237	118	172	235	376	500	473
2. Transfer receipts	234	305	328	324	242	119	181	239	378	503	475
a. of wh. workers remit.	191	205	254	239	180	59	111	163	211	388	360
3. Transfer payments	5	6	3	2	5	1	9	4	2	3	2
F.1 Curr A/C bal before Off Trans	-1621	-2051	-2243	-3364	-2983	-1536	-225	748	-641	-698	-1822
2. Net official transfers	128	148	182	164	235	268	207	206	197	275	357
3 Curr A/C bal after Off Trans	-1495	-1903	-2061	-3200	-2748	-1268	-18	954	-444	-423	-1465
G.1. Long-term capital inflow	1106	877	1503	1566	1464	308	3094	1249	457	-59	998
2. Net direct investment	7	-108	172	16	105	9	12	127	307	986	854
3. Net LT Loans (DRS)	1130.5	1317.7	1494.2	1512.5	1751.7	994	1013.8	401.7	-88	71	720
a. disbursements	2087.3	1852.9	2212.4	2479.8	2574.7	1512.4	1639.4	1511.3	1356.1	1372	1837
b. repayments	956.8	535.2	718.2	967.3	823	518.4	625.6	1109.6	1424.1	1301	1118
4. Other LT Inflows (net)	-31.5	-334.7	-163.1	37.5	-392.8	-695.2	2068.3	720.3	217.9	-1116	-576
H.1. Other items (Net)	765.9	1981.6	226.1	916.2	-761.8	1143.6	-3224.1	-1072	-281.3	654	606
2. Net short-term capital	513.9	1857.4	712.7	1280.1	-402.7	1104.8	-3866.6	-1103.7	-139.2	-303	-91
3. Capital flows n.e.i.	0	0	0	0	0	0	0	0	0	478	312
4. Errors and omissions	251.9	124.1	-486.6	-363.9	-359.1	38.9	642.6	31.7	-142.1	479	385
I.1. Changes in net reserves	-376.9	-955.6	331.9	717.8	2045.8	-183.6	148.1	-1131	268.3	-172	-139
2. Use of IMF credit	92.7	185.3	105	-124.8	108.3	-185	279	137.2	21.2	-72	126
3. Other reserve changes	-469.6	-1140.9	226.8	842.6	1937.5	1.3	-131	-1268.2	247.1	-100	-265

Source: Philippines Standard Tables, IEC, World Bank

TABLE 4.1:
External Debt: Disbursements and Repayments
(US$ millions at Current Prices)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
DISBURSEMENTS											
A. Public & Publicly Guar. LT	1619.8	1381	1604.9	1915.9	2305.7	1442.4	1354.4	1411.3	1276.1	1371.8	1837
1. Official Creditors	583.3	459.7	906.2	664.1	1179.1	979.4	687.9	733.5	1151.1	1229.1	1631
a. Multilateral	302.3	320.8	573.9	389.2	795.2	495.5	391.1	340.8	404.6	430.8	747
aa of which IBRD	210.3	228.7	441.2	250.9	600.3	290.8	262.7	188.9	262.5	258.5	463.4
ab of which IDA	2.5	1.7	7.1	7.7	12.7	10.2	13.3	8.1	7.6	3.1	1.4
b. Bilateral	281	138.9	332.3	274.9	383.9	483.9	296.8	392.7	746.5	798.3	884
2. Private Creditors	1036.5	921.3	698.7	1251.8	1126.6	463	666.5	677.8	125	142.7	206
a. Suppliers	136.5	56.4	77	87.8	112.5	124.3	170.1	122.2	92.7	124.4	98
b. Commercial Banks	830.4	662.8	552	1062.5	762.6	206.5	405	528.5	7.7	8	93
c. Other Private	69.6	202.1	69.7	101.5	251.5	132.2	91.4	27.1	24.6	10.3	15
B. Private Non-Guaranteed LT	467.5	471.9	607.5	563.9	269	70	285	100	80	0	0
C. Total LT Disbursements	2087.3	1852.9	2212.4	2479.8	2574.7	1512.4	1639.4	1511.3	1356.1	1371.8	1837
D. IMF Purchases	235.8	446.4	236.5	0	308.5	87.1	322.9	268.8	161.1	94.1	302.4
E. Net Short-Term Capital	0	0	0	0	0	0	0	267	414	114	22
F. Total Disbursements	2323.1	2299.3	2448.9	2479.8	2883.2	1599.5	1962.3	2047.1	1931.2	1579.9	2161.4
REPAYMENTS											
A. Public & Publicly Guar. LT	469.9	215.2	330.9	489.7	535	344.4	474.8	924.6	1315.7	1219.9	1000.2
1. Official Creditors	155.3	93.3	128.6	186.8	174.6	224.1	333.8	529.7	404.6	389.1	383.2
a. Multilateral	36.6	45.2	53	86.6	95.1	120.8	142.2	208.7	269.2	349.9	346.2
aa of which IBRD	25	33.3	38.1	61.3	72.2	92.2	109.8	169.3	219.3	282.9	268.1
ab of which IDA	0	0	0	0	0.2	0.3	0.3	0.3	0.3	0.5	0.8
b. Bilateral	118.7	48.1	75.6	100.2	79.5	103.3	191.6	321	135.4	39.2	37
2. Private Creditors	314.6	121.9	202.3	302.9	360.4	120.3	141	394.9	911.1	830.8	617
a. Suppliers	95.8	42.9	58.7	60.4	49.6	36.1	4.8	116.7	105.5	21.8	18
b. Commercial Banks	201.6	43.5	107.9	181.7	236.3	17.6	11.1	189.3	629.5	621.2	473
c. Other Private	17.2	35.5	35.7	60.8	74.5	66.6	125.1	88.9	176.1	187.8	126
B. Private Non-Guranteed LT	486.9	320	387.3	477.6	288	174	150.8	185	108.4	100	118
C. Total LT Repayments	956.8	535.2	718.2	967.3	823	518.4	625.6	1109.6	1424.1	1319.9	1118.2
D. IMF Repurchases	92	145.3	54	74.7	159.2	242	190.4	302.5	353.7	195.8	196.4
E. Total LT Repay + IMF Repur.	1048.8	680.5	772.2	1042	982.2	760.4	816	1412.1	1777.8	1515.7	1314.6

Source: Philippines Standard Tables, IEC, World Bank

TABLE 4.2:
External Debt: Interest and Debt Outstanding
(US$ millions at Current Prices)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
INTEREST											
A. Public & Publicly Guar. LT	304.4	369.9	522	536.5	656.6	791.7	798.2	1008.1	1302.2	1515.1	1827.2
1. Official Creditors	146.9	138.7	165	210.3	243.3	322.9	320	457.2	505.7	507.7	623
a. Multilateral	82.6	99.5	119.4	152.3	177.1	229.1	249	320.4	375.9	387.3	444
aa of which IBRD	61.1	72.6	88.2	112.8	132.8	169.6	175.5	236.9	274.5	289	267.7
ab of which IDA	0.2	0.2	0.3	0.3	0.4	0.5	0.6	0.7	0.7	0.8	0.8
b. Bilateral	64.3	39.2	45.6	58	66.2	93.8	71	136.8	129.8	120.4	179
2. Private Creditors	157.5	231.2	357	326.2	413.3	468.8	478.2	550.9	796.5	1007.4	1204.2
a. Suppliers	26.3	20.3	19.3	17.5	21.4	14.1	9.1	30.5	23	24.3	20.2
b. Commercial Banks	79.4	167.7	260.2	227.8	298.6	363.3	379.5	413.1	668.4	859.2	1080
c. Other Private	51.8	43.2	77.5	80.9	93.3	91.4	89.6	107.3	105.1	123.9	104
B. Private Non-Guaranteed LT	186	204	298.5	384	284	132	138.8	130	132	123	83
C. Total LT Interest	490.4	573.9	820.5	920.5	940.6	923.7	937	1138.1	1434.2	1638.1	1910.2
D. IMF Service Charges	35.1	41.6	58	83.4	80.8	76.9	68	78.2	83	74.1	115
E. Interest Paid on ST Debt	0	875.3	1307.2	1452.2	1015.7	925.9	750	400	365	341	395
F. Total Interest Paid	525.5	1490.8	2185.7	2456.1	2037.1	1926.5	1755	1616.3	1882.2	2053.2	2420.2
DEBT OUTSTANDING & DISB.											
A. Public & Publicly Guar. LT	5081.4	6367.8	7486.5	8768.8	10465.6	11244.1	13782.6	19284.4	23484	23474.6	24462
1. Official Creditors	2184.1	2628.1	3345.7	3771.4	4774.5	5331.7	6748.6	8153.8	10302.5	10956.2	11822
a. Multilateral	1034.4	1309.6	1831	2133.5	2833.6	2827.1	3478.7	4187.7	5008.9	4775	5178
aa of which IBRD	781.1	926.1	1329.8	1519.4	2047.5	1864.8	2420.5	3017.1	3746.7	3408	3491.7
ab of which IDA	32.2	33.9	41	48.6	61.2	71.1	84.1	91.8	99.1	101.7	102.3
b. Bilateral	1149.7	1318.5	1514.7	1637.9	1940.9	2504.6	3269.9	3966.1	5293.6	6181.2	6644
2. Private Creditors	2897.3	3739.7	4120.8	4997.4	5691.1	5912.4	7034	11130.6	13181.5	12518.4	12640
a. Suppliers	314.5	343.1	337	348.4	408.2	461.5	626.7	698.6	641.5	873	674
b. Commercial Banks	1643	2272.7	2689.8	3550.5	4032.8	4186.5	4997.1	8888.8	10640.6	9768.8	10607
c. Other Private	939.8	1123.9	1094	1098.5	1250.1	1264.4	1410.2	1543.2	1899.4	1876.6	1359
B. Private Non-Guaranteed LT	2071.3	2454.3	2760.7	3229.2	3125.4	2711	2600	2294	1516	992.4	874
C. Total LT DOD	7152.7	8822.1	10227.2	11998	13591	13955.1	16382.6	21578.4	25000	24467	25336
D. Use of IMF Credit	812.8	1044.3	1133.4	999.3	1094.7	885.4	1168.4	1266	1259.7	1093.1	1176.5
E. Short-Term Debt	5315	7556	9521	11465	9608	9402	9092	5486	3792	3888	3910
F. Total External Debt	13280.5	17422.4	20881.6	24462.3	24293.7	24242.5	26643	28330.4	30051.7	29448.1	30422.5

Source: Philippines Standard Tables, IEC, World Bank

TABLE 4.8:
External Debt Derived Indicators
DEBT RATIOS

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
BANK AND IDA RATIOS											
A. Share of Total Long-Term DOD											
1. IBRD as % of Total	10.2	10.5	13	12.7	15.1	13.4	14.8	14	15	13.9	13.8
2. IDA as % of Total	0.5	0.4	0.4	0.4	0.5	0.5	0.5	0.4	0.4	0.4	0.4
3. IBRD+IDA as % of Total	10.7	10.9	13.4	13.1	15.5	13.9	15.3	14.4	15.4	14.3	14.2
B. Share of LT Debt Service											
1. IBRD as % of Total	5.9	9.5	8.2	9.2	11.6	18.2	18.3	18.1	17.3	19.3	17.7
2. IDA as % of Total	0	0	0	0	0	0.1	0.1	0	0	0	0.1
3. IBRD+IDA as % of Total	6	9.6	8.2	9.2	11.7	18.2	18.3	18.1	17.3	19.4	17.7
C. DOD-to-Exports Ratios a/											
1. Long-Term Debt/Exports	110.9	107.5	115.7	145.6	163.5	172.8	204.1	245.3	266.4	221.4	202.6
2. IMF Credit/Exports	12.6	12.7	12.8	12.1	13.2	11	14.6	14.4	13.4	9.9	9.4
3. Short-Term Debt/Exports	82.4	92.1	107.7	139.1	115.6	116.4	113.3	62.4	40.4	35.2	31.3
4. LT+IMF+ST DOD/Exports	206	212.4	238.3	296.8	292.3	300.2	331.9	322.1	320.2	266.5	243.3
D. DOD-to-GDP Ratios											
1. Long-Term Debt/GDP	24.3	25	26.5	30.1	39.3	43.1	49.7	70.2	72.7	62.4	57.2
2. IMF Credit/GDP	2.8	3	2.9	2.5	3.2	2.7	3.5	4.1	3.7	2.8	2.7
3. Short-Term Debt/GDP	18	21.4	24.6	28.7	27.8	29	27.6	17.8	11	9.9	8.8
4. LT+IMF+ST DOD/GDP	45	49.4	54	61.3	70.3	74.9	80.9	92.2	87.4	75.1	68.7
E. Debt Service /Exports a/											
1. Public & Guranteed LT	12	7.1	9.7	12.4	14.3	14.1	15.9	22	27.9	24.7	22.6
2. Private Non-guranteed LT	10.4	6.4	7.8	10.5	6.9	3.8	3.6	3.6	2.6	2	1.6
3. Total Long-Term Debt Service	22.4	13.5	17.4	22.9	21.2	17.9	19.5	25.6	30.5	26.8	24.2
4. IMF Repurchases+Serv. Chgs.	2	2.3	1.3	1.9	2.9	3.9	3.2	4.3	4.7	2.4	2.5
5. Interest only on ST Debt	0	10.7	14.8	17.6	12.2	11.5	9.3	4.5	3.9	3.1	3.2
6. Total (LT+IMF+ST Int.)	24.4	26.5	33.5	42.4	36.3	33.3	32.5	34.4	39	32.3	29.9
F. Interest Burden Ratios											
1. Total Interest/GDP	1.7	1.6	2.1	2.3	2.7	2.9	2.8	3.7	4.2	4.2	5.5
2. Total Interest/Exports a/	7.6	7	9.3	11.2	11.3	11.4	11.7	12.9	15.3	14.8	15.3

a/ "Exports" are defined to include merchandize exports, receipts from services and workers remittances.
Source: Philippines Standard Tables, IEC, World Bank

TABLE 5.1:
External Trade by commodity type
(Volume Index & millions of current US$)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
A. VOLUME, VALUE AND PRICES											
MERCHANDISE EXPORTS:											
(Vol. Index 1980=100)											
X.FOOD.COCONUT OIL	88	100	113	100	109	64	71	136	112	86	83
X.FOOD.SUGAR	66	100	70	72	55	67	33	13	9	8	12
X.TIM.LUMBER & LOGS	149	100	86	92	104	95	66	54	45	40	28
X.MET.COPPER CONCENTRATE	92	100	100	93	69	39	30	32	32	39	37
Manufactures	85	100	115	115	123	143	125	118	133	156	..
Other Exports		100								99	..
Merchandise Exports (FOB)	87	100	107	104	97	99	96	103	102	111	122
(Value - Curr. mill. $)											
X.FOOD.COCONUT OIL	743	567	533	401	516	581	347	338	381	408	377
X.FOOD.SUGAR	212	624	567	416	299	308	169	87	60	60	89
X.TIM.LUMBER & LOGS	343	273	202	202	223	194	130	130	155	157	136
X.MET.COPPER CONCENTRATE	440	545	429	312	249	115	84	90	109	216	237
Manufactures	1485	2042	2406	2391	2495	3067	2765	2969	3642	4338	5192
Other Exports	1379	1737	1585	1298	1223	1127	1134	1234	1373	1895	1790
Merchandise Exports (FOB)	4601	5788	5722	5021	5005	5391	4629	4842	5720	7074	7821
MERCHANDISE IMPORTS:											
(Vol. Index 1980=100)											
Food	81	100	105	133	109	96	98	89	109	139	..
Other Consumer Goods	114	100	116	126	120	87	119	156	157	196	..
POL and Other Energy	102	100	96	91	101	80	73	87	88	109	129
Intermediate Goods	98	100	88	95	91	75	62	69	90	98	..
Primary	103	100	54	75	62	43	45	78	117	108	..
Manufactures	96	100	100	102	102	88	67	66	81	94	..
Capital Goods	..	100	..	..	..	..	..	..	..	82	..
Total Merch. Imports (CIF)	97	100	99	101	101	84	72	76	88	105	127
(Value - Curr. mill. $)											
Food	373	512	581	666	553	458	439	413	463	702	909
Other Consumer Goods	308	317	309	333	306	236	282	343	456	704	779
POL and Other Energy	1385	2248	2458	2105	2123	1649	1452	869	1249	1096	1397
Intermediate Goods	2291	2665	2673	2776	2807	2577	2150	2555	3359	4020	4910
Primary	476	691	814	827	905	1029	781	893	1101	2405	2685
Manufactures	1815	1974	1859	1949	1902	1548	1369	1662	2258	1615	2225
Capital Goods	1765	1986	1925	1786	1698	1150	788	864	1210	1637	2424
Total Merch. Imports (CIF)	6142	7727	7946	7667	7487	6070	5111	5044	6737	8159	10419
COUNTRY INDICES (1980=100):											
Merchandise Export Price	..	100	92.3	83.2	88.9	93.8	83.6	81.2	97.1	110.5	110.6
Merchandise Import Price	..	100	104.4	98.3	95.8	93.9	91.9	85.4	98.8	101.0	106.0
Merch. Terms of Trade	..	100	88.5	84.6	92.8	99.9	91.0	95.0	98.3	109.4	104.3

Source: Philippines Standard Tables, IEC, World Bank

TABLE 5.2:
External Trade with Commodity type
(percentages)

	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989
B. SHARES OF TOTAL X OR M (CP)											
MERCHANDISE EXPORTS:											
X.FOOD.COCONUT OIL	16.1	9.8	9.3	8.0	10.3	10.8	7.5	6.9	6.7	5.8	4.8
X.FOOD.SUGAR	4.6	10.8	9.9	8.3	6.0	5.7	3.6	1.8	1.1	0.8	1.1
X.TIM.LUMBER & LOGS	7.4	4.7	3.5	4.0	4.5	3.6	2.8	2.7	2.7	2.2	1.7
X.MET.COPPER CONCENTRATE	9.6	9.4	7.5	6.2	5.0	2.1	1.8	1.9	1.9	3.1	3.0
Manufactures	32.3	35.3	42.0	47.6	49.9	56.9	59.7	61.3	63.7	61.3	66.4
Other Exports	30.0	30.0	27.7	25.9	24.4	20.9	24.5	25.5	24.0	26.8	22.9
Merchandise Exports (FOB)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
MERCHANDISE IMPORTS:											
Food	6.1	6.6	7.3	8.7	7.4	7.5	8.6	8.2	6.9	8.6	8.7
Other Consumer Goods	5.0	4.1	3.9	4.3	4.1	3.9	5.5	6.8	6.8	8.6	7.5
POL and Other Energy	22.5	29.1	30.9	27.5	28.4	27.2	28.4	17.2	18.5	13.4	13.4
Intermediate Goods	37.3	34.5	33.6	36.2	37.5	42.5	42.1	50.7	49.9	49.3	47.1
Primary	7.7	8.9	10.2	10.8	12.1	17.0	15.3	17.7	16.3	29.5	25.8
Manufactures	29.6	25.5	23.4	25.4	25.4	25.5	26.8	33.0	33.5	19.8	21.4
Capital Goods	29.1	25.7	24.2	23.3	22.7	18.9	15.4	17.1	18.0	20.1	23.3
Total Merch. Imports (CIF)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
C. GROWTH RATES AT CONST. PRICES:											
MERCHANDISE EXPORTS:											
X.FOOD.COCONUT OIL	..	14.2	13.3	-11.4	8.4	-41.1	10.7	92.0	-17.5	-23.3	-3.8
X.FOOD.SUGAR	..	50.9	-29.6	2.1	-22.8	20.3	-50.6	-61.1	-26.7	-13.8	46.9
X.TIM.LUMBER & LOGS	..	-32.7	-14.0	7.2	12.7	-8.7	-30.5	-18.2	-17.2	-10.4	-29.4
X.MET.COPPER CONCENTRATE	..	8.8	-0.2	-6.9	-25.7	-42.8	-23.6	4.5	0.6	22.9	-5.3
Manufactures	..	18.1	15.0	-0.4	7.0	17.0	-13.0	-5.6	13.1	17.0	..
Other Exports	..	..	..	..	..	..	..	..	..	..	..
Merchandise Exports (FOB)	..	15.4	7.1	-2.6	-6.7	2.0	-3.6	7.7	-1.3	8.7	10.5
MERCHANDISE IMPORTS:											
Food	..	24.1	5.3	26.0	-18.0	-11.4	2.2	-9.9	23.0	27.3	..
Other Consumer Goods	..	-12.5	16.2	8.4	-4.8	-27.2	35.9	31.3	0.8	25.1	..
POL and Other Energy	..	-2.1	-3.6	-5.2	10.2	-20.7	-8.4	19.6	1.1	23.0	18.2
Intermediate Goods	..	2.5	-11.7	7.2	-3.6	-18.1	-17.6	12.2	30.7	8.1	..
Primary	..	-3.0	-45.6	37.0	-16.8	-30.1	3.2	74.6	49.4	-7.3	..
Manufactures	..	4.6	0.2	1.5	-0.2	-15.6	-21.3	-2.3	22.9	15.8	..
Capital Goods	..	..	..	..	..	..	..	..	..	..	..
Total Merch. Imports (CIF)	..	3.0	-1.5	2.4	0.2	-17.3	-13.9	6.1	15.5	18.4	21.8

Source: Philippines Standard Tables, IEC, World Bank

TABLE A.1: NATIONAL GOVERNMENT EXPENDITURES BY OBJECT, 1985-1989
(P Billion)

	1985	1986	1987	1988	1989
Current Expenditures	55.3	66.9	97.2	112.1	142.5
Personnel	22.9	25.0	32.8	40.8	51.4
O&M	13.2	15.0	21.2	19.5	26.6
Interest Payments	14.7	21.6	37.0	45.9	54.8
Subsidies	1.0	1.7	1.4	2.0	5.6
Tax Expenditures	0.0	0.0	0.5	1.0	0.9
Assistance to LGU's	3.5	3.6	4.3	2.9	3.2
Capital Outlays	23.1	28.4	18.3	18.6	26.2
Infrastructure	5.5	7.8	7.3	8.4	13.1
Corporate Equity	14.3	12.3	5.4	1.8	2.2
Capital Transfers to LGU's, etc.	0.0	4.4	0.0	1.5	0.0
Other Capital Outlays	3.3	3.9	5.6	6.9	10.9
Net Lending	1.7	15.1	7.1	5.4	3.7
Total Expenditures	80.1	110.4	122.6	136.1	172.4

Source: Department of Budget and Management.

TABLE A.2: NATIONAL GOVERNMENT EXPENDITURES BY OBJECT, 1985-1989
(Shares)

	1985	1986	1987	1988	1989
Current Expenditures	69.0%	60.6%	79.3%	82.4%	82.7%
Personnel	28.6%	22.6%	26.8%	30.0%	29.8%
O&M	16.5%	13.6%	17.3%	14.3%	15.4%
Interest Payments	18.4%	19.6%	30.2%	33.7%	31.8%
Subsidies	1.2%	1.5%	1.1%	1.5%	3.2%
Tax Expenditures	0.0%	0.0%	0.4%	0.7%	0.5%
Assistance to LGU's	4.4%	3.3%	3.5%	2.1%	1.9%
Capital Outlays	28.8%	25.7%	14.9%	13.7%	15.2%
Infrastructure	6.9%	7.1%	6.0%	6.2%	7.6%
Corporate Equity	17.9%	11.1%	4.4%	1.3%	1.3%
Capital Transfers to LGU's, etc.	0.0%	4.0%	0.0%	1.1%	0.0%
Other Capital Outlays	4.1%	3.5%	4.6%	5.1%	6.3%
Net Lending	2.1%	13.7%	5.8%	4.0%	2.1%
Total Expenditures	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Department of Budget and Management.

TABLE A.3: NATIONAL GOVERNMENT EXPENDITURES BY OBJECT, 1985-1989
(P Billion, 1980 prices)

	1985	1986	1987	1988	1989
Current Expenditures	23.2	27.7	37.3	39.2	45.1
Personnel	9.6	10.3	12.6	14.3	16.3
O&M	5.5	6.2	8.1	6.8	8.4
Interest Payments	6.2	8.9	14.2	16.1	17.3
Subsidies	0.4	0.7	0.5	0.7	1.8
Tax Expenditures	0.0	0.0	0.2	0.3	0.3
Assistance to LGU's	1.5	1.5	1.6	1.0	1.0
Capital Outlays	9.7	11.7	7.0	6.5	8.3
Infrastructure	2.3	3.2	2.8	2.9	4.1
Corporate Equity	6.0	5.1	2.1	0.6	0.7
Capital Transfers to LGU's, etc.	0.0	1.8	0.0	0.3	0.0
Other Capital Outlays	1.4	1.6	2.1	2.4	3.4
Net Lending	0.7	6.2	2.7	1.9	1.2
Total Expenditures	33.7	45.6	47.0	47.6	54.5

Source: Department of Budget and Management.

TABLE A.4: NATIONAL GOVERNMENT EXPENDITURES BY OBJECT, 1985-1989
(Percent of GNP)

	1985	1986	1987	1988	1989
Current Expenditures	9.3%	10.8%	13.8%	13.6%	14.8%
Personnel	3.8%	4.0%	4.6%	4.9%	5.3%
O&M	2.2%	2.[illegible]%	3.0%	2.4%	2.8%
Interest Payments	2.5%	3.5%	5.2%	5.6%	5.7%
Subsidies	0.2%	[illegible].3%	0.2%	0.2%	0.6%
Tax Expenditures	0.0%	0.0%	0.1%	0.1%	0.1%
Assistance to LGU's	0.6%	0.6%	0.6%	0.4%	0.3%
Capital Outlays	3.9%	4.6%	2.6%	2.3%	2.7%
Infrastructure	0.9%	1.3%	1.0%	1.0%	1.4%
Corporate Equity	2.4%	2.0%	0.8%	0.2%	0.2%
Capital Transfers to LGU's, etc.	0.0%	0.7%	0.0%	0.2%	0.0%
Other Capital Outlays	0.6%	0.6%	0.8%	0.8%	1.1%
Net Lending	0.3%	2.4%	1.0%	0.7%	0.4%
Total Expenditures	13.4%	17.8%	17.4%	16.5%	17.9%

Source: Department of Budget and Management.

TABLE A.5: 'NATIONAL EXPENDITURES BY SECTOR, OBLIGATION BASIS, 1985-1989 (in million pesos)

	1985	1986	1987	1988	1989
Economic Services	20241	28114	25039	26091	45964
Agriculture, Agrarian Reform and Natural Resources	4733	5149	7477	8429	16353
Trade & Industry	972	603	1001	890	1234
Tourism	152	136	156	256	298
Power & Energy	1345	1368	1778	211	936
Water Resource Development and Flood Control	1468	1594	1395	1412	3026
Communications, Roads and Other Transportation	9081	9051	9184	12945	19010
Other Economic Services	2490	10213	4048	1948	5107
Social Services	15274	21015	27493	31061	42148
Education, Culture and Manpower Development	10722	14838	17040	22022	29559
Health	3113	3570	4089	5564	7338
Social Security & Labor Welfare	741	826	1005	1147	1576
Land Distribution (CARP)	0	220	369	0	899
Housing and Community Development	671	1550	443	595	298
Other Social Services	27	11	4547	1733	2478
Defense	10067	11587	12549	18298	20431
General Public Services	10522	10662	12559	15730	18438
Net Lending	12535	15066	7641	4907	2727
Debt Service	18751	28061	69694	71320	97713
Interest Payments	14652	21612	36905	45864	51459
Debt amortization	4099	6449	32789	25456	46254
TOTAL	87390	114505	154975	167407	227421

Source: Department of Budget and Management

TABLE A.6: NATIONAL GOVERNMENT EXPENDITURES BY SECTOR, OBLIGATION BASIS, 1985-1989 (Shares)

	1985	1986	1987	1988	1989
Economic Services	23.2%	24.6%	16.2%	15.6%	20.2%
Agriculture, Agrarian Reform and Natural Resources	5.4%	4.5%	4.8%	5.0%	7.2%
Trade & Industry	1.1%	0.5%	0.6%	0.5%	0.5%
Tourism	0.2%	0.1%	0.1%	0.2%	0.1%
Power & Energy	1.5%	1.2%	1.1%	0.1%	0.4%
Water Resource Development and Flood Control	1.7%	1.4%	0.9%	0.8%	1.3%
Communications, Roads and Other Transportation	10.4%	7.9%	5.9%	7.7%	8.4%
Other Economic Services	2.8%	8.9%	2.6%	1.2%	2.2%
Social Services	17.5%	18.4%	17.7%	18.6%	18.5%
Education, Culture and Manpower Development	12.3%	13.0%	11.0%	13.2%	13.0%
Health	3.6%	3.1%	2.6%	3.3%	3.2%
Social Security & Labor Welfare	0.8%	0.7%	0.6%	0.7%	0.7%
Land Distribution (CARP)	0.0%	0.2%	0.2%	0.0%	0.4%
Housing and Community Development	0.8%	1.4%	0.3%	0.4%	0.1%
Other Social Services	0.0%	0.0%	2.9%	1.0%	1.1%
Defense	11.5%	10.1%	8.1%	10.9%	9.0%
General Public Services	12.0%	9.3%	8.1%	9.4%	8.1%
Net Lending	14.3%	13.2%	4.9%	2.9%	1.2%
Debt Service	21.5%	24.5%	45.0%	42.6%	43.0%
Interest Payments	16.8%	18.9%	23.8%	27.4%	22.6%
Debt amortization	4.7%	5.6%	21.2%	15.2%	20.3%
TOTAL	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Department of Budget and Management

TABLE A.7: NATIONAL GOVERNMENT EXPENDITURES BY SECTOR, OBLIGATION BASIS
1985-1989 (in million pesos, at 1980 prices)

	1985	1986	1987	1988	1989
Economic Services	8508	11622	9597	9126	14541
Agriculture, Agrarian Reform and Natural Resources	1989	2129	2866	2948	5173
Trade & Industry	409	249	384	311	390
Tourism	64	56	60	90	94
Power & Energy	565	566	681	74	296
Water Resource Development and Flood Control	617	659	535	494	957
Communications, Roads and Other Transportation	3817	3742	3520	4528	6014
Other Economic Services	1047	4222	1552	681	1616
Social Services	6420	8687	10538	10864	13334
Education, Culture and Manpower Development	4507	6134	6531	7703	9351
Health	1309	1476	1567	1946	2321
Social Security & Labor Welfare	311	341	385	401	499
Land Distribution (CARP)	0	91	141	0	284
Housing and Community Development	282	641	170	208	94
Other Social Services	11	5	1743	606	784
Defense	4232	4790	4810	6400	6463
General Public Services	4423	4408	4814	5502	5833
Net Lending	5269	6228	2929	1716	863
Debt Service	7882	11600	26713	24946	30912
Interest Payments	6159	8934	14145	16042	16279
Debt amortization	1723	2666	12568	8904	14633
TOTAL	36734	47336	59400	58554	71946

Source: Department of Budget and Management

TABLE A.8: NG EXPENDITURES BY SECTOR, OBLIGATION BASIS, 1985-1989 (percent of GNP)

	1985	1986	1987	1988	1989
Economic Services	3.4%	4.5%	3.5%	3.2%	4.8%
Agriculture, Agrarian Reform and Natural Resources	0.8%	0.8%	1.1%	1.0%	1.7%
Trade & Industry	0.2%	0.1%	0.1%	0.1%	0.1%
Tourism	0.0%	0.0%	0.0%	0.0%	0.0%
Power & Energy	0.2%	0.2%	0.3%	0.0%	0.1%
Water Resource Development and Flood Control	0.2%	0.3%	0.2%	0.2%	0.3%
Communications, Roads and Other Transportation	1.5%	1.5%	1.3%	1.6%	2.0%
Other Economic Services	0.4%	1.6%	0.6%	0.2%	0.5%
Social Services	2.6%	3.4%	3.9%	3.8%	4.4%
Education, Culture and Manpower Development	1.8%	2.4%	2.4%	2.7%	3.1%
Health	0.5%	0.6%	0.6%	0.7%	0.8%
Social Security & Labor Welfare	0.1%	0.1%	0.1%	0.1%	0.2%
Land Distribution (CARP)	0.0%	0.0%	0.1%	0.0%	0.1%
Housing and Community Development	0.1%	0.3%	0.1%	0.1%	0.0%
Other Social Services	0.0%	0.0%	0.6%	0.2%	0.3%
Defense	1.7%	1.9%	1.8%	2.2%	2.1%
General Public Services	1.8%	1.7%	1.8%	1.9%	1.9%
Net Lending	2.1%	2.4%	1.1%	0.6%	0.3%
Debt Service	3.1%	4.5%	9.9%	8.6%	10.1%
Interest Payments	2.5%	3.5%	5.2%	5.6%	5.3%
Debt amortization	0.7%	1.0%	4.6%	3.1%	4.8%
TOTAL	14.6%	18.5%	21.9%	20.3%	23.6%

Source: Department of Budget and Management

TABLE A.9: NATIONAL GOVERNMENT REVENUES BY SOURCE, 1985-1989
(P Billion)

	1985	1986	1987	1988	1989
Tax Revenues	61.1	65.5	85.9	90.3	123.1
BIR	42.6	46.8	58.6	63.7	82.6
Domestic based	41.0	46.4	58.3	63.2	82.1
Net Income	18.6	19.1	21.8	27.9	37.6
Excise Taxes	13.5	16.4	22.6	20.2	24.9
Sales Tax, VAT & Licenses	7.6	9.2	12.1	11.6	15.7
Other domestic taxes	1.3	1.7	1.8	3.5	3.9
Int'l trade	1.6	0.4	0.3	0.5	0.5
Travel Tax	1.4	0.3	0.3	0.5	0.5
Others	0.2	0.1	0.C	0.0	0.0
Bu. of Customs	16.8	17.5	26.0	25.0	38.4
Import Duties	15.8	16.9	26.0	25.0	35.1
VAT on imports	0.0	0.0	0.0	0.0	3.3
Export Taxes	1.0	0.6	0.0	0.0	0.0
Other offices	1.7	1.2	1.3	1.6	2.1
Motor vehicle tax	1.0	1.0	1.1	1.3	1.5
Real Property tax	0.1	0.1	0.2	0.3	0.5
Special Oil Impost	0.5	0.0	0.0	0.0	0.0
Others	0.1	0.1	0.0	0.0	0.1
Non-Tax Revenues	7.7	13.8	17.3	22.6	30.4
Collection from other offices	6.5	7.4	8.3	10.0	13.5
Foreign Grants	0.1	0.2	1.4	1.4	1.3
ESF	1.1	6.2	3.1	0.2	4.8
PCGG Collections	0.0	0.0	0.2	3.0	0.5
APT Collections	0.0	0.0	1.0	3.0	1.5
Interest income from CB	0.0	0.0	1.8	4.7	6.1
Interest on Advances to corporations	0.0	0.0	1.5	0.3	2.7
Total revenues	68.8	79.3	103.2	112.9	153.5

Source: Bureau of Treasury

TABLE A.10: NATIONAL GOVERMENT REVENUES BY SOURCE, 1985-1989
(Shares)

	1985	1986	1987	1988	1989
Tax Revenues	88.8%	82.6%	83.2%	80.0%	80.2%
BIR	61.9%	59.0%	56.8%	56.4%	53.8%
Domestic based	59.6%	58.5%	56.5%	56.0%	53.5%
Net Income	27.0%	24.1%	21.1%	24.7%	24.5%
Excise Taxes	19.6%	20.7%	21.9%	17.9%	16.2%
Sales Tax, VAT & Licenses	11.0%	11.6%	11.7%	10.3%	10.2%
Other domestic taxes	1.9%	2.1%	1.7%	3.1%	2.5%
Int'l trade	2.3%	0.5%	0.3%	0.4%	0.3%
Travel Tax	2.0%	0.4%	0.3%	0.4%	0.3%
Others	0.3%	0.1%	0.0%	0.0%	0.0%
Bu. of Customs	24.4%	22.1%	25.2%	22.1%	25.0%
Import Duties	23.0%	21.3%	25.2%	22.1%	22.9%
VAT on imports	0.0%	0.0%	0.0%	0.0%	2.1%
Export Taxes	1.5%	0.8%	0.0%	0.0%	0.0%
Other offices	2.5%	1.5%	1.3%	1.4%	1.4%
Motor vehicle tax	1.5%	1.3%	1.1%	1.2%	1.0%
Real Property tax	0.1%	0.1%	0.2%	0.3%	0.3%
Special Oil Impost	0.7%	0.0%	0.0%	0.0%	0.0%
Others	0.1%	0.1%	0.0%	0.0%	0.1%
Non-Tax Revenues	11.2%	17.4%	16.8%	20.0%	19.8%
Collection from other offices	9.4%	9.3%	8.0%	8.9%	8.8%
Foreign Grants	0.1%	0.3%	1.4%	1.2%	0.8%
ESF	1.6%	7.8%	3.0%	0.2%	3.1%
PCGG Collections	0.0%	0.0%	0.2%	2.7%	0.3%
APT Collections	0.0%	0.0%	1.0%	2.7%	1.0%
Interest income from CB	0.0%	0.0%	1.7%	4.2%	4.0%
Interest on Advances to corporations	0.0%	0.0%	1.5%	0.3%	1.8%
Total revenues	100.0%	100.0%	100.0%	100.0%	100.0%

Source: Bureau of Treasury.

TABLE A.11: NATIONAL GOVERNMENT REVENUES BY SOURCE 1985-1989
(P Billion, 1980 prices)

	1985	1986	1987	1988	1989
Tax Revenues	25.7	27.1	32.9	31.6	38.9
BIR	17.9	19.3	22.5	22.3	26.1
Domestic based	17.2	19.2	22.3	22.1	26.0
Net Income	7.8	7.9	8.4	9.8	11.9
Excise Taxes	5.7	6.8	8.7	7.1	7.9
Sales Tax, VAT & Licenses	3.2	3.8	4.6	4.1	5.0
Other domestic taxes	0.5	0.7	0.7	1.2	1.2
Int'l trade	0.7	0.2	0.1	0.2	0.2
Travel Tax	0.6	0.1	0.1	0.2	0.2
Others	0.1	0.0	0.0	0.0	0.0
Bu. of Customs	7.1	7.2	10.0	8.7	12.1
Import Duties	6.6	7.0	10.0	8.7	11.1
VAT on imports	0.0	0.0	0.0	0.0	1.0
Export Taxes	0.4	0.2	0.0	0.0	0.0
Other offices	0.7	0.5	0.5	0.6	0.7
Motor vehicle tax	0.4	0.4	0.4	0.5	0.5
Real Property tax	0.0	0.0	0.1	0.1	0.2
Special Oil Impost	0.2	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0
Non-Tax Revenues	3.2	5.7	6.6	7.9	9.6
Collection from other offices	2.7	3.1	3.2	3.5	4.3
Foreign Grants	0.0	0.1	0.5	0.5	0.4
ESF	0.5	2.6	1.2	0.1	1.5
PCGG Collections	0.0	0.0	0.1	1.0	0.2
APT Collections	0.0	0.0	0.4	1.0	0.5
Interest income from CB	0.0	0.0	0.7	1.6	1.9
Interest on Advances to corporations	0.0	0.0	0.6	0.1	0.9
Total revenues	28.9	32.8	39.6	39.5	48.6

Source: Bureau of Treasury

TABLE A.12: NATIONAL GOVERNMENT REVENUES BY SOURCE, 1985-1989
(Percent of GNP)

	1985	1986	1987	1988	1989
Tax Revenues	10.2%	10.6%	12.2%	10.9%	12.8%
BIR	7.1%	7.6%	8.3%	7.7%	8.6%
Domestic based	6.9%	7.5%	8.3%	7.7%	8.5%
Net Income	3.1%	3.1%	3.1%	3.4%	3.9%
Excise Taxes	2.3%	2.6%	3.2%	2.4%	2.6%
Sales Tax, VAT & Licenses	1.3%	1.5%	1.7%	1.4%	1.6%
Other domestic taxes	0.2%	0.3%	0.3%	0.4%	0.4%
Int'l trade	0.3%	0.1%	0.0%	0.1%	0.1%
Travel Tax	0.2%	0.0%	0.0%	0.1%	0.1%
Others	0.0%	0.0%	0.0%	0.0%	0.0%
Bu. of Customs	2.8%	2.8%	3.7%	3.0%	4.0%
Import Duties	2.6%	2.7%	3.7%	3.0%	3.6%
VAT on imports	0.0%	0.0%	0.0%	0.0%	0.3%
Export Taxes	0.2%	0.1%	0.0%	0.0%	0.0%
Other offices	0.3%	0.2%	0.2%	0.2%	0.2%
Motor vehicle tax	0.2%	0.2%	0.2%	0.2%	0.2%
Real Property tax	0.0%	0.0%	0.0%	0.0%	0.1%
Special Oil Impost	0.1%	0.0%	0.0%	0.0%	0.0%
Others	0.0%	0.0%	0.0%	0.0%	0.0%
Non-Tax Revenues	1.3%	2.2%	2.4%	2.7%	3.1%
Collection from other offices	1.1%	1.2%	1.2%	1.2%	1.4%
Foreign Grants	0.0%	0.0%	0.2%	0.2%	0.1%
ESF	0.2%	1.0%	0.4%	0.0%	0.5%
PCGG Collections	0.0%	0.0%	0.0%	0.4%	0.1%
APT Collections	0.0%	0.0%	0.1%	0.4%	0.2%
Interest income from CB	0.0%	0.0%	0.3%	0.6%	0.6%
Interest on Advances to corporations	0.0%	0.0%	0.2%	0.0%	0.3%
Total revenues	11.5%	12.8%	14.6%	13.7%	15.9%

Source: Bureau of Treasury.

TABLE A.13: CB NET INCOME POSITION: 1986-1989

	1986	1987	1988	1989
I. Net Interest Income/ Expense (-)	-18.5	-10.2	-16.2	-20.3
A. Interest Income	8.8	8.1	7.0	6.6
1. Domestic Assets	7.8	6.2	5.7	5.3
Loans and Advances	6.8	5.1	4.9	4.5
Overdrafts	.1	.3	.03	.03
Domestic Securities	.9	.8	.8	.7
2. Foreign Assets	1.0	1.9	1.3	1.3
B. Interest Expenses	27.2	18.3	23.2	26.9
1. Domestic Liabilities	11.2	4.8	8.5	10.7
Legal Reserves	.5	.7	.9	1.2
Blocked Peso Differential	2.0	.9	1.2	1.6
NG Deposits	--	1.8	5.1	6.3
Open Market Instruments	8.7	1.4	1.3	1.6
2. Foreign Liabilities	16.0	13.5	14.7	16.2
II. Forward Cover Losses	-0.7	-0.1	-0.02	-0.02
III. Swap Cover Profits/Losses	1.0	-.5	-.7	-.8
Overall CB Surplus (+)/ Deficit (-)	-18.2	-10.9	-16.9	-21.1

Source: Central Bank of the Philippines

TABLE A.14: REVENUES AND INTERNAL CASH GENERATION OF 14 MAJOR GOVERNMENT CORPORATIONS IN 1989

	Revenues		Internal Cash Generation	
	Actual	Program	Actual	Program
Total	63.5	57.9	10.4	8.4
National Power Corp. (NPC)	22.2	21.7	6.6	6.1
Phil. National Oil Co. (PNOC)	26.0	20.7	2.5	1.2
Metropolitan Waterworks Sewerage System	2.6	2.5	0.2	0.2
National Irrigation Authority (NIA)	2.0	2.2	-0.6	-0.3
National Development Co. (NDC)	1.3	1.6	0.7	0.9
Light Rail Transit Authority (LRTA)	0.6	0.5	-0.1	-0.1
Local Water Utilities Administration (LWUA)	0.3	0.2	0.1	0.0
National Electrification Administration (NEA)	0.8	0.8	-0.1	-0.1
National Housing Authority (NHA)	0.5	0.5	0.2	0.2
Phil. National Railways	0.5	0.5	0.1	0.1
Phil. Ports Authority (PPA)	1.4	1.3	0.5	0.5
National Food Authority (NFA)	4.8	4.6	0.5	-0.2
Export Processing Zone Authority (EPZA)	0.2	0.2	0.0	0.0
Metro Manila Transport Commission (MMTC)	0.4	0.3	0.1	0.1

Source: GCMCC

TABLE A.15: EXPENDITURES OF 14 MAJOR GOVERNMENT CORPORATIONS IN 1989 (P BILLION)

	Current		Capital	
	Actual	Program	Actual	Progra
Total	53.1	49.4	18.2	17.8
National Power Corp. (NPC)	15.6	15.5	8.3	8.3
Phil. National Oil Co. (PNOC)	23.5	19.6	3.6	1.8
Metropolitan Waterworks Sewerage System (MVSS)	2.4	2.2	1.3	1.3
National Irrigation Authority (NIA)	2.6	2.6	2.4	2.5
National Development Co. (NDC)	0.6	0.6	0.2	0.1
Light Rail Transit Authority (LRTA)	0.6	0.6	0.1	0.1
Local Water Utilities Administration (LWUA)	0.2	0.2	0.6	0.8
National Electrification Administration (NEA)	1.0	1.0	0.8	0.8
National Housing Authority (NHA)	0.3	0.3	0.4	0.5
Phil. National Railways (PNR)	0.5	0.4	0.2	0.4
Phil. Ports Authority (PPA)	0.8	0.8	0.4	0.8
National Food Authority (NFA)	4.3	4.8	-0.5	-0.2
Export Processing Zone Authority (EPZA)	0.3	0.2	0.1	0.1
Metro Manila Transport Commission (MMTC)	0.3	0.3	0.2	0.3

Source: GCMCC

TABLE A-16: COMPARATIVE SCHEDULE OF INCOME AND EXPENDITURES FOR LOCAL GOVERNMENT UNITS, ALL FUNDS: 1980 TO 1987
(In million pesos)

Income/ Expenditure	1980	1982	1985	1986	1987
Income					
Tax Revenue	3,280.6	4,501.2	6,198.5	6,537.3	6,777.4
Operating & Miscellaneous Revenues	638.2	879.2	1,430.7	1,322.8	1,460.3
Capital Revenue	6.7	9.8	15.3	5.0	8.6
Grants	368.0	459.5	747.8	734.2	632.9
Extraordinary Income	7.3	11.7	38.8	12.1	30.4
Borrowing	272.6	67.7	79.2	49.7	13.4
Total Income	4,573.4	5,929.1	8,510.3	8,661.1	8,923.5
Expenditures					
Personal Services	1,664.9	2,358.0	3,732.3	4,355.5	4,819.6
Maintenance and Other Operating Expenses	1,871.3	2,393.7	3,569.0	3,484.4	3,654.6
Capital Outlay	953.8	961.1	1,206.6	878.8	1,113.0
Total Expenditures	4,490.0	5,712.8	8,507.9	8,718.7	9,587.2

TABLE A-17: ASSETS, INVESTMENTS AND EARNINGS OF THE SOCIAL SECURITY SYSTEM 1/: 1980 TO 1988
(in million pesos)

Year	Year-End Assets	Year-End Investments	Yearly Earnings
1980	8,220.7	8,066.3	779.5
1981	9,958.2	9,711.3	1,013.6
1982	11,834.0	11,538.5	1,270.5
1983	13,936.6	13,633.2	1,577.0
1984	17,155.9	16,449.0	2,573.0
1985	22,245.8	21,121.5	4,335.6
1986	26,155.1	25,290.7	3,961.4
1987	36,664.9	35,422.8	4,386.9

1/ Excludes Medicare and Employees' Compensation

Source: Philippines Statistical Year Book, 1989.

TABLE A-18: FINANCIAL CONDITION OF GOVERNMENT SERVICE INSURANCE SYSTEM
(in million pesos)

Year	Assets	Reserves	Surplus
1980	9,245.8	8,210.7	672.1
1981	10,943.8	9,789.1	782.5
1982	13,312.3	11,514.0	992.2
1983	14,610.0	12,959.7	937.7
1984	15,641.7	13,961.3	672.3
1985	16,752.9	15,225.3	521.5
1986	19,326.2	18,113.9	(562.0)
1987	22,537.5	18,931.9	1,034.0
1988	24,899.5	21,537.3	1,415.0

Source: Philippines Statistical Yearbook, 1989

TABLE A-19: INTERNAL DEBT OUTSTANDING CLASSIFIED BY LEVEL OF GOVERNMENT: 1950 TO 1988

End of Period	Total	National Government	Local Government	Government Corporations	Monetary Institutions
1980	41,181.6	21,875.5	335.9	4,978.5	13,991.7
1981	49,364.6	28,657.0	361.7	6,656.4	13,689.5
1982	57,563.4	35,343.6	431.9	9,855.5	11,932.4
1983	61,114.4	41,841.3	380.5	12,157.1	6,735.5
1984	84,146.2	57,735.1	174.0	13,206.0	13,031.1
1985	116,286.5	75,972.2	182.4	14,003.8	26,128.1
1986	144,351.6	108,085.2	161.3	12,411.1	23,694.0
1987	161,100.3	150,751.2	116.0	9,313.3	919.8

Source: Central Bank of the Philippines.

TABLE A-20: INTERNAL DEBT OUTSTANDING CLASSIFIED BY PERIOD OF MATURITY: 1950 TO 1988
(in million pesos)

End of Period	Total	Long Term	Medium Term	Short Term
1980	41,181.6	13,533.5	16,683.5	10,964.6
1981	49,364.6	16,476.6	17,616.7	15,271.3
1982	57,563.4	20,085.1	19,579.0	17,899.3
1983	61,114.4	21,727.7	24,971.9	14,414.8
1984	84,146.2	21,086.5	24,153.6	38,906.1
1985	116,286.5	26,278.2	20,427.4	69,580.9
1986	144,351.6	27,595.8	16,976.2	99,779.6
1987	161,100.3	24,252.2	22,997.2	113,850.9

Source: Central Bank of the Philippines.

TABLE A-21: HOLDERS OF OUTSTANDING GOVERNMENT DOMESTIC SECURITIES: 1977 TO 1988
(in million pesos)

End of Period	Total 1/	Central Bank	Commercial and Other Banks	Trust Funds	Semi-Government Entities	Private Sector
1980	34,000.2	4,657.7	12,969.5	4,326.6	6,990.5	5,055.9
1981	38,199.5	5,002.7	13,760.8	4,897.4	9,561.0	4,977.6
1982	46,713.6	7,809.7	16,232.0	5,279.9	10,917.7	6,474.3
1983	48,599.2	8,368.2	16,375.5	5,749.0	13,552.9	4,553.6
1984	69,590.3	11,336.6	20,867.1	6,522.5	11,892.8	18,971.3
1985	94,889.8	12,182.0	19,728.2	7,340.6	14,016.1	41,622.9
1986	123,711.1	11,070.1	26,116.5	7,809.8	15,062.4	63,652.3
1987	150,299.6	9,156.8	21,405.2	10,032.7	20,607.6	89,097.3

1/ Revised to exlude dollar treasury bills and Central Bank certificate of indebtedness (CBCIs).

Source: Central Bank of the Philippines.

Table B.1 - MONEY SUPPLY AND ITS ORIGIN: 1980 TO 1988
(in million Pesos)

End of Period	Money Supply	Net Foreign Assets	Net Domestic Credits	Non-Money Supply Deposits	Net Other Accounts
1980	22,537.0	(17,303.3)	96,209.0	48,392.0	7,977.0
1981	28,523.0	(22,835.0)	117,678.0	61,692.0	9,628.0
1982	28,495.4	(41,601.2)	141,493.7	74,516.9	1,880.2
1983	32,489.3	(74,494.9)	171,396.2	83,371.2	(18,959.2)
1984	33,629.4	(99,937.3)	167,005.5	90,894.9	(57,456.1)
1985	35,826.6	(121,663.9)	156,745.0	99,473.5	(100,219.0)
1986	42,657.2	(112,514.3)	124,728.0	101,463.5	(131,907.0)
1987	52,090.3	(106,213.1)	108,380.4	110,346.5	(162,269.5)
1988	59,548.4	(94,713.0)	121,941.7	139,283.3	(170,603.0)

Source: Central Bank of the Philippines.

Table B.2: DOMESTIC LIQUIDITY, COMPOSITION OF MONEY SUPPLY AND QUASI-MONEY DEPOSITS: 1980 TO 1988

(In Million Pesos)

End of Period	Money Supply				Quasi-Money Deposits			Deposits Substitutes
	Domestic	Total	Currency	Peso Deposits Subject to Check	Total	Savings Deposits	Time Deposits	
1980	67,803.20	22,537.50	10,174.60	12,362.90	32,894.30	19,529.90	13,364.40	12,371.40
1981	82,091.30	23,524.30	11,625.80	11,898.50	42,114.80	24,198.30	17,916.50	16,452.20
1982	95,268.80	23,495.40	12,680.20	10,815.20	55,207.80	28,919.30	26,288.50	16,565.60
1983	112,962.10	32,489.30	19,607.30	12,882.00	63,366.50	34,089.70	29,276.80	17,106.30
1984	121,215.20	33,629.40	21,797.90	11,831.50	76,310.10	38,189.90	38,120.20	11,275.70
1985	132,882.50	35,826.60	24,066.10	11,760.50	88,447.40	46,412.50	42,034.90	8,608.50
1986	141,139.90	42,657.20	29,311.00	13,346.20	98,608.20	60,557.20	38,051.10	4,874.50
1987	159,232.00	52,090.20	35,451.70	16,638.50	103,536.40	70,632.50	32,903.90	3,605.40
1988	194,940.00	59,548.40	40,724.60	18,823.80	13,857.40	89,682.60	43,179.80	2,534.20

Source: Central Bank of the Philippines

Table B.3: FACTORS AFFECTING MONEY SUPPLY: 1980 TO 1988
(In Million Pesos)

End of Period	Money Supply	Internal Sector: Total	Internal Sector: Public Sector	Internal Sector: Private Sector	External Sector
1980	22,537.00	39,840.00	14,993.00	24,847.00	(17,303.00)
1981	23,523.00	46,358.00	19,497.00	26,861.00	(22,835.00)
1982	23,495.40	65,096.60	35,304.20	29,792.40	(41,601.20)
1983	32,489.30	106,984.20	75,527.70	31,456.50	(74,494.90)
1984	33,629.40	133,566.70	118,986.40	14,580.30	(99,937.30)
1985	35,826.60	157,490.50	138,413.10	19,077.40	(121,663.90)
1986	42,677.20	155,171.50	171,224.20	(16,052.70)	(112,494.30)
1987	52,090.30	160,303.40	178,876.50	(18,573.10)	(108,213.10)
1988	59,548.40	154,261.40	186,822.30	(32,560.90)	(94,713.00)

Source: Central Bank of the Philippines

TABLE B.4: ASSETS AND LIABILITIES
BY INSTITUTION: 1980 TO 1988
(in million Pesos)

End of Period	Central Bank		Commercial Banks	
	Total Assets	Total Liabilities	Total Assets	Total Liabilities
1980	65,447.3	64,943.4	138,417.1	127,709.3
1981	71,571.2	71,042.1	164,614.6	150,565.4
1982	91,691.8	91,169.1	190,979.4	174,248.1
1983	130,371.1	129,817.9	247,928.2	227,956.2
1984	206,026.5	205,434.5	289,150.9	264,492.5
1985	251,611.9	250,970.6	283,347.1	261,770.3
1986	294,810.1	294,149.3	293,418.9	271,013.0
1987	325,185.0	324,473.0	274,562.2	242,516.4

Savings Banks		Rural Banks		Development Banks	
Total Assets	Total Liabilities	Total Assets	Total Liabilities	Total Assets	Total Liabilities
7,352.4	6,730.8	5,642.2	4,769.5	29,284.1	24,089.5
6,930.5	6,447.1	6,631.2	5,607.8	38,079.1	31,997.1
5,872.4	5,415.7	8,136.5	6,965.3	48,348.7	41,087.9
7,399.4	6,825.9	9,499.7	8,107.5	60,553.5	52,760.8
7,613.8	6,963.4	9,023.3	7,513.0	72,236.4	65,426.1
6,847.2	6,400.1	8,821.7	7,240.8	79,035.6	71,605.5
8,124.4	7,540.9	9,350.5	7,651.6	75,037.4	68,944.6
10,534.1	9,722.2	9,960.8	8,101.1	18,498.8	12,077.5

Source: Central Bank of the Philippines

Table B.5: TOTAL LOANS AND INVESTMENTS OUTSTANDING BY INSTITUTION: 1980 TO 1988
(in million Pesos)

Period	Total	Commercial Banks	Rural Banks	Development Banks	Savings Banks 1/
1980	135,802.4	102,064.2	4,820.7	23,459.9	5,457.6
1981	162,652.9	117,789.8	5,658.9	33,929.6	5,274.6
1982	188,704.9	136,507.8	6,923.1	40,683.8	4,590.2
1983	236,238.0	171,558.5	7,974.0	51,013.9	5,691.6
1984	247,293.2	180,667.5	7,384.0	53,731.5	5,510.2
1985	215,453.3	162,171.6	7,072.5	41,412.7	4,796.5
1986	189,052.4	163,377.2	7,266.4	12,485.0	5,923.8
1987 2/	143,914.0	113,472.7	7,693.7	14,611.8	8,135.8
1988	163,296.2	130,405.8	8,428.4	15,757.4	8,704.6

1/ Banco Filipino not included (closed) starting 1985; PAIC Bank not included (closed) starting 1985.

2/ After transfer of selected assets and liabilities of one specialized government bank.

Source: Central Bank of the Philippines.

Table B.6: TOTAL INVESTMENTS IN SECURITIES BY INSTITUTION: 1980 TO 1988
(In million pesos)

Period	Total	Commercial Banks	Rural Banks	Development Banks	Savings Banks 1/
1980	20484.9	13314.4	130	6053	987.5
1981	25353.4	15386.4	170.8	8976.9	819.3
1982	30519.4	18689.1	253.1	10700.9	876.3
1983	34616.7	21443.5	326	11919.8	927.4
1984	42665.1	29679.4	361.5	12140.1	485.1
1985	39679.5	27667.6	436.2	10409.5	1166.2
1986	35778.9	31015.0	475.9	2865.0	1423.0
1987 2/	36570.0	29298.4	466.7	5570.4	1234.5
1988	50093.8	41666.4	458.2	5788.8	2180.4

1/ Beginning 1959, includes private development banks.

2/ After transfer of selected assets and liabilities of one specialized government bank.

Source: Central Bank of the Philippines

TABLE B.7: PUBLIC SECTOR SHARE OF GROSS DOMESTIC CREDITS OF DEPOSIT MONEY BANKS

	1980	1982	1984	1985	1986	1987	1988
				(Million Pesos)			
Government	12,983	19,046	32,983	28,975	32,601	32,166	46,193
Securities	5,843	10,918	15,127	12,256	18,531	20,328	32,347
Loans	7,141	8,128	17,856	16,720	14,070	11,838	13,846
Total	95,842	130,310	158,477	142,547	125,574	141,308	174,281
				(Shares)			
Government	13.55%	14.62%	20.81%	20.33%	25.96%	22.76%	26.50%
Securities	6.10%	8.38%	9.55%	8.60%	14.76%	14.39%	18.56%
Loan	7.45%	6.24%	11.27%	11.73%	11.20%	8.38%	7.94%
Total	100%	100%	100%	100%	100%	100%	100%

Source: Central Bank of the Philippines

TABLE B.8 LEGAL RESERVE REQUIREMENTS AGAINST PESO DEPOSIT LIABILITIES OF COMMERCIAL BANKS, 1980-1990

	Reserve Ratio (percent)			
Effective Date	Demand	Savings	Time	"NOW" Accts.
August 22, 1980	20	20	20	
February 27, 1981	16	16	16 & 5	16
January 1, 1982	18	18	18 & 1	18
September 1, 1983	19	19	19 & 4	19
October 1, 1983	21-1/2	21-1/2	21-1/2 & 4	21-1/2
December 1, 1983	23	23	23 & 4	23
January 1, 1984	23	23	23 & 5	23
April 25, 1984	24	24	24 & 6	24
September 30, 1985	23	23	23	23
May 26, 1986	22	22	22 & 6	22
August 4, 1986	21	21	21 & 6	21
December 1, 1986	21	21	21 & 5	21
June 23, 1989	21	21	21 & 7	21
August 4, 1989	21	21	21 & 9	21
September 4, 1989	20-1/2	20-1/2	20-1/2 & 13	20-1/2
October 5, 1989	20	20	20 & 17	20
November 5, 1989	20	20	20	20
March 26, 1990	21	21	21	21

Source: Central Bank of the Philippines

TABLE B.9: DIFFERENCES BETWEEN VARIOUS INTEREST RATES

	A	B	C	D	D-A	D-B	D-C
	Savings	Time	MRR	T-Bills			
1980	9.000	13.417	-	12.312	3.312	-1.105	-
1981	9.202	14.744	-	12.884	3.682	-1.860	-
1982	9.817	15.429	15.157	14.422	4.605	-1.007	-0.735
1983	9.729	15.288	14.896	14.520	4.791	-0.768	-0.376
1984	9.855	22.277	23.437	27.557*	17.699	5.277	4.117
1985	10.842	21.980	20.980	26.754*	15.912	4.774	5.774
1986	7.993	14.255	12.385	15.852	7.849	1.597	3.457
1987	4.530	9.833	9.203	13.077	8.547	3.244	3.874
1988	4.100	13.161	12.497	15.721	11.621	2.560	3.224
1989	4.372	15.724	16.255	19.462	15.009	3.738	3.207

Source: CB

* From July 1984 to Oct. 1986, issuance of T-Bill rates were on a negotiated basis. This was reverted to an auction basis starting November, 1986.

TABLE B.10: LOANS GRANTED BY COMMERCIAL BANKS, BY INDUSTRY
(PB)

	1981	1982	1983	1984	1985	1986	1987	1988	1989*
Total:	252.4	276.6	307.9	322.2	264.7	320.0	359.3	366.6	267.9
Agriculture	18.9	20.8	22.5	23.7	23.9	20.9	21.2	25.6	21.3
Mining	11.5	15.1	14.8	19.0	12.8	8.4	5.5	7.8	16.3
Manufacturing	85.4	83.7	109.3	115.6	87.2	82.2	94.2	123.9	113.8
Trade	58.6	58.1	58.3	63.4	41.1	46.4	54.2	59.0	47.0
Financing, Insurance & Business Services	55.3	71.8	74.3	66.2	76.5	137.9	151.2	103.7	29.0
Real Estate	3.4	3.6	4.2	5.0	2.9	2.0	3.5	6.4	9.7

*As of end-September, 1989

Source: Department of Economic Research - Domestic, Central Bank of the Philippines.

Table C.1: BALANCE OF PAYMENTS, 1985-89
($ Million)

	1985	1986	1987	1988	1989
Current Account	-103	996	-539	-389	-1554
Merchandise Trade	-482	-202	-1017	-1085	-2598
Exports	4629	4842	5720	7074	7821
Imports	5111	5044	6737	8159	10419
Non-Merchandise Trade	0	757	-76	-93	369
Inflow	3288	3791	3497	3590	4586
Outflow	3288	3034	3573	3683	4217
Transfers	379	441	554	789	675
Inflow	388	445	556	791	676
Outflow	9	4	2	2	1
Non-Monetary Capital Account	1711	39	588	642	1613
Long-term loans	2787	815	242	-329	367
Inflows	3962	2545	2437	2372	2787
Outflow	1175	1730	2195	2701	2420
Foreign Investments	17	140	205	986	854
Inflow	124	186	318	1077	972
Outflow	107	46	113	91	118
Short-Term Capital (NRT)	1731	-814	52	-205	-33
Errors & Omissions	638	-102	89	190	425
Monetization of gold	221	279	365	314	288
Unremittable Arrears/Adjustments	560	--	--	--	--
Revaluation Adjustments	-88	-72	-150	83	101
Debt Reduction				73	223
Overall Surplus (+)/Deficit (-)	2301	1242	264	650	448

Source: Central Bank

Table C.2: EXPORTS BY COMMODITY
($ Million)

	1985	1986	1987	1988	1989
Coconut Products	459	470	561	582	541
Sugar Products	185	103	71	74	2 113
Fruits & Vegetables	135	137	150	306	319
Other Agro-based Products	551	602	585	480	454
Forest Products	199	201	243	261	197
Mineral Products	243	267	224	764	829
Petroleum Products	39	63	88	162	95
Manufactures	2765	2879	3642	4338	5192
Electronics	1056	919	1119	1476	1751
Garments					
Textile	623	751	1098	1317	1575
Footwear	39	31	31	77	96
Trans/Goods & Handbags	10	12	16	22	41
Wood Manufactures	43	49	62	79	88
Furniture-Fixtures	84	89	130	184	204
Chemicals	150	243	245	256	27[illegible]
Non-metallic Mineral	24	18	22	33	45
Machinery & Transport Equipment	30	45	78	54	115
Processed Food & Beverages	106	116	126	184	206
Others	561	562	647	585	705
Special Transactions	12	8	7	27	10
Re-exports	40	112	149	80	71
Total Exports	4629	4842	5720	7574	7821

Source: Central Bank.

Table C-8: IMPORTS BY COMMODITY, 1985-89
($ Million)

	1985	1986	1987	1988	1989
Capital Goods	788	864	1210	1637	2424
Elec. & Non-Elec. Machinery	659	728	988	1279	1852
Power Generators	73	89	63	639	987
Office & EDP Machines	29	32	45	69	104
Telecom Eqpt. Elec. Mach	40	41	41	571	761
Land Transport Eqpt. Exl. Passenger Cars	48	54	116	144	253
Aircraft, Ships & Boats	20	24	33	123	195
Prof. Scientific Instruments	61	59	73	91	124
Raw Matl. & Int. Goods	2198	2671	3426	4415	5388
Wheat	106	129	82	136	197
Crude Mat'ls. Inedible	150	229	290	413	529
Animal & Vegetable Oils & Fats	13	13	13	18	24
Chemicals	584	711	924	1039	1215
Manufactures	508	654	957	1238	1787
Embroideres	196	253	334	377	437
Mat'ls. for Manufacture of Elec. Eqp't.	585	640	767	910	885
Iron Ore, not Agglomerated	56	42	59	43	56
Others	0	0	0	241	258
Mineral Fuels & Lubricant	1452	869	1249	1096	1397
Consumer Goods	441	398	547	597	898
Food & Live Animals	320	271	368	379	492
Beverage & Tobacco	76	72	107	22	29
Others	45	55	72		
Special Transactions	232	242	305	414	812
TOTAL IMPORTS	5111	5044	6737	8159	10419

Source: Central Bank

Table C.4: MEDIUM AND LONG-TERM LOANS
(In Million US$)

ITEM	1983 1/	1984	1985	1986	1987	1988	1989 2/
Inflow	2336	1259	3962	2605	2598	2412	2611
Multilateral	775	471	283	348	396	423	665
Pipeline	622	223	109	294	227	166	196
New Money	153	248	174	54	169	257	469
Bilateral	328	516	1093	943	1385	1140	1262
Pipeline	328	178	208	372	189	59	53
New Money		338	225	192	413	456	592
Rescheduling 3/			660	379	733	625	617
Commercial Banks 4/	1083	151	2545	1256	857	827	769
Pipeline	1083	151	0	525		28	
New Money		0	400				
Rescheduling			2145 5/	731	857	799	769
Others	150	121	41	58	10	22	115
Pipeline	150	119		38	10	22	12
New Money		2					16
Rescheduling			41	20			
Others							87
Outflow	944	781	1173	1873	2439	2931	2432
Multilateral	95	129	114	225	254	364	352
Bilateral	79	65	602	618	765	574	545
Commercial Banks	560	294	407	742	1158	1663	1342
Others	210	293	52	288	262	330	193

1/ Data for 1983-1985 are adjusted for arrears per official concept.
2/ Preliminary.
3/ Refers to Paris Club rescheduling.
4/ Includes financial institutional and for period 1980 to 1982, includes suppliers credits. In 1983 onwards, suppliers credits are lodged under others.
5/ Includes the rescheduling of BB (monetary) and KBS (monetary with hold-outs) liabilities as well as arrears as of 12/31/84.

TABLE C.5: NET INTERNATIONAL RESERVES a/
(Million U.S. Dollars At End of Year)

Year	Gross Reserves		Foreign Exchange Liabilities		Net International Reserves d/ (NIR)	Changes in N I R
	Central Bank	Commercial Bank b/	Central Bank c/	Commercial Bank		
1980	3155	1904	2183	3687	-811	-372
1981 e/	2574	2297	2523	4410	-2062	-1251
1982	1711	2540	3114	4870	-3733	-1671
1983	865	1655	2690	4526	-4696	-963
1984	886	1837	2696	4277	-4250	446
1985	1061	1915	2897	3338	-3259	991
1986	2459	1986	3373	3089	-2017	1242
1987	1959	2464	2685	3491	-1753	264

a/ Revalued, excludes adjustments for non-monetary arrears computed per NIR definition under the 1985 IMF Standby Agreement.
b/ Net of dollar treasury bills held by KBS
c/ The net international reserves for 1970-81. The CB liabilities are already net of certain long-term yen liabilities (IBRD), rural credit liabilities, long-term yen liabilities to OECF agreed with the IMF. The NIR for 1982 to 1983 uses the new concept of NIR computation under the 1983 IMF Standby Agreement where only short-term and IMF credits are included as CB liabilities. Thus, due to the difference in concepts used, the change in net reserves for 1981 and 1982 will not be equal to the the BOP in Table 3.1.
d/ Beginning in 1976 when an understanding was reached with IMF in connection with the Extended Fund Facility, change in net reserves equals overall balance in balance of payments statement (Table 3.1).
e/ SBV adjustments are reflected from 1981 onwards.

Source: Treasury and Foreign Exchange Department, Central Bank of the Philippines

TABLE C-6: AVERAGE NOMINAL TARIFF RATES
1985 - 1989

Sector	Weighted Average 1985	Weighted Average 1988	Unweighted Average 1985	Unweighted Average 1989*
Agriculture	26.9	12.6	27.3	27.0
Mining	10.5	10.3	13.1	12.9
Manufacturing	21.3	22.2	28.0	28.0
Food Beverage Tobacco	21.3	30.4	34.8	36.1
Textiles	30.7	30.6	39.3	39.4
Wood and Products	36.5	37.8	34.9	34.9
Paper and Printing	31.9	27.9	30.2	30.9
Chemicals Petr. Coal	17.9	19.2	20.5	20.2
Non Metallix Mineral	19.5	25.4	33.6	33.0
Basic Metal Industry	13.0	13.8	15.8	16.6
Machinery Metal	22.0	22.6	25.0	24.5
Other Manufacturing	35.2	34.4	36.3	36.3
Overall Average	18.3	19.5	27.6	27.6

*Provisional data.

Source: Tariff Commission.

TABLE C.7
COMMODITIES LIBERALIZED UNDER THE IMPORT LIBERALIZATION PROGRAM (PHASE I & II)
1985-1990
(FOB VALUE IN MILLION US$)

	1985	1986	1987	1988	1989
I. Total Imports	5111	5044	6737	8159	10419
II. Liberalized Commodities					
A. Phase I					
Total, commodities liberalized					
In 1986, 1987 & 1988 (1229 Items)	696	777	1148	1417	1912
Capital Goods (4 items)	0	0	0	0	0
Raw Materials (789 Items)	562	739	1098	1315	1794
Consumer Goods (436 Items)	134	38	50	102	118
B. Phase II					
Total, commodities liberalized under					
Phase II (1988 & 1989) as of Dec. 1989					
(226 Items)	116	133	187	285	403
	---	---	---	---	----
Capital goods (180 Items)	114	128	173	270	377
Raw materials (17 Items)	0	1	8	5	14
Mineral fuels (2 Items)	0	0	0	0	0
Consumer goods (25 Items)	2	4	6	10	12
SPL.Transactions (2 Items)	0	0	0	0	0
C. Total, Phase I & Phase II					
(as of Dec. 1989, 1455 Items)	812	910	1330	1702	2315
	====	====	=====	=====	=====
Capital goods (184 Items)	114	128	173	270	377
Raw material (806 Items)	562	740	1101	1320	1808
Mineral fuels (2 Items)	0	0	0	0	0
Consumer goods (461 Items)	136	42	56	112	130
SPL. Transactions (2 items)	0	0	0	0	0
MEMO ITEMS:					
IMPORTS BY BROAD ECONOMIC CATEGORIES					
A. Capital goods	769	889	1164	1687	2424
B. Raw materials	2338	2321	3628	4415	5388
C. Mineral fuels	1452	869	1249	1096	1397
D. Consumer goods	320	273	391	597	898
E. Special transactions	232	242	305	414	312
TOTAL IMPORTS	5111	5044	6737	8159	10419
	====	====	====	====	=====

1/ Phase I includes commodities liberalized under circular 1100 through circular 1174 covering the period April 1986-April 1988.
Phase II includes commodities liberalized under circular 1192 through circular 1219 covering the period December 1988-December 1989.

0 Means there were no importations, or that these were less than $1 million.

Source: Central Bank

TABLE C.8
COMMODITIES LIBERALIZED UNDER THE IMPORT LIBERALIZATION PROGRAM (PHASE I & II)
1986-1990
(PERCENTAGE POINT CONTRIBUTION TO IMPORT GROWTH)

	1986	1987	1988	1989
I. Total Imports	-1.31	33.56	21.11	27.70
II. Liberalized Commodities				
A. Phase I				
Total, commodities liberalized				
In 1986, 1987 & 1988 (1229 Items)	1.58	7.26	4.07	6.07
Capital Goods (4 items)	0.00	0.00	0.00	0.00
Raw Materials (789 Items)	3.46	7.02	3.30	5.87
Consumer Goods (436 Items)	-1.88	0.24	0.77	0.20
B. Phase II				
Total, commodities liberalized under				
Phase II (1988 & 1989) as of Dec. 1989				
(226 Items)	0.33	1.07	1.45	1.45
Capital goods (180 Items)	0.27	0.89	1.44	1.31
Raw materials (17 Items)	0.02	0.14	-0.04	0.11
Mineral fuels (2 Items)	0.00	0.00	0.00	0.00
Consumer goods (25 Items)	0.04	0.04	0.06	0.02
SPL.Transactions (2 Items)	0.00	0.00	0.00	0.00
C. Total, Phase I & Phase II				
(as of Dec. 1989, 1455 Items)	1.92	8.33	5.52	7.51
Capital goods (184 Items)	0.27	0.89	1.44	1.31
Raw material (806 Items)	3.48	7.16	3.25	5.98
Mineral fuels (2 Items)	0.00	0.00	0.00	0.00
Consumer goods (461 Items)	-1.84	0.28	0.83	0.22
SPL. Transactions (2 items)	0.00	0.00	0.00	0.00
MEMO ITEMS:				
IMPORTS BY BROAD ECONOMIC CATEGORIES				
A. Capital goods	1.37	6.44	7.02	9.65
B. Raw materials	9.45	16.00	11.68	11.98
C. Mineral fuels	-11.41	7.53	-2.27	3.69
D. Consumer goods	-0.92	2.34	3.06	3.69
E. Special transactions	0.20	1.25	1.63	-1.25
TOTAL IMPORTS	-1.31	33.56	21.11	27.70

1/ Phase I includes commodities liberalized under circular 1100 through circular 1174 covering the period April 1986-April 1988.
Phase II includes commodities liberalized under circular 1192 through circular 1219 covering the period December 1988-December 1989.

0 Means there were no importations, or that these were less than $1 million.

Source: Central Bank

Table D1: NUMBER OF PAID EMPLOYEES AND AVERAGE COMPENSATION AND EARNINGS PER MONTH OF PAID EMPLOYEES, PHILIPPINES: 1985
(Data for establishments employing ten or more workers)

PSIC	Paid Employer	Monthly Average Compensation/Employee (₱)	Monthly Average Earnings/Employee (₱)
2	55,042	2,175	2,063
3	618,335	2,067	1,951
311-312	125,783	1,994	1,876
313	27,836	2,591	2,470
314	14,756	2,256	2,047
321	63,251	1,556	1,445
322	85,595	1,732	1,618
323	2,185	1,215	1,143
324	8,732	1,301	1,232
331	45,641	1,545	1,470
332	19,585	1,230	1,181
341	10,356	2,239	2,135
342	14,191	1,909	1,819
351	8,835	3,079	2,837
352	23,706	4,518	4,260
353	2,326	9,042	8,640
354	371	1,728	1,657
355	17,884	2,059	1,973
356	10,556	1,731	1,637
361	2,819	1,917	1,790
362	5,057	3,208	3,068
363	5,863	2,767	2,661
369	7,306	1,610	1,510
371	14,992	2,283	2,206
372	3,309	2,494	2,349
381	14,459	2,092	1,967
382	13,358	1,845	1,767
383	37,575	2,790	2,588
384	12,137	2,131	2,003
385	3,872	1,593	1,476
386	583	1,281	1,223
390	15,416	1,553	1,484
4	47,609	3,951	3,435
5	69,834	2,212	2,066
6	147,531	2,272	2,165
7	109,001	2,686	2,465
8	163,013	3,142	2,968
9	328,322	1,685	1,547

Sources: Annual Survey of Establishments, National Statistics Office.

Table D2: NUMBER OF PAID EMPLOYEES AND AVERAGE COMPENSATION PER MONTH OF PAID EMPLOYEES BY SECTOR, PHILIPPINES: 1986-1989
(Data for establishments employing ten and more workers)

Industry	1986		1987		1988		1989	
	Paid Employees	Monthly Ave. Compensation Per Employees (₱)	Paid Employees	Monthly Ave. Compensation Per Employees (₱)	Paid Employees	Monthly Ave. Compensation Per Employees (₱)	Paid Employees	Monthly Ave. Compensation Per Employees (₱)
MINING AND QUARRYING	52,184	2,487	51,790	3,006	48,107	3,255	47,217	3,598
MANUFACTURING	630,996	2,319	671,051	2,713	802,865	3,077	845,404	3,548
Food	120,791	2,347	131,056	2,813	151,920	3,905	166,284	4,084
Beverage	26,693	3,102	27,250	4,052	34,921	3,805	36,512	4,220
Tobacco	12,330	2,220	12,964	2,503	13,323	2,792	13,438	2,594
Textiles	70,565	1,736	76,757	1,987	98,756	1,893	100,237	2,113
Wearing apparel except footwear	91,375	1,882	101,242	2,056	136,980	2,308	141,607	3,561
Leather & leather products, leather substitutes, fur except footwear & wearing apparel	2,166	1,222	2,886	1,337	3,697	1,400	4,139	1,354
Leather footwear	8,352	1,369	6,365	1,500	8,154	1,571	9,129	1,519
Wood & wood, cork prods. except furn.	44,440	1,606	44,634	1,947	47,200	2,527	47,241	2,166
Furn. & fix except prim'ly of metal	21,598	1,336	26,836	1,529	32,603	1,606	33,827	1,822
Paper & Paper Products	11,460	2,355	11,688	2,643	12,381	3,772	13,071	4,580
Printing, publishing and allied industries	16,218	2,257	16,688	2,567	18,919	1,902	19,026	2,307
Industrial chemicals	8,795	3,297	9,080	4,638	9,665	6,326	9,934	6,747
Other chemicals	24,600	5,463	24,688	6,318	26,276	8,617	27,006	9,191
Petroleum refineries	2,351	14,517	2,451	14,716	2,590	17,296	2,624	18,367
Misc. prods. of petr. and coal	395	2,358	396	2,630	418	3,091	424	3,282
Rubber products	18,512	2,264	22,685	2,457	26,131	2,955	26,938	3,260
Plastic products	12,126	1,809	13,431	2,167	14,296	2,956	14,694	3,152
Pottery china & earthware	2,880	2,097	3,590	2,332	4,416	3,040	4,897	3,454
Glass & glass products	14,628	3,665	5,116	4,691	6,293	6,115	6,979	6,948
Manufacture of cement	6,018	2,821	4,817	4,358	5,925	5,681	6,572	6,455
Other non-metalic mineral products	7,474	1,587	7,640	1,963	9,398	2,564	10,422	2,914
Iron & steel basic metal industries	15,365	2,774	14,378	3,370	16,099	3,646	16,766	4,266
Non-ferrous metal basic industries	2,889	2,907	2,567	3,864	2,761	4,532	2,795	5,127
Fabricated metal products except machinery equipment furnitures and fixtures primarily of metal	16,533	1,871	18,112	2,151	19,383	2,576	22,169	2,560
Machinery except electrical	12,352	1,938	12,380	2,308	13,495	2,733	14,915	2,730
Elec. machin. apparatus appliance, etc.	40.052	2,869	43,407	3,432	53,651	3,521	57,684	5,719
Transport equipment	11,317	2,363	11,485	2,808	15,716	2,858	17,461	3,592
Prof. scient'c measuring & controlling equipment n.e.c. & photographic & opti inst	3,39[illegible]	2,317	3,172	2,088	3,371	2,322	3,586	1,976
Manufacture & repair of furnitures & fixtures primarily of metals	616	1,505	685	1,581	728	1,758	774	1,496
Other manufacturing industries	14,406	1,803	12,607	2,368	13,399	2,633	14,253	2,241
ELECTRICITY, GAS & WATER	52,919	4,216	52,126	4,996	55,201	7,205	60,023	7,455
CONSTRUCTION	58,443	1,994	70,429	2,075	72,070	2,322	73,338	2,411
WHOLESALE & RETAIL TRADE	140,213	2,349	140,799	2,636	132,816	3,029	134,322	3,258
TRANSPORTATION, STORAGE & COMMUNICATION	118,515	3,083	120,807	4,092	124,443	4,866	126,146	5,646
FINANCING, INSURANCE, REAL ESTATE & BUSINESS SERV.	174,022	3,768	179,041	3,958	184,162	4,706	191,753	5,037
COMMUNITY, SOCIAL AND PERSONAL SERVICE	338,943	1,974	356,835	2,231	374,890	2,524	385,953	2,759

Sources: Annual Survey of Establishments (1985-87) and DOLE's Estimates based on the Quarterly Survey of Establishments, National Statistics Off[illegible] (1988-89).

Table D3: PHILIPPINES: LEGISLATED MONEY AND REAL WAGES, 1975-1989)
(Pesos per Day)

	Non-Agricultural Sector				Agricultural Sector			
	Metro LW	Manila RW	Outside LW	MM RW	Metro LW	Manila RW	Outside LW	MM RW
1975	10.65	12.94	10.65	13.90	7.13	9.31	7.13	9.31
1976	12.09	13.94	11.37	13.42	8.75	4.7[illegible]	8.03	9.48
1977	14.40	15.40	13.32	14.28	11.15	11.95	10.07	10.79
1978	15.74	15.74	14.65	14.65	12.48	12.48	11.40	11.40
1979	20.48	17.17	19.40	16.55	16.63	14.19	14.16	12.08
1980	27.39	19.36	26.30	19.00	22.68	16.49	17.03	12.30
1981	31.37	19.77	30.29	19.32	25.85	16.49	19.43	12.39
1982	31.82	18.06	30.74	17.81	26.18	15.17	19.65	11.38
1983	34.22	17.52	33.14	17.48	27.97	14.75	20.95	11.05
1984	48.47	16.63	47.38	16.60	39.66	13.90	29.92	10.48
1985	57.08	16.22	56.00	15.87	46.67	13.23	35.67	10.11
1986	57.08	15.41	56.00	15.90	46.67	13.25	35.47	10.12
1987	58.27	14.73	57.24	15.74	47.67	13.11	36.49	10.04
1988	69.33	16.81	69.33	18.42	58.80	15.55	47.12	12.52
1989	94.33	21.21	94.33	21.21				

Notes: LW = Legislated wage. RW = Real wage. Legislated money wage is the total of minimum wage, cost of living allowances and 13th month pay. The 1989 figures are not fully consistent with those in Table A4 due to discrepancies in the original sources.

Source: Edna A. Reyes and Ma. Teresa C. Sanchez: An Assessment of Labor and Employment Policies in the Philippines, 1986-88, Manila: PIDS Working Paper No. 90-01, pp. 22-23.

Table D4: PHILIPPINES: LEGISLATED DAILY WAGE RATES
(In Pesos per Day)

Indicators	1987	1988	1989							
			Average	1st Sem.	July	August	Sept.	Oct.	Nov.	Dec.
IN NOMINAL TERMS										
Non-Agricultural										
NCR	58.27	69.33	82.88	69.33	96.42	96.42	96.42	96.42	96.42	96.42
Basic Minimum Wage	45.48	64.00	76.50	64.00	89.00	89.00	89.00	89.00	89.00	89.00
COLA	9.00	-	-	-	-	-	-	-	-	-
13th Month Pay	3.79	5.33	6.38	5.33	7.42	7.42	7.42	7.42	7.42	7.42
ONCR	57.24	69.33	82.88	69.33	96.42	96.42	96.42	96.42	96.42	96.42
Basic Minimum Wage	44.53	64.00	76.50	64.00	89.00	89.00	89.00	89.00	89.00	89.00
COLA	9.00	-	-	-	-	-	-	-	-	-
13th Month Pay	3.71	5.33	6.38	5.33	7.42	7.42	7.42	7.42	7.42	7.42
Agricultural										
Plantation	47.67	58.50	72.04	58.50	85.58	85.58	85.58	85.58	85.58	85.58
Basic Minimum Wage	38.19	54.00	66.50	54.00	79.00	79.00	79.00	79.00	79.00	79.00
COLA	6.29	-	-	-	-	-	-	-	-	-
13th Month Pay	3.19	4.50	5.54	4.50	6.58	6.58	6.58	6.58	6.58	6.58
Non-Plantation	36.49	47.12	55.25	47.12	63.38	63.38	63.38	63.38	63.38	63.38
Basic Minimum Wage	30.03	43.50	51.00	43.50	58.50	58.50	58.50	58.50	58.50	58.50
COLA	3.96	-	-	-	-	-	-	-	-	-
13th Month Pay	2.50	3.62	4.25	3.62	4.88	4.88	4.88	4.88	4.88	4.88
IN REAL TERMS (at 1978 Prices)										
Non-Agricultural										
NCR	14.73	15.93	17.37	14.99	20.18	19.90	19.77	19.54	19.36	18.97
ONCR	15.74	17.58	18.97	16.44	22.00	21.63	21.46	21.27	21.03	20.56
Agricultural										
Plantation	13.11	14.84	16.49	13.88	19.52	19.20	19.04	18.88	18.67	18.25
Non-plantation	10.04	11.95	12.64	11.18	14.46	14.22	14.10	13.98	13.82	13.51

Sources: National Wages Council and Bureau of Labor and Employment Statistics.

Table D5: PHILIPPINES: DAILY REAL WAGES OF SELECTED OCCUPATIONS IN THE NON-AGRICULTURAL PRIVATE SECTOR

Area/Occupation	1985	1986	1987	1988	1989
Philippines	23.40	24.59	25.77	27.52	
Carpenter	22.04	22.17	21.60	22.77	
Cashier I	33.34	36.25	36.57	38.56	
Clerk-Typist	26.04	27.59	30.16	29.94	
Driver	21.48	23.69	25.06	27.03	
Electrician	22.70	24.79	25.63	28.50	
Janitor	20.99	21.82	22.96	23.96	
Laborer	20.59	20.47	22.27	23.93	
Mechanic I	23.20	24.66	26.20	28.97	
Messenger	23.67	25.72	26.72	28.71	
Plumber	21.23	21.82	22.39	23.62	
Secretary	29.42	30.98	34.24	36.45	
Telephone Operator	23.33	24.93	27.26	28.32	
NCR	26.20	26.32	26.61	28.20	
Carpenter	21.38	21.27	20.73	20.99	
Cashier I	40.48	42.19	40.87	44.90	
Clerk-Typist	30.55	30.51	33.27	32.05	
Driver	23.87	23.72	24.12	24.62	
Electrician	23.20	23.24	24.05	25.37	
Janitor	21.40	21.47	21.97	22.30	
Laborer	21.09	20.67	21.00	21.81	
Mechanic I	23.63	22.98	23.63	26.88	
Messenger	25.65	26.90	26.42	29.43	
Plumber	22.04	25.75	20.22	22.47	
Secretary	32.69	32.83	35.06	37.34	
Telephone Operator	26.36	26.64	28.95	31.97	
Outside NCR	22.20	23.60	24.75	27.47	
Carpenter	22.00	22.38	21.77	23.73	
Cashier I	29.15	31.98	32.71	34.48	
Clerk-Typist	21.53	23.56	24.92	26.91	
Driver	20.70	23.57	25.14	28.36	
Electrician	22.40	25.40	25.88	30.71	
Janitor	20.80	21.72	22.98	25.05	
Laborer	20.47	20.38	22.51	25.05	
Mechanic I	22.99	25.29	27.04	30.33	
Messenger	22.23	24.21	25.85	27.87	
Plumber	20.84	21.64	22.99	24.42	
Secretary	26.20	27.96	31.27	35.06	
Telephone Operator	21.42	23.33	25.10	25.70	

Note: Daily real wages were computed by dividing the monthly real wages by 20 for a five-day week work schedule.

Source: As in Table D4.

Table D6: PHILIPPINES: AVERAGE HOURS ACTUALLY WORKED PER WEEK OF PRODUCTION WORKERS IN THE INDUSTRY SECTOR BY MAJOR INDUSTRY GROUP SECOND QUARTER 1989
(Data for establishments with ten or more workers)

PSIC	Production Workers /a	Total Hours Actually worked	Average Hours Worked Per Week
2	52,070	29,471,620	43.5
3	776,274	479,967,244	47.6
311-312	141,621	93,522,281	50.8
313	5,382	4,133,376	59.1
314	11,358	7,144,182	48.4
321	81,410	55,277,390	52.2
322	183,892	93,968,812	39.3
323	17,954	3,913,972	16.8
324	9,981	5,419,683	41.8
331	38,359	27,081,454	54.3
332	36,712	23,715,952	49.7
341	11,178	7,209,810	49.6
342	14,425	10,833,175	57.8
351	5,402	3,419,466	48.7
352	18,488	12,072,664	50.2
353	1,701	/b	-
354	75	61,650	63.2
355	29,259	13,195,809	34.7
356	12,360	9,381,240	58.4
361	3,912	2,601,480	51.2
362	4,091	3,796,448	71.4
363	3,390	2,756,070	62.5
369	8,805	5,177,340	45.2
371	16,971	13,339,206	60.5
372	2,743	1,665,001	46.7
381	21,147	15,987,132	58.2
382	14,556	9,970,860	52.7
383	44,300	30,522,700	53.0
384	11,938	7,031,482	45.3
385	2,449	1,444,910	45.4
386	728	468,104	49.5
390	21,687	14,855,595	52.7
4	20,109	12,085,509	46.2
5	84,852	61,772,256	56.0

P = Preliminary.

/a Not comparable with "paid employees", which includes category other than production workers.
/b No data available.

Sources: Employment, Hours and Earnings Survey. Bureau of Labor and Employment Statistics.

Table D7: PHILIPPINES: SECTORAL DISTRIBUTION OF EMPLOYMENT, THIRD QUARTER 1970-1989
(in thousands)

	1970	1975	1980/a	1985/a	1986/a	1987	1988	1989
Agriculture	6,100	7,768	8,453	9,698	10,289	9,940	9,920	9,854
Forestry, Hunting & Fishing	(53.7)	(53.5)	(51.4)	(49.0)	(50.0)	(47.8)	(46.1)	(45.1)
Industry	1,876	2,207	2,554	2,812	2,746	3,045	3,348	3,452
	(16.5)	(15.2)	(15.5)	(14.2)	(13.3)	(14.6)	(15.6)	(15.8)
Mining & Quarrying	51	54	94	128	150	146	157	153
	(0.4)	(0.4)	(0.6)	(0.6)	(0.7)	(0.7)	(0.7)	(0.7)
Manufacturing	1,354	1,651	1,814	1,922	1,905	2,059	2,238	2,294
	(11.9)	(11.2)	(11.0)	(9.7)	(9.2)	(9.9)	(10.4)	(10.5)
Electricity, Gas Water & Sanitary Services	33	46	59	73	62	81	95	87
	(0.3)	(0.3)	(0.4)	(0.4)	(0.3)	(0.4)	(0.4)	(0.4)
Construction	438	456	588	684	629	759	858	918
	(3.4)	(3.1)	(3.6)	(3.5)	(3.1)	(3.6)	(4.0)	(4.2)
Services	3,198	4,504	5,421	7,292	7,561	7,810	8,227	8,543
	(28.2)	(31.0)	(33.0)	(36.8)	(36.7)	(37.6)	(38.3)	(39.1)
Wholesale & Retail Trade			1,660	2,611	2,814	2,857	2,972	3,081
			(10.1)	(13.2)	(13.7)	(13.7)	(13.8)	(14.2)
Transport, Storage & Communication			732	931	841	946	1,049	1,092
			(4.5)	(4.7)	(4.1)	(4.6)	(4.9)	(5.0)
Financing, Insurance, Real Estate & Business Services			336	342	390	386	379	393
			(2.0)	(1.7)	(1.9)	(1.9)	(1.8)	(1.8)
Community, Social & Personal Services			2,693	3,408	3,516	3,621	3,827	3,977
			(16.4)	(17.2)	(17.1)	(17.4)	(17.8)	(18.2)
Total Employed	11,358	14,518	16,434	19,801	20,595	20,795	21,497	21,849
Total Unemployed /b	942	643	1,368	2,320	2,400	2,085	1,954	2,009
Unemployment /b (%)	7.7	4.2	7.9	11.1	11.1	9.1	8.3	8.4

Note: Figures in brackets give percentages. Due to change in definition of service sectors in 1976 no data provided for 1970 and 1975.

/a Data for -1980-86 are based on past quarter reference period, while all other years are based on past week reference period.

/b Unemployment data based on past week reference period.

Source: Gyaberts and T.S. Papola: Employment Promotion in the Philippines: An Overview, Manila; ILO/Japan Project, 1990.

Table D8: PHILIPPINES: NUMBER AND PERCENT DISTRIBUTION OF ACTUAL STRIKES/LOCKOUTS DECLARED, WORKERS INVOLVED AND MAN-DAYS LOST BY MAJOR INDUSTRY GROUP, 1969

Major Industry Groups	Actual Strikes/Lockouts Declared		Workers Involved		Man-Days Lost (000)	
	Number	Percent	Number	Percent	Number	Percent
ALL INDUSTRIES	197	100.0	58,541	100.0	955	100.0
Agriculture, fishery and forestry	8	4.1	1,642	2.9	16	1.7
Mining and Quarrying	5	2.5	9,789	17.3	64	6.7
Manufacturing	112	56.9	24,440	43.2	604	63.2
Electricity, gas & water	13	6.6	2,300	4.1	14	1.5
Construction	1	0.5	200	0.4	1	0.1
Wholesale & retail trade	8	4.1	1,278	2.3	84	8.8
Transportation, storage and communication	12	6.1	8,628	15.3	62	6.5
Financing, insurance, real estate and business services	9	4.6	2,255	4.0	28	2.9
Community, social and personal services	29	14.7	6,009	10.6	82	8.6

Source: National Conciliation and Mediation Board.

Table D9: PHILIPPINES: NUMBER AND PERCENT DISTRIBUTION OF ACTUAL STRIKES/LOCKOUTS DECLARED, WORKERS INVOLVED AND MAN-DAYS LOST BY MAJOR INDUSTRY GROUP, 1986-88

Major Industry Groups	Actual Strikes/Lockouts Declared		Workers Involved		Man-Days Lost (000)	
	Number	Percent	Number	Percent	Number	Percent
1986						
ALL INDUSTRIES	581	100.0	169,479	100.0	3,638	100.0
Agriculture, fishery and forestry	20	3.4	5,241	3.1	62	1.7
Mining and Quarrying	9	1.5	7,030	4.2	186	5.1
Manufacturing	366	63.0	87,869	51.8	2,531	69.6
Electricity, gas & water	5	0.9	160	0.1	11	0.3
Construction	6	1.0	419	0.2	23	0.6
Wholesale & retail trade	53	9.1	7,230	4.3	160	4.4
Transp., storage & communic.	52	9.0	32,091	18.9	362	10.0
Financing, insurance, real estate and business services	11	1.9	1,168	0.7	25	0.7
Community, social & pers. serv.	59	10.2	28,271	16.7	278	7.6
1987						
ALL INDUSTRIES	438	100.0	89,574	100.0	1,908	100.0
Agriculture, fishery & forestry	23	5.3	7,085	7.9	178	9.3
Mining and Quarrying	8	1.8	686	0.7	28	1.5
Manufacturing	232	53.2	52,890	59.1	1,254	65.7
Electricity, gas & water	12	2.7	1,778	2.0	21	1.1
Construction	2	0.5	1,200	1.3	27	1.4
Wholesale & retail trade	43	9.9	4,077	4.6	120	6.3
Transp., storage & communic.	31	7.1	11,487	12.8	98	5.1
Financing, insurance, real estate and business services	12	2.8	1,541	1.7	24	1.3
Community, social & pers. serv.	73	16.7	8,884	9.9	158	8.3
1988						
ALL INDUSTRIES	267	100.0	75,848	100.0	1,525	100.0
Agriculture, fishery & forestry	14	5.2	3,536	4.7	103	6.8
Mining and Quarrying	2	0.7	1,470	1.9	6	0.4
Manufacturing	131	49.1	42,351	55.8	1,030	67.5
Electricity, gas & water	15	5.6	2,259	3.0	11	0.7
Construction	3	1.1	172	0.2	4	0.3
Wholesale & retail trade	24	9.0	4,354	5.7	85	5.6
Transp., storage & communic.	22	8.2	9,620	12.7	103	6.8
Financing, insurance, real estate and business services	12	4.5	3,507	4.6	74	4.9
Community, social & pers. serv.	44	16.5	8,579	11.3	108	7.1

Sources: Bureau of Labor and Employment Statistics, National Conciliation and Mediation Board.

Table D10: PHILIPPINES: NUMBER AND PERCENT DISTRIBUTION OF ACTUAL STRIKES/LOCKOUTS DECLARED, WORKERS INVOLVED AND MAN-DAYS LOST BY MAJOR INDUSTRY GROUP, 1990
(As of May 31) /a

Major Industry Groups	Actual Strikes/Lockouts Declared		Workers Involved		Man-Days Lost (000)	
	Number	Percent	Number	Percent	Number	Percent
ALL INDUSTRIES	86	100.0	37,474	100.0	418	100.0
Agriculture, fishery and forestry	12	14.0	2,026	5.4	23	5.6
Mining and Quarrying	1	1.2	1,100	2.9	26	6.3
Manufacturing	54	62.8	28,566	76.2	289	70.0
Electricity, gas & water	2	2.3	360	1.0	2	0.5
Construction	1	1.2	300	0.8	4	1.0
Wholesale & retail trade	4	4.7	1,188	3.2	49	11.9
Transportation, storage and communication	4	4.7	3,348	8.9	8	1.9
Financing, insurance, real estate and business services	3	3.5	240	0.6	4	1.0
Community, social and personal services	5	5.8	356	0.9	8	1.9

/a Preliminary.

Source: National Conciliation and Mediation Board.

Table D11: PHILIPPINES: ESTABLISHMENTS WITH VIOLATIONS ON MINIMUM WAGE AS PERCENT OF INSPECTED BY REGION, 1986-89

Region	1986		1987		1988		1989	
	Establishments Inspected	Percent Violating (%)	Establishments Inspected	Percent Violating (%)	Establishments Inspected	Percent Violating (%)	Establishments Inspected	Percent Violating (%)
All Regions	1,441	6.3	12,044	13.7	12,988	21.9	27,219	25.9
NCR	948	1.5	2,390	10.7	3,142	9.5	6,039	13.8
CAR	/a	/a	/a	/a	/a	/a	409	38.0
I	42	2.4	2,644	10.6	3.18	44.7	1,978	38.5
II	0	0.0	869	1.8	707	26.0	1,768	23.2
III	0	0.0	769	3.6	1,331	2.7	2,490	15.3
IV	224	18.3	1,858	20.8	842	34.2	2,229	35.1
V	28	/b	790	22.8	1,217	27.6	1,306	26.0
VI	31	/b	643	2.0	857	22.1	2,016	42.3
VII	41	43.9	70	54.3	272	21.7	1,160	13.5
VIII	8	/b	635	19.1	767	16.0	1,307	22.7
IX	30	26.7	410	19.0	730	13.0	1,474	13.2
X	43	2.3	277	10.1	139	2.9	1,972	24.9
XI	32	3.1	443	35.0	2,275	38.0	2,318	43.6
XII	16	18.7	246	27.2	386	55.7	763	34.5

/a No data available.

/b No data reported.

Sources: Bureau of Working Conditions and Bureau of Labor and Employment Statistics.

Table D12: PHILIPPINES: ESTABLISHMENTS WITH VIOLATIONS ON MINIMUM WAGE AS PERCENT OF INSPECTED BY MAJOR INDUSTRY GROUP, 1989 /a

Major Industry Group	Establishment Inspected	Percent Violating (%)
All Industries	27,219	25.9
Agricultural, Fishery and Forestry	1,307	28.6
Mining and Quarrying	54	40.0
Manufacturing /b	6,968	28.2
Electricity, Gas and Water	109	48.1
Construction	354	25.5
Wholesale and retail trade	11,486	27.5
Transportation, Storage and Communication	517	25.0
Financing, Insurance, Real Estate and Business Services	1,552	24.2
Community, Social and Personal Services	4,872	33.7

/a Data for previous years and cross-tabulation by region and major industry group not available.

/b Data by detailed groupings not available.

Sources: Bureau of Working Conditions and Bureau of Labor and Employment Statistics.

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PHILIPPINES

CLASSIFICATION OF PROVINCES BY GEOGRAPHICAL REGIONS

I ILOCOS
- 1 Ilocos Norte
- 2 Ilocos Sur
- 3 La Union
- 4 Pangasinan

CORDILLERA ADMINISTRATIVE REGION (CAR)
- 5 Abra
- 6 Kalinga-Apayao
- 7 Mountain Province
- 8 Ifugao
- 9 Benguet

II CAGAYAN VALLEY
- 10 Batanes
- 11 Cagayan
- 12 Isabela
- 13 Nueva Vizcaya
- 14 Quirino

III CENTRAL LUZON
- 15 Nueva Ecija
- 16 Tarlac
- 17 Zambalares
- 18 Pampanga
- 19 Bataan
- 20 Bulacan

NATIONAL CAPITAL REGION (NCR)

IV SOUTHERN TAGALOG
- 21 Aurora
- 22 Quezon
- 23 Rizal
- 24 Cavite
- 25 Laguna
- 26 Batangas
- 27 Marinduque
- 28 Mindoro Oriental
- 29 Mindoro Occidental
- 30 Rombion
- 31 Palawan

V BICOL
- 32 Camarines Norte
- 33 Camarines Sur
- 34 Cantanduanes
- 35 Albay
- 36 Sorsogon
- 37 Masbate

VI WESTERN VISAYAS
- 38 Aklan
- 39 Capiz
- 40 Antique
- 41 Iloilo
- 42 Negros Occidental
- 43 Guimaras

VII CENTRAL VISAYAS
- 44 Cebu
- 45 Negros Oriental
- 46 Bohol
- 47 Siquijor

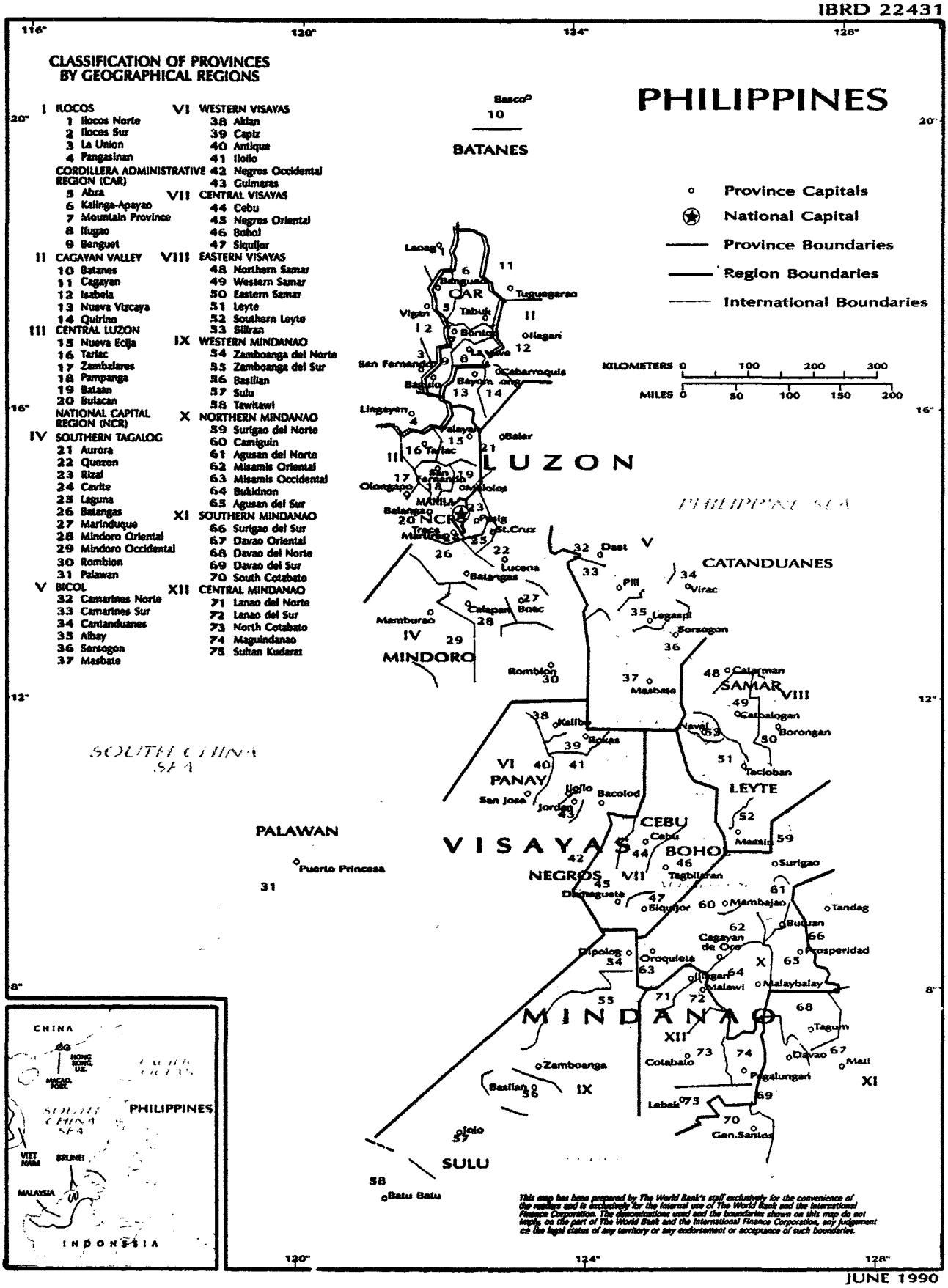
VIII EASTERN VISAYAS
- 48 Northern Samar
- 49 Western Samar
- 50 Eastern Samar
- 51 Leyte
- 52 Southern Leyte
- 53 Biliran

IX WESTERN MINDANAO
- 54 Zamboanga del Norte
- 55 Zamboanga del Sur
- 56 Basilian
- 57 Sulu
- 58 Tawitawi

X NORTHERN MINDANAO
- 59 Surigao del Norte
- 60 Camiguin
- 61 Agusan del Norte
- 62 Misamis Oriental
- 63 Misamis Occidental
- 64 Bukidnon
- 65 Agusan del Sur

XI SOUTHERN MINDANAO
- 66 Surigao del Sur
- 67 Davao Oriental
- 68 Davao del Norte
- 69 Davao del Sur
- 70 South Cotabato

XII CENTRAL MINDANAO
- 71 Lanao del Norte
- 72 Lanao del Sur
- 73 North Cotabato
- 74 Maguindanao
- 75 Sultan Kudarat



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JUNE 1990

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