A WORKING PAPER ON

RURAL GROWTH AND DEVELOPMENT REVISITED

Summary Report

The World Bank Group in the Philippines
Supporting Islands of Good Governance
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Summary Report

JUNE 2006

Rural Development and Natural Resources Sector Unit
East Asia and the Pacific Region

THE WORLD BANK GROUP
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This report is prepared under the overall supervision of Ms. Idah Pswarayi-Riddihough and Ms. Carolina Figueroa-Geron of the Rural Development and Natural Resources Sector Unit. Mr. Ajay Markanday provided significant input to the summary document.

Contributing to the report were Messieurs and Mesdames: Messieurs Rolando Dy (Private Sector Investments); Gilberto Llanto (Rural Finance — subsequently consolidated into sections of Private Investments and Agricultural Policy working papers); Joselito Supangco (Rural Infrastructure); Germelino Bautista (Natural Resource Management); and Gerry Bulatao (Comprehensive Agrarian Reform Program), and Mesdames Dely Pascual-Gapasin (Agricultural Research, Development, and Extension), Ching de la Peña (Agricultural Policy); and Josefina Esguerra (Governance Issues). Copies of their working papers are available from the World Bank Office, Manila and the World Bank website: www.worldbank.org.ph.

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<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>AARNR</td>
<td>Agriculture, Agrarian Reform and Natural Resources</td>
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<tr>
<td>ACEF</td>
<td>Agriculture Competitiveness Enhancement Fund</td>
</tr>
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<td>AE</td>
<td>Allocative Efficiency</td>
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<tr>
<td>AFMA</td>
<td>Agricultural and Fisheries Modernization Act</td>
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<tr>
<td>AFMP</td>
<td>Agriculture and Fisheries Modernization Plan</td>
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<td>AMCFP</td>
<td>Agriculture Modernization Credit Financing Program</td>
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<td>ARB</td>
<td>Agrarian Reform Beneficiary</td>
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<tr>
<td>ARF</td>
<td>Agrarian Reform Fund</td>
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<tr>
<td>BSP</td>
<td>Bangko Sentral ng Pilipinas (Philippine Central Bank)</td>
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<tr>
<td>CARP</td>
<td>Comprehensive Agrarian Reform Program</td>
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<td>CBFMA</td>
<td>Community Based Forest Management Agreements</td>
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<tr>
<td>CO</td>
<td>Capital Outlay</td>
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<tr>
<td>CPSD</td>
<td>Consolidated Public Sector Deficit</td>
</tr>
<tr>
<td>DA</td>
<td>Department of Agriculture</td>
</tr>
<tr>
<td>DAR</td>
<td>Department of Agrarian Reform</td>
</tr>
<tr>
<td>DBCC</td>
<td>Development Budget Coordination Committee</td>
</tr>
<tr>
<td>DBM</td>
<td>Department of Budget Management</td>
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<tr>
<td>DCP</td>
<td>Directed Credit Programs</td>
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<td>DENR</td>
<td>Department of Environment and Natural Resources</td>
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<tr>
<td>DOF</td>
<td>Department of Finance</td>
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<tr>
<td>EIU</td>
<td>Economist Intelligence Unit</td>
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<tr>
<td>ENRM</td>
<td>Environment and Natural Resource Management</td>
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<tr>
<td>FDI</td>
<td>Foreign Direct Investment</td>
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<tr>
<td>FTAA</td>
<td>Financial and Technical Assistance Agreement</td>
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<tr>
<td>GAA</td>
<td>General Appropriations Act</td>
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<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>GFI</td>
<td>Government Financing Institutions</td>
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<td>GOCC</td>
<td>Government-Owned and Controlled Corporations</td>
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<tr>
<td>GOP</td>
<td>Government of the Philippines</td>
</tr>
<tr>
<td>ICC</td>
<td>Investment Coordination Committee</td>
</tr>
<tr>
<td>IPAF</td>
<td>Integrated Protected Areas Fund</td>
</tr>
<tr>
<td>IRA</td>
<td>Internal Revenue Allotment</td>
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<td>LAD</td>
<td>Land Acquisition and Distribution (CARP)</td>
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<td>LBP</td>
<td>Land Bank of the Philippines of the Philippines</td>
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<tr>
<td>LGC</td>
<td>Local Government Code</td>
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<tr>
<td>LGU</td>
<td>Local Government Unit</td>
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<tr>
<td>MFO</td>
<td>Major Final Output</td>
</tr>
<tr>
<td>MOOE</td>
<td>Miscellaneous Operating and Other Expenses</td>
</tr>
<tr>
<td>MPSA</td>
<td>Mineral Production Sharing Agreements</td>
</tr>
<tr>
<td>MTEF</td>
<td>Medium-Term Expenditure Framework</td>
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<td>MTPDP</td>
<td>Medium Term Philippines Development Plan 2004-2010</td>
</tr>
<tr>
<td>MTPIP</td>
<td>Medium Term Philippine Implementation Plan</td>
</tr>
<tr>
<td>NEDA</td>
<td>National Economic Development Authority</td>
</tr>
<tr>
<td>NFA</td>
<td>National Food Administration</td>
</tr>
<tr>
<td>NG</td>
<td>National Government</td>
</tr>
<tr>
<td>NRM</td>
<td>Natural Resource Management</td>
</tr>
<tr>
<td>NSO</td>
<td>National Statistics Office</td>
</tr>
<tr>
<td>ODA</td>
<td>Official Development Assistance</td>
</tr>
<tr>
<td>PAMB</td>
<td>Protected Areas Management Board</td>
</tr>
<tr>
<td>PAP</td>
<td>Programs Activities and Projects</td>
</tr>
<tr>
<td>PIP</td>
<td>Public Investment Plan</td>
</tr>
<tr>
<td>PS</td>
<td>Personnel Service</td>
</tr>
<tr>
<td>R&amp;D</td>
<td>Research and Development</td>
</tr>
<tr>
<td>SEER</td>
<td>Sector Efficiency and Effectiveness Reviews</td>
</tr>
<tr>
<td>VAT</td>
<td>Value Added Tax</td>
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</tbody>
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1. EXECUTIVE SUMMARY

1.1. This summary report integrates the findings and recommendations outlined in the various working papers included in the Rural Growth and Development Revisited Study. It is structured around the framework of drivers and facilitators of, as well as policy and regulatory issues and Medium Term Philippine Development Plan (MTPDP) 2004 – 2010 thrusts in rural growth in the Philippines. In addition, it emphasizes the relative weight of rural sectors in the economy and the importance of effective public sector and expenditure management. It has done so given the intrinsic link and commonality and commorality of issues governing growth in the economy as a whole and in rural areas, and the necessity of Government in setting the macro environment for improving governance, rationalizing the bureaucracy, and improving fiscal and expenditure discipline. The issues raised in this report are central to the debate on sector growth as they determine the direction of the economy (what appears to be working and what not) and the relative success of Government and the public sector in targeting and managing scarce public resources and providing the right signals for stimulating investment and competitiveness, which ultimately determine growth.

1.2. The economy and rural growth are discussed in Section 2, the drivers of economic and rural growth in Section 3, and the facilitators of such growth in Section 4. Governance, policy and regulatory issues are tackled in Section 5, which also outlines the public role in meeting the needs of the private sector in stimulating agribusiness [section 5.3.2].

1.3. Rural growth is intrinsically linked to overall economic performance and the efficiency of Government in managing it through the legislature, policies and resources. A primary driver in economic growth is domestic and foreign investments. However, relative to other regional and world economies, the standing of the Philippines needs to improve considerably in attracting foreign direct investments (FDIs). The chief disincentives to FDIs appear to be political and fiscal instability, perceived poor governance and corruption in public institutions, and ineffective infrastructure, transport and information networks. This does not mean that opportunities do not exist, especially with a rapidly growing regional economy, but that the country needs to address these issues urgently to make full use of its comparative and competitive advantages.

1.4. The economic, social and development cost of not doing so are significant, especially as a low domestic saving rate and a potential fall in remittances, a principal driver of private consumption and the economy, could have serious knock-on consequences. For the same reasons, the domestic private sector remains risk averse in making investments. Additionally there are a number of programs, policies and legislation in agriculture that distort prices, resource allocation and markets, all of which create uncertainties. For example, land distribution under the Comprehensive Agrarian Reform Program (CARP), has not been completed; land markets are distorted by significant weaknesses in property rights, title and ownership, and land cannot be used freely as collateral for accessing credit. These inconsistencies, therefore, undermine land investment, productivity and growth.

1.5. Government efforts at boosting confidence and investments in factors of production need to be strongly supported by the way it manages and allocates public resources. The past five years have witnessed the emergence of significant fiscal imbalances, increased Government borrowing and growing indebtedness. The rise in public debt is particularly worrying as it has reached levels that are deterring public and private investments. Added to this are structural weaknesses in the way public resources and expenditures are allocated and used. Proportionately, very little in public finances actually goes to increasing capital stock, whilst the bulk is spent for keeping the bureaucracy going. To redress this, Government
must steadfastly implement its bureaucratic and public expenditure reform program.

1.6. Moreover, the process of Government planning, budgeting and monitoring is fragmented, with inadequate linkages between priority setting and resource allocation, while a significant portion of public finances (e.g. congressional allocations) are not subject to prioritization, accountability and transparency rigors. Meanwhile, local government units (LGUs) have not been fiscally weaned off national government, more than 10 years after the passage of the Local Government Code (LGC) that provided for, among others, the devolution of substantial responsibilities for service delivery to LGUs. The onus therefore clearly lies on improving fiscal and expenditure discipline by adopting a holistic approach to public planning and investment which is closely aligned to budget realities. In formulating a meaningful public investment plan (PIP), the National Economic and Development Authority (NEDA), Department of Finance (DOF) and Department of Budget and Management (DBM), working closely with Congress, could lead the way by making difficult investment choices. Without this, PIPs at the agency level have limited worth.

1.7. These imbalances and inefficiencies significantly impede agriculture and the rural economy. Despite resource advantages and expanding domestic and international market opportunities, the sector’s importance in the economy is declining as it fails to modernize, diversify and become more productive and competitive. This lack of responsiveness and dynamism in the rural sectors, especially as others in the economy (like telecommunications and electronics) can and are taking off, is at the heart of this study.

1.8. For producers and entrepreneurs to be more responsive, the price and market signals in agriculture have to be consistent, non-distortive and consumer-orientated. Agricultural and food security policies, however, have historically emphasized public investment in commodity and price support programmes, which have shielded producers from being more dynamic and responsive to market needs. To this end, the current MTPDP thrusts on asset reform (e.g. expediting completion of the CARP and the passage of the Farmland Collateral Bill) and focusing policy and public investment on market and agribusiness development are encouraging.

1.9. In contrast to common perceptions, the overall economy is faring reasonably well, registering reasonable growth rates in the last two years. This suggests that some sectors are expanding, though not agriculture, wherein a fall in national income is evident. This need not be the case. Continued growth in private consumption and the service sectors will fuel strong domestic demand for food and agri-products through corresponding growth in sectors such as hotels, restaurants and tourism. The challenge, however, will be how much of the growth in this demand domestic producers will meet and how much will go to outsiders. On the broader front, regional economic expansion, particularly in China, means there are significant opportunities for suppliers of quality products, as long as they remain competitive. From a public expenditure perspective, increasing resources to the market aspects of the Agricultural and Fisheries Modernization Act (AFMA) are likely to have high returns.

1.10. The competitive base of the Philippine rural economy remains hampered by continued lack of investment in good, reliable and reasonably priced transport infrastructure. The roads are not there or are poorly maintained, whilst shipping remains uncompetitive and overpriced due to monopolistic practices. Apart from the direct benefit of linking producers to markets, reliable infrastructure is a critical precursor to investment as confidence grows.

1.11. While economic growth is essential to development, it is not without environment and natural resource repercussions and costs. Recent experience in managing these in the Philippines has been inadequate and if current trends continue there will be few resources to exploit before long and the cost of cleaning up the environment will outweigh the short term benefits. Viewed by this cost/benefit perspective, the proper management of the environment and natural resource is arguably as much a long term driver of economic growth as investment.
2. THE ECONOMY AND RURAL GROWTH

2.1. The economy grew at over 6 percent in 2004, the fastest in 15 years. This was encouraging and is partly attributed to positive external factors in the world economy and to past structural reforms, which have begun integrating significant sectors of the economy to global trade and investment flows, enhanced competition in the private sector, and began transforming the export base from reliance on commodities to value added goods such as electronics. Moreover, entrepreneurial talent and proficiency in English are strongly enhancing competitiveness in sectors such as business outsourcing and telecommunications which further support growth.

2.2. In terms of Gross Domestic Product (GDP) growth, the country has fared reasonably well compared with other regional economies, although the MTPDP growth targets seem somewhat optimistic compared to trend and a (comparative) forecast by the Economist Intelligence Unit (EIU) [Figure 1].

2.3. Although the agricultural sector, including forestry and fisheries, will continue playing a strategic role in the economy and rural growth, its relative share of GDP (around 20 percent) has been declining for years because of the slow rate of output growth [Section 3.5]. In contrast, the relative share of industry and services, which employ far less people than agriculture, will likely increase from the present 33 percent and 48 percent respectively, as they continue registering stronger productivity and growth rates [Figures 2 & 3], in response to demand.

2.4. Agricultural exports have been declining and now account for less than 5 percent of foreign earnings. [Figures 4 & 5, Table 1]. This has been the result of slow agriculture and productivity growth, subsidies, and limited diversification away from staple crops, which are raised almost entirely for the domestic
market. Subsidies and limited diversification have meant that there has been little pressure for producers to innovate or response to price and other signals.

2.5. Private consumption, fuelled by large expatriate remittances, [Figure 6] will remain a principal driver in economic growth in the medium term.

2.6. A related growth driver in both the rural and national economy will be the high level of employment (and hence household income) agriculture provides and the consequent demand this generates for services and consumption [Figure 7].

2.7. To take advantage of the food demand from a rapidly growing population, which more than doubled from 36 million in 1970 to 76 million in 2000, and increased consumption, the sector will have to increase productivity and growth. Achieving this poses considerable challenges as overall crop and factor productivity in the sector is low compared to those of other countries in the region and

<table>
<thead>
<tr>
<th>Table 1. Major Agricultural Exports 2003</th>
<th>Total Export earnings</th>
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<tbody>
<tr>
<td></td>
<td>US $ m</td>
</tr>
<tr>
<td>Coconut oil</td>
<td>5051.4</td>
</tr>
<tr>
<td>Desiccated coconut</td>
<td>96</td>
</tr>
<tr>
<td>Copra</td>
<td>36</td>
</tr>
<tr>
<td>Bananas</td>
<td>333</td>
</tr>
<tr>
<td>Pineapple products</td>
<td>131</td>
</tr>
<tr>
<td>Mangoes</td>
<td>31</td>
</tr>
<tr>
<td>Total inc others</td>
<td>1458</td>
</tr>
</tbody>
</table>

Source: BSP
to the world average [Figure 8 & 9]. Low productivity, moreover, compounds serious underlying problems of a stagnant sector which requires urgent impetus for innovation and diversification.

![Fig. 8: Paddy Yields Mt/ha](source: FAO)

![Fig. 9: Corn Yield MT/ha](source: FAO)

2.8. The Philippines will also need to look at neighbouring economies as sources of further growth. For the country, being home to a large ethnic-Chinese business community has meant that trade relations with China will become increasingly more central to the economy. China and Hong Kong together accounted for almost 15% of Philippine exports in 2004 up from 7% three years ago [Figure 10].

2.9. Rapid GDP and income growth in China and its projected demand for diversified, quality agricultural and fisheries products also mean that its markets will be of considerable strategic (and growth) importance to the Philippine rural economy – providing the latter is suitably geared up and flexible. The government is also targeting China as a critical source of investment capital. This is founded on China’s strong demand for raw materials in the medium term and by the recent opening up of the mining sector to foreign investment2. In April 2005, agreements worth US$1.5bn3 covering loans and investments in railway and mining projects were signed between the two countries. This represents a significant increase in volume of potential investment given recent trends, which have been quite volatile due to uncertainty and changes in the political landscape of the Philippines [Figure 3 & section 3.1]. Clearly, exploiting these types of comparative advantages and historic and indigenous trade linkages in the domestic and regional economy will be important to future growth in the whole economy and key in sectors in rural areas.

2.10. The sectors that are projected to benefit most from this growth are telecoms, health, restaurants, hotels, tourism, leisure and education. The share of these growth markets that domestic producers are able to capture from agriculture and related sectors (i.e. food, beverages and agro-processing)

\[\text{Fig. 10: Major Exports Destination (%)} \text{ Total FOB Value}\]

Source: EIU/BSP

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2 This ruling will open the way for significant outside investment (interest) in the sector, which would be important for growth, it will be equally important that such investments are managed responsibly from an environment and Natural Resource Management (NRM) perspective to ensure that long term costs do not outweigh the short term benefits. [Ref section 3.3]. Australia is also likely to be an important investment source in mining.

will be highly relevant in determining the direction and extent of rural growth.

2.11. In summary, the overall economy appears to be faring well in certain quarters but not so well in others. In the rural/agricultural economy there will be a number of factors that will influence future growth. First, there are clear domestic growth triggers, such as an increasing population and an expanding non-agricultural economy, with growing aggregate income, which will need to be supplied with food and food products. Second, with increasing incomes, the domestic market is becoming increasingly sophisticated and price and quality conscious. How much of this demand can be successfully captured by domestic suppliers is a key challenge. Third, as other powerful regional economies grow, and trade barriers relax, the export market for agriculture produce will grow rapidly. The Philippines, however, has only been able to capture a small, and declining share of this market. Fourth, the natural comparative advantages the Philippines has, together with its literacy and technical and entrepreneurial skills, have only been partially harnessed in pushing economic growth – and little in agriculture. Growth in rural areas, therefore, would benefit enormously if the signals (policy and price) are less distorting and can capture the competitiveness and dynamism which are being enjoyed by other, emerging sectors in the broader economy. Last, the overall peace and security situation, particularly in Mindanao greatly hinders investment and output. Long term peace and security in Mindanao would greatly improve the overall economic environment.
3. DRIVERS IN ECONOMIC & RURAL GROWTH

3.1 Aggregate Capital Investment

3.1.1 Economic growth is highly contingent on investment, which is critical to developing and maintaining the country’s vital capital stock. Capital stock, in turn, stimulates employment, incomes, demand for improved productivity enhancing technologies, and demand for higher human skills capacity while facilitating better integration between producers and consumers in existing and emerging markets. This vital synergy underpins a number of essential economic linkages and multipliers, which inter alia, stimulate (Figure 11).

![Fig. 11: Investment-Economic Growth and Multipliers](image)

3.1.2. Foreign Direct Investment. As the Philippines has one of the lowest domestic savings rates in Asia, foreign direct investment (FDI) will remain an extremely important engine of growth [Figure 12].

![Fig. 12: Foreign Direct Investment, 2001-2004](image)

3.1.3. Clearly, in the medium term, the business environment has to remain competitive to ensure higher volumes of both FDI and domestic investment to maintain sustainable growth. In an analysis conducted by the Economist Intelligence Unit (EIU), the Philippines is ranked 36th among 60 countries worldwide and 10th among 16 countries in Asia in terms of projected investment flows for the period 2000-2004 (Table 2), although its score is projected to improve over the next five years (2005-2009), its regional ranking is likely to remain unchanged, suggesting that efforts in other countries to court investment will be equally strong or stronger.

3.1.4. Globally however, the Philippines’ ranking is projected to decrease to 40th, again suggesting stronger global competition for investment and a sluggish momentum in the country’s reform agenda. The country’s score for political stability and effectiveness will remain middling to poor, as uncertainties persist and progress remains very slow on policy legislation. However more encouraging improvements are forecast in the macroeconomic environment and in policies toward foreign investment, trade, and exchange controls. The macroeconomic environment will improve as tighter fiscal measures are brought in to reduce the budget deficit. These measures, however, will mostly be on the revenue side (taxes) as the scope for lowering expenditures is limited given high interest payments and public service costs. The largest single factor that compromises investment in the country is poor infrastructure, the ranking for which is almost at the bottom of the world and regional scores. Higher public/private investment in infrastructure would therefore have considerable benefits in improving not only investor confidence but directly in opening up markets and economic linkages through multipliers. The issues that the government ought to address are: (i) how to generate such investment in the first place, given the budget situation; and (ii) how to prioritize infrastructure investment given a limited public purse and conflicting public expenditure demands [Table 2].
Table 2. Philippine Business Environment Ranking

<table>
<thead>
<tr>
<th></th>
<th>Value of Index(^a)</th>
<th>Global Rank(^b)</th>
<th>Regional Rank(^c)</th>
</tr>
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<tbody>
<tr>
<td>Overall</td>
<td>5.78</td>
<td>6.45</td>
<td>36</td>
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<tr>
<td>Political Env</td>
<td>4.9</td>
<td>4.9</td>
<td>41</td>
</tr>
<tr>
<td>Political Stability</td>
<td>6.0</td>
<td>6.0</td>
<td>38</td>
</tr>
<tr>
<td>Political Effectiveness</td>
<td>4.0</td>
<td>4.0</td>
<td>44</td>
</tr>
<tr>
<td>Marco-economic Env</td>
<td>6.8</td>
<td>8.5</td>
<td>45</td>
</tr>
<tr>
<td>Market Opportunities</td>
<td>5.5</td>
<td>5.9</td>
<td>39</td>
</tr>
<tr>
<td>Policy toward private enterprise &amp; competition</td>
<td>5.2</td>
<td>5.8</td>
<td>39</td>
</tr>
<tr>
<td>Policy toward foreign investment</td>
<td>6.1</td>
<td>7.2</td>
<td>41</td>
</tr>
<tr>
<td>Foreign trade &amp; exchange controls</td>
<td>7.2</td>
<td>8.9</td>
<td>31</td>
</tr>
<tr>
<td>Taxes</td>
<td>6.9</td>
<td>6.9</td>
<td>16</td>
</tr>
<tr>
<td>Financing</td>
<td>5.5</td>
<td>5.9</td>
<td>37</td>
</tr>
<tr>
<td>Labour market</td>
<td>6.9</td>
<td>6.7</td>
<td>18</td>
</tr>
<tr>
<td>Infrastructure</td>
<td>2.8</td>
<td>3.9</td>
<td>56</td>
</tr>
</tbody>
</table>

Source: EIU; a. out of 10; b. out of 60 countries

3.1.5. **Domestic Investments.** In addition to FDIs, domestic private investments will play an invaluable role in stimulating growth and increasing the country’s competitive edge. The trends have not been encouraging, however. Compared to close regional players, the Philippines generally fares unfavourably with its low domestic investment-to-GDP ratio, although the gap appears less significant after the Asian financial crisis in the late 1990s [Figure 13].

3.1.6. A major knock-on effect of this low investment has been the slow emergence and integration into the economy of improved, productivity enhancing technologies [Section 3.5]. This lag in productivity has resulted from failures in education and human capital, which indeed are relatively high in the Philippines, but to much lower physical capital accumulation and sustenance in productivity growth. Consequently, in the period 1960 to 2003, the output per worker in the Philippines rose by around 50%, compared to 450% in other East Asian economies. This gap, needless to say is a major hurdle which will need to be redressed.

3.1.7. **Investments in Rural Infrastructure.** In relation to most countries, the Philippines has comparatively more complex and costly transport system, given its island-based economy. Additionally, its overall state of infrastructure is poor due to significant long term underinvestment. In roads, less than 50 percent are all weather and many of the feeder roads are in poor condition due to substandard construction, inadequate maintenance, and use by overloaded vehicles. Bridges are often weak or absent, and some remote areas have very little in access roads. In rural areas, primary economic growth will be highly dependent on a reliable road and water transport network, which links producers with consumers, and, on irrigation, which reduces risks and raises productivity. The major cost of these infrastructures will lie with national and local government as they are clearly
perceived as public goods. For the national and local governments, the issues are: (i) how can national Government can mobilize resources for infrastructure investment in the current fiscal climate, without substantial cost cutting across other sectors and expenditure categories; and (ii) what capital and recurrent investment can be expected from Local Government Units (LGUs). The first will require Government to develop and adopt a holistic public investment plan, covering national priorities and funding strategies across all sectors. The second will require a clear understanding of fund flow and cost share modalities between National Government (NG) and LGUs together with a substantial strengthening of their financial management and technical capacity [See also section 5].

3.2 Land and Asset Reform

3.2.1. In addition to capital and labour, the third crucial factor in growth in the Philippines will be land, which is the principal asset in rural areas. Here the regulations, principles and signals that govern how the asset is, or allowed to be, used will ultimately determine investor confidence, the assets contribution to agricultural productivity and overall contribution to growth. The longer, for example, distortions and uncertainties in these signals and in asset valuation, property rights and land markets are allowed to persist, the less their contribution and the higher their cost to the economy in terms of competitiveness and growth. Indeed, a key reason put forward for the failure of the Philippine economy to take off (compared to others in the region) is the ‘treatment of land’—its historic and skewed distribution (formerly) and the long delays in completing land and agrarian reform. The Comprehensive Agrarian Reform Program (CARP) is far behind schedule and will not be completed by 2008, the current completion target. To remove uncertainties and improve investment and productivity in land, it is important that the agrarian reform process be completed expeditiously.

3.2.2. To achieve this, however, the Government has difficult choices to make and challenges to face, including:

- Substantial lack of funding for completing and consolidating land reform under the CARP;[4]
- Political and social resistance to further distribution of the remaining lands;[5]
- Slow resolution of existing land disputes and lack of property rights, which are substantially

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[4] Latest estimates indicate that some 100 billion pesos (US$ 1.85 billion) would be required to complete the Land Acquisition and Distribution (LAD) component of the CARP. Of this, a part of the 38 billion pesos (US$ 556 million) from ex Marcos assets could be used, though a substantial gap still remains. Appropriations through the GAA for this level of funding, especially in the remaining period of the CARP, are also unlikely given the present fiscal climate and other Government priorities. It also unlikely that substantial recoveries will be generated through collection of amortization.

[5] There are some 1.78 million hectares of CARPable land remaining. Much of this is private coconut land where current owners are not investing in production.
3.2.3. In addition, there are a number of distortions and uncertainties in the reform process which affect land being used productively as an asset. These include:

- Poor recovery of amortization funds from Agrarian Reform Beneficiaries (ARBs);
- Poor recovery in private transactions as this is reliant on the buyer’s capacity to pay;
- The decline in government land available for future redistribution, thus leaving the redistribution of private lands, which are mostly plantations whose conversion to viable agricultural lands will require investment funds inaccessible to agrarian reform beneficiaries (ARBs), as the main vehicle for agrarian reform;
- The legal prohibition that currently mortgaged land under the CARP cannot be sold on the open market within a period of 10 years after purchase, and then, only to other ARBs, which deters banks from lending against such land due to uncertain value and future ownership, thus severely limiting producer access to credit and distorting the land market;
- The hampered access to land through rental and sales markets caused by compulsory land acquisition and collateral-based lending under which collateral in land cannot be foreclosed, which, together with uncertainties in landownership, has depressed investment and productivity in agriculture;
- The highly inefficient land transaction system exacerbated by multiple fake and bad land titles;
- The highly inefficient land registration system: under which only 45 percent of parcels have deeds; while the total number of land parcels is unknown, and the titling of land and the registration of land transactions are long delayed; and
- The high land transaction costs due to tax, corruption and informal payments resulting in the emergence of a parallel, informal land market, which does not contribute to tax revenues.

MTPDP Thrust - Land and Asset Reform:
In view of the issues above, related plan thrusts under Agrarian Reform include: (i) the use of the Agrarian Reform Fund (ARF), including the Marcos assets, to complete land distribution and fast track support services; (ii) expedite the passage of the Farmland as Collateral Bill to improve credit access; (iii) fast track mediation and resolution of land disputes to improve tenure; and (iv) accelerate the provision of support services.

3.3 The Environment and Natural Resource Management

3.3.1. To complement measures for a sound and open investment base in the economy, there is the need for proper management of natural resources (agriculture, marine, forests and minerals) and the environment. Inadequate regard for implementing sound natural resource management (NRM) measures and safeguarding the economy from excessive environmental costs is rapidly eroding resource inventories and will seriously compromise short term economic gains by larger, longer term costs. In addition to direct resource costs, in the form of a depleted resource base, that lack of concern for the natural resourced base and the environment will cause investor confidence to lag as pollution, health and congestion costs increase, tourism revenues to decline as the earlier comparative advantages (wild life and natural beauty) disappear, and the cost of cleaning up after irresponsible industries to fall on Government. Consequently, continued Environment and Natural Resources Management (ENRM) mismanagement constitutes a major impediment to long-term growth.

3.3.2. The cost of past failures has already been high. Forestry is now a marginal sector, as a result of resource depletion and unsustainable management over a long period, which took the country from being the world’s biggest exporter of tropical hardwoods in the 1970s to being a net importer of forest products by the 1990s. In the early 1960s, the timber industry was the largest source of foreign exchange earnings, which declined rapidly and
by the 1990s the sector’s contribution to export earnings was less than 0.5 percent. In addition to export products, there was also significant loss of natural bio-diversity with the loss of a wide variety of tropical rain forest, floral species, a diverse range of endemic faunal species and several important marine and coastal ecotypes. [Figure 14].

3.3.3. Unregulated illegal logging, moreover, has also increased human and economic cost, as landslide and flood disasters in central Luzon demonstrated in 2004.

3.3.4. In fisheries, the problems of over-fishing and fishery stock depletion are attributed to the prevalence of an open-access system, the use of destructive techniques, and the inability of government enforcement agencies to regulate entry to fishing waters and penalize destructive and depletive activities. The decline in fishery stock is also related to upstream externalities, i.e. pollution, siltation, sedimentation, and mine tailings, and the loss or damage of coral reefs, mangroves, and other fish habitats.

3.3.5. Long term, sustainable economic growth and poverty reduction in the Philippines will depend critically on how successful Government will be in providing an effective framework for ENRM. However, despite some improvement in policy and other instruments to institute responsible ENRM, results have been mixed at best. This is attributed to a variety of reasons, including:

- An open access policy, and weak property rights and management authority, the open access policy being brought about by the limited success of various tenurial instruments to confer property rights and their failure to close access, thus encouraging over-exploitation;
- The Department of Environment and Natural Resource’s [DENR] falling budget and its structure which allocates a high proportion on personnel services and little for operations and investment in ENRM;
- The fragmentation of the DENR’s budget over diverse and undercoordinated functions (bureaus) and its high dependence on Official Development Assistance (ODA);
- The slow devolution toward more community and local responsibility for ENRM, compounded by complex and cumbersome processes of securing tenure and property rights, and recently, the blanket cover annulment of all Community Based Forest Management Agreements (CBFMAs) to the benefit of the private sector;
- The goals of more local transparency and accountability in ENRM not being met as the Integrated Protected Areas Fund (IPAF) mechanism remains ineffective and there is significant lack of assured funding for local institutional bodies - provincial environment councils and Protected Areas Management Boards (PAMBs); and
- The lack of service and performance standards in ENRM, e.g. very slow procedures in securing tenure instruments and issuance of resource use permits.

What is needed?

- A sound and efficient institutional basis for ENRM based on a watershed and ecosystem approach - only after which other purposeful policy and regulatory actions become more feasible;
- A substantial management and institutional overhaul to improve service delivery, including (a) the rationalization of expenditures (e.g.
Personnel Services (PS vs non PS); (b) a significant improvement in prioritization of functions – linking major final outputs (MFOs) with budget; (c) more effective partnership with line agencies to improve delivery; (d) more effective devolution and local responsibility for ENRM; and (e) the rationalization/streamlining of the policy and legal framework for ENRM to improve efficiency;

- The structuring of ENRM on the integrated management of: (a) watersheds, (b) coastal resource and (c) protected areas, which requires the DENR to develop effective land use and real time database systems to update inventories and monitor the country’s resources, thus providing sound basis for Environment and Natural Resources (ENR) planning and management;
- Closing open access forestry, marine fishery and water resource areas and establishing secure tenure systems; and
- Concerted efforts to improve mineral resource share agreements, to solicit approval and participation, particularly in protected areas, areas with ancestral domain claims and areas of high seismic and natural hazard risks.

**MTPDP Thrust - ENRM:**

The thrusts in the MTPDP can only be realized if the financial and institutional basis for ENR management (primarily through DENR, LGUs and communities) is made much stronger, allowing them to direct more efficiently operational resources in aggressively pursuing the policy, legislative, regulatory and governance changes required. [Section 4]. The key thrusts in ENRM are: (i) sustainable and productive utilization and investment in natural resource; (ii) promotion of responsible mining; (iii) protection of vulnerable and ecologically fragile areas; (iv) a healthier environment; and (v) disaster mitigation.

### 3.4 Technology and Productivity Development

#### 3.4.1. Enhancing the contribution of factors of production (land, labour and capital) in economic growth requires complementary investment in productivity enhancing technologies and their efficient dissemination. Past efforts in research have been undeniably successful, with yields of staples increasing significantly in the 1960s, when food shortages were rampant and the world food outlook was bleak. During this period, although it also progressed, the Philippines lagged behind other countries in Asia. This accrued particularly in corn, where the projected productivity gap (over the plan period) is likely to increase leading to further rises in imports [Figures 15 & 16].

![Fig. 15: Corn Yields Philippines (1961-2004)](image1)

![Fig. 16: Rice Paddy Yields Philippines/Asia (1961-2004)](image2)

Source: FAO

#### 3.4.2 The main reasons put forward for the country’s low productivity are: (i) declining and poor structure of research expenditure; (ii) institution weaknesses; (iii) the nature of research; and (iv) availability and price of inputs. Taking these in turn:

- **Research Expenditure.** International funding for research has been declining. For example, the
World Bank’s lending to research has decreased to around US $ 30 million in 2002, from a peak of almost US $ 400 million in 1998. In part, the decline is attributed to the failure of borrowing countries to commit to programs of institutional reforms. In the Philippines, research is mostly publicly funded, with private research accounting for around 20%. In public expenditure, Research and Development (R&D) has to clamour for scarce resources with other Government departments and agencies and rates fairly low in terms of national expenditure priority in comparison, for example, to infrastructure. Problems of the decline in aggregate research funding, are further exacerbated by expenditures disbursed over multiple institutions and expenditure structure, which, in common with other departments, is heavily weighted toward personnel (wage) costs. Without being able to invest more in actual research and to operationalize it much more effectively, research is becoming almost an end in itself, demoralized, non-responsive to changing demands, and poorly disseminated.

- **Institutional Weaknesses.** There are a large number of public R&D institutions with overlapping functions and roles, many duplicating R&D networks; and with weak linkages to producers, LGU extension units and the private sector. There is, therefore, clear need to converge and streamline functions and responsibilities. Recommendations toward this end include developing unified systems for planning, and research and extension programming amongst the various agencies.

- **Nature of Research.** Research expenditures are almost entirely on expanding production, mostly food crops, with little provided for market-driven and post-harvest research in high value commodities with recognized market potential. Likewise, funding for training is largely on supply-driven issues. Correcting this imbalance between supply- (production) and demand- (market) led research will be important in modifying and strengthening the system.

- **High Input Prices.** Low productivity is also attributed to the poor input distribution network and cost. Irrespective of productivity enhancing research recommendations and packages, many farmers will not apply recommended doses nor use high yielding seed varieties due to the potential risk involved in failure and cost. Although this is common to most poor farmers in developing economies, in the Philippines the problems are exacerbated by inordinately inflated costs. For example, prices paid for urea in some years have been markedly higher than world market price\(^8\) [Figure 17]. The most likely reasons attributed for inflated cost are the monopoly in fertilizer supply, and inefficient regulations governing distribution and supply. The same situation probably exists for pesticides and other agro chemicals. There are also supply constraints in high yielding seed varieties.

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\(^8\) Border prices CIF.
4. THE FACILITATORS OF GROWTH

4.1 Policy, Public Sector & Expenditure Management.
Public resource availability to finance expenditures in the medium term is saddled with critical constraints that will have to be addressed if the volume, allocative efficiency (AE) and management of public financing is to be improved meaningfully. These include poor: (i) overall fiscal sustainability, budget size and investment capital; (ii) allocative efficiency, public expenditure management and budget structure; and (iii) linkage between public sector policy, planning and budgeting. Taking these in turn:

4.1.1. Poor Fiscal Sustainability: The Philippine public debt has grown to a level that significantly constrains public and private investments, and this is significantly undermines the quality and sustainability of economic growth. Large public sector financing requirements mean that the country is particularly vulnerable to shifts in investor sentiment [Section 3.1], and is at increasing risk of financial market volatility and crisis. Overall, fiscal flexibility is being steadily eroded as revenues decline and mandated expenditures remain high. Discretionary expenditures, growing transfers to sub-national governments, low revenue collections, rising debt service, and high expenditures on personnel services provide very little flexibility to evolving needs, to trigger growth. Since 1997, there has been a continued deterioration in public finances, which has seen a slight budget surplus translate into a significant deficit. There have, however, been some upward trends since 2003 and slight improvements which are projected to continue as recent tax revenue measures (e.g. VAT) filter in to the economy and the gap between revenues and expenditure narrows [Figure 18].

In most agencies, this deterioration in public finances has led to significant decline in real budgets for example, that of the DENR [Figure 19].

4.1.2. To sustain fiscal flexibility, the clear options are to: (i) reduce expenditures; (ii) raise revenues (reverse the decline in tax revenues since 1997); and (iii) improve allocative efficiencies and streamline the bureaucracy. Unless these are addressed there would be continued adverse impacts on growth, through: (i) reduced resources for human development and infrastructure; and (ii) declining public capital investment and lower foreign and private investor confidence.

4.1.3. A key area on the revenue side would be to enhance the capacity of LGUs to generate more local revenues, the relative levels of which have not increased significantly over the last 10 years. On the other hand, the proportion of national budget going through Internal Revenue Allotments (IRAs) has continued to increase [Figure 20].

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4.1.1. Moreover, although revenue mobilization and administration at the local level appear to have great potential, the impasse vis-à-vis IRAs and cost share arrangements between NG and LGUs has introduced considerable uncertainty in investment planning and expenditure. This needs to be addressed quickly.

4.2.1. Maintenance, Operating and Other Expenses (MOOE) and Capital Outlay (CO) are essential for making and maintaining past and current investments. That these cost items have had declining allocations is unfavourable in terms of increasing and sustaining the productive, capital stock of the country. These will require Government to focus on providing strategic public goods in line with recognized priorities, reducing the public sector wage bill through rationalizing the bureaucracy to increase the share of non-wage expenditure.

4.2.2. Allocative efficiency is also diminished by various distortions. A major concern is the allocation of scarce resources to special budget/development funds that are not necessarily aligned with national priorities and are not transparent in use. The prevalence of special congressional funds in the national budget raises the issue of budget comprehensiveness, as expenditures from these funds are frequently “off-budget” as they are not accounted for either during budget formulation or execution. Individual senators and congressmen are also entitled to a variety of additional funds for development purposes, and other congressional initiatives, and to compensatory allowances. These congressional funds in effect represent a significant amount of off-budget resource allocation that is not open to prioritization, accountability, and transparency requirements as other expenditures are. This inevitably undermines the efficiencies of proper public investment planning [section 4.3].

4.2.3. An additional issue is the myriad of special authorities, corporations, funds, and administrations affiliated with sectoral departments. For example, the DA and DAR have 11 government corporations and numerous special-purpose funds, the total allocation of which represents more than two thirds of the total sectoral budget. In Agriculture, public goods and services account for only 40 percent, whilst rice price stabilization receives 20 percent of allocation.

4.2.4. The slow devolution of functions and resources has added to the problem and costs, as institutional arrangements for service delivery remain incomplete and national agencies continue playing a role in functions that should
have been fully developed. In Agriculture, research and extension, for example, remain de-linked and key infrastructure such as farm-to-market roads and communal irrigation are deteriorating due to this confusion of responsibility and fund flow. To make devolution and decentralization more effective and less costly, LGU capacity in financial management and procurement will be essential to improve service delivery and accountability.

4.2.5. Improving Allocative Efficiency in Agriculture and Agrarian Reform. In line with the thrusts in the MTPDP, the allocative efficiency of public resources to agriculture and agribusiness sectors has to be improved substantially. In agriculture, given resource constraints, public expenditure will need to be more narrowly focused on “growth-enhancing public goods and services” and less on personnel. Figure 22, illustrates the distribution of DA’s regular (non-AFMA) budget by category.

![Fig. 22: Percentage of Total DA Budget by Category, 2005](image)

Source: DA

4.2.6. Conversely, non-growth enhancing expenditures such as those for rice price stabilization, which account for 20 percent of the agriculture sector’s allocations, need to be phased out. The Government has also expressed determination to resolve issues related to the removal of the National Food Authority’s monopoly to import rice and to allow farmers’ organizations to undertake direct importation.

4.2.7. The major sources of growth in crop production will also need sustained public expenditure investments in improved and strategically located irrigation and farm-to-market roads, market related developments and increased farmer access to these facilities, adoption of improved seed varieties, and limited area expansion.

4.2.8. In agrarian reform, key recommendations would be to complete land distribution and agrarian reform as quickly as possible to reduce distortions and uncertainties as the economic cost of delaying the process are extremely high. The suggestions toward this end include: (i) exploring ways to finance land acquisition through alternative sources, in view of the magnitude of the resources required; (ii) greater use of market-oriented and community-driven modalities of land transfer; and (iii) pursuit of a “parallel approach” that balances public expenditure on land acquisition and distribution with provision of support services to previously redistributed landholdings. The provision of support service through convergence in rural development involving agencies and stakeholders, under some form of area based approach, for example agribusiness [Section 5.3.2], would also have additional benefits through comparative advantages, value addition and multipliers.

4.2.9. The composition of expenditures can also be improved by GOP: (i) phasing out of private and non-growth-enhancing goods and services - including price stabilization, which benefits only 3 percent of rice farmers, and production inputs (e.g., seeds); and (ii) moving LGUs toward financing major gaps in devolved responsibilities, especially communal irrigation, research and extension and strengthening farmers’ institutions. Directing more resources for agriculture development in Mindanao would also have large benefits, in view of the island’s considerable untapped potential.

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4.3. Policy, Planning and Budgeting

4.3.1. Government efforts at improving fiscal health and discipline could be considerably compromised by the continued poor linkage among development policy (targets), planning and budgeting. This contributes to poor budgeting outcomes at the macro, strategic and operational levels as the process is highly fragmented and independent. Planning, moreover, is mostly focused on donor funded investment activities, which supplement capital outlay and MOOE. Consequently, annual budgeting is reduced to allocating resources thinly across donor and domestically funded capital projects and to operations [Figure 23].

4.3.2. In addition, line agencies tend to budget and spend on an ad hoc basis as even small discretionary allocations are rarely predictable. Indeed, unpredictability of funding, from one year to the next and within the budget year, is one of many factors that contribute to poor operational performance in the public sector. Others are related to the failure to direct resources to policy priorities – in significant part because budgeting is treated as an annual funding exercise, not a policy-based exercise - and to the lack of authority and responsibility given to line managers to manage resources at their disposal.

4.3.3. Budgeting in the line agencies is mostly “plan or needs driven” rather than based on a perception of availability, despite the Department of Budget Management’s (DBM) prior warning on the available funding in an annual cycle. These conflicting positions have become par of the course. The Department of Finance (DOF) and DBM are obliged to keep tight budget ceilings in line with the present fiscal climate and forecast availability, whilst line agencies routinely inflate needs to protect against perceived cuts and fear that if lower better prioritized budgets were submitted their ceilings would be cut. This leads to significant discrepancies between proposed and appropriated budgets [Figure 24]. The result is an inefficient budget process, which undermines effectiveness.

4.3.4. Moreover, better reconciliation between proposed and appropriated budgets will need time and more fundamental restructuring of public expenditure engaging DBM, NEDA, line departments and the cabinet (as inter-sectoral trade-offs have to
be faced) in a process that has a medium-term perspective. Donors also need to be involved given their significant contribution to budget financing. “Availability,” both domestic funds and aid, must be projected beyond a single year, and indicative shares communicated to departments. “Needs” must be prioritized and made consistent with the resource framework. All these must happen in a manner that encourages departments to re-examine commitments, together with oversight agencies, under a workable and holistic Public Investment Program framework.

4.3.5. **Improving Planning and Budgeting in Agriculture.** To continue the process of improving budgeting and resource utilization in the agriculture sector, there is a need to continue moving towards functional budgets and away from the commodity-based structure while also enhancing convergence of resources. There is also a need to eliminate costly duplication of functions (e.g., public sector several agencies involved in farm to market roads). Short-term actions toward these ends comprise strengthening the linkage between planning and budgeting within each agency in line with MFOs and the further simplification of reporting systems. In the medium-term, budget control needs to be decentralized away from agencies to LGUs, as capacity and accountability improve, and ways found to make levels of LGU financing proportionate to devolved responsibilities. In the longer term, a holistic PIP would require that sector representation participate in the budget setting process.

4.3.6. For prioritizing PAPs, key recommendations for the short term include the pursuit of a “plan-driven” approach to budgeting with stronger output-outcome linkages, and a systematic review of the key reasons for reversion of funds at year-end. In the medium term, there is a need to strengthen strategic planning capacity in agencies and LGUs, and develop and use quantitative methodologies for prioritizing agency and LGU PAPs, develop and pilot sector-level, agency and LGU performance monitoring and assessment methodologies. In the longer term, there is a need to adjust sector allocations based on sector performance assessment results, adjustment of interagency and LGU allocations based on performance assessment results, and develop congressional capacity for more effective oversight of the planning and budgeting process.

4.3.7. In view of the levels of expenditure in agriculture and agrarian reform, key actions in the short term could comprise a more detailed review of apparent agency and LGU under-spending on agriculture and agrarian reform based on AFMA, Agriculture and Fisheries Modernization Plan (AFMP), and other objective criteria, exploring alternative methods of financing; and implementing new land acquisition. In the medium term, a review of agriculture sector allocations based on AFMA levels, building LGU capacity to access alternative financing schemes for agriculture and agrarian reform PAPs will be needed. In the longer term, the employment of alternative financing schemes and modalities for new land acquisition, and the design and implementation of alternative LGU financing schemes are recommended.

4.3.8. Allocating resources by function\(^{11}\) and measuring the impact of outcomes and service delivery are also important in effective planning and budgeting. In the short term, this would include strengthening the Sector Efficiency and Effectiveness Reviews (SEER) process and the capacity of LGUs in agriculture sector planning, budgeting, and extension. In the medium term, there is a need to pursue effective cost-sharing mechanisms for expenditures on infrastructure, research, development and extension, and production inputs. There is also a need to pursue the convergence of PAPs across DA, DAR, LGUs and the private sector especially in agrarian reform communities and conduct of independent impact and outcome assessments at sector, agency and LGU levels. In the longer term, it may be necessary to “mainstream” key issues regarding implementation of externally-financed projects.

\(^{11}\)An example includes the World Bank Diversified Farm Income and Market Development project, which set budget targets by MFO/ function (not commodity or programme) to meet better declared DA priorities in market development under AFMA. The project also prioritized improved linkages between planning and budgeting. The proposed World Bank projects for DENR and DAR will also be based on targeted expenditure support by MFO.
4.4. Agricultural Finance

4.4.1. Agricultural finance is critical to producers for meeting a range of production and marketing needs i.e. inputs, irrigation, technologies; transport and other marketing costs. Such financing enables producers to insure against price and/or yield fluctuations and invest in value addition and agribusinesses. The international experience of programs in credit and rural finance, however, has not been overly encouraging as many schemes have not proved to be neither financially nor economically sound and sustainable, principally due to the prevalence of subsidies. Consequently, lending for rural financing, like research, has been declining. This is attributed to the growing importance of finance to other sectors, the poor performance of agricultural banks and credit lines, and moves against the use of subsidized credit.

4.4.2. The focus of recent Bank operations is therefore shifting more to credit for agricultural production and agribusiness, small loans for off-farm activities, and savings services. Although these have met with some success, there is considerable need to find viable mechanisms to address the specific demands for agricultural financing. To meet these challenges, therefore, the World Bank advocates a number of innovative approaches including financial systems development, which views agriculture financing as part of the wider rural finance market. The approach is based on the premise that institutions adhering to commercial principles are more likely to achieve outreach and sustainability, whilst that the role of the public sector should be focused on ensuring that the environment remains conducive for the establishment and growth of such institutions. The Bank also advocates the formulation of a policy framework for the crucial role of the public sector in maintaining macroeconomic stability and establishing sound regulatory principles in the financial sector. To be effective this must be supported by accompanying provisions for secure property rights, financial transactions, and mobilisation of savings. The Bank further advocates credit focus for the poor through microfinance and the provision of subsidies, credit lines and guarantees under certain agreeable circumstances, which will not distort markets.

4.4.3. In the Philippines, a number of key reforms were introduced in rural financial markets in the late 1990s in recognition of the failure of earlier subsidized directed credit programs (DCP). To facilitate and consolidate programs, the Agricultural Modernization Credit Financing Program (AMCFP) was created under the AFMA and was viewed as a wholesale financing facility for the agriculture sector. A number of constraints, however, still persist in rural lending, chiefly: (i) some subsidized programs

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still remain in the DA and its bureaus; (ii) the DA and Land Bank of the Philippines (LBP) have yet to develop details of the AMCFP and the strategies and instruments to be used for financing agricultural modernization; (iii) banking obstacles that do not allow land from agrarian reform to be used as collateral for credit still exist; and (iv) the partnership between government financial institutions (GFIs) and private sector institutions for on-lending remain very weak. Of total lending, therefore, little (less than 10 percent) goes to agriculture. [Figure 25]

4.4.4. The following are needed: (i) the rationalization of directed credit programs in agriculture and the immediate termination of remaining (subsidized) credit programs; (ii) the downsizing of more funds need to be channelled through GFIs for on-lending through the private sector; (iii) the finalization by the Land Bank of the Philippines (LBP) and DA, working with the private sector, of operational modalities for implementing the AMCFP in line with the AFMA; (iv) making more accessible funding for long-term crops; and (v) increasing the facility for small loans (150,000 - 1 million pesos) as financing for export orientated crops needs to be encouraged and increased.

**MTPDP Thrusts - Rural Credit:**
To ensure efficient rural finance support to agriculture and agri-business development the plan advocates:
(i) all directed credit programs will be rationalized by December 2005; (ii) public-private sector mechanisms to mobilize finance for the fisheries sector will also be established; (iii) legislation on the farmland as collateral bill will be expidited; and (iv) the Agriculture Competitiveness Enhancement Fund (ACEF) will be extended to 2015.
5. Governance, Policy and Regulations

In spearheading economic growth, the Government has to maintain a conducive and competitive macro-economic, policy and regulatory environment that will encourage greater inflows of aggregate foreign and domestic investments. In addition to physical infrastructure, this will require it to send the right and sustained political, fiscal, expenditure, policy, institutional and governance signals. Strengthening the overall investment climate, providing the required infrastructure, improving fiscal discipline and rationalizing public sector expenditure are discussed above. The remaining issues include: (i) governance and corruption; (ii) bureaucratic and institutional efficiency; and (iii) “good” policy and regulations.

5.1. Governance and Corruption

5.1.1. Efforts by the administration in strengthening governance in public institutions and reducing corruption will go a considerable way in determining overall investor confidence. However, the Philippines has been ranked poorly by the World Economic Forum at 100 out of 104 countries worldwide for widespread corruption in 2004.¹³ This external perception is consistent with that of domestic investors, a large proportion of whom consider most public institutions as being corrupt. Although a number of initiatives have been effected, these will need to be sustained and followed-up to have real impact. These include: (i) procurement and financial management reform under the Procurement Reform Act of 2003; and (ii) greater decentralization of services to local governments.

MTPDP Thrusts - Corruption:
The main strategies are: (i) zero corruption tolerance; (ii) minimize opportunities for misconduct in government; (iii) improve audit of systems and procedures; and (iv) further strengthening procurement reforms.

5.2. Bureaucratic and Institutional Efficiency

5.2.1. In addition to rationalizing costs through rightsizing, efforts at making the civil service more merit-based, improving the structure of salaries and remuneration and inculcating stronger integrity in public office are essential to improving overall public service delivery and performance.

Further progress is essential on the government’s plans for providing incentives for exit packages (EO 366) and ensuring that related costs are fiscally manageable and that there are minimal abuses through re-entry. Reducing the number of presidential appointments to civil service positions would also send a strong signal of government commitment to strengthening civil service meritocracy, professionalism and morale.

5.2.1. Specifically in rural institutions (DA, DENR and DAR), the problems of a large bureaucracy are exacerbated by overlapping mandates, functional duplication, and incomplete functional and fiscal devolution to local governments. These inefficiencies add substantially to the cost of running institutions and substantially compromises service delivery. To redress these inefficiencies will require greater efforts, outlined in the MTPDP, at forging agency convergence on planning and implementation of rural development activities, rationalizing overlapping functions and strengthening devolution to LGUs for devolved public services like infrastructure. Caution in the devolution process, however, is needed, as experience shows that although some LGUs have performed well, others have not. Improving service delivery through improved LGU performance calls for greater local resource mobilization and the implementation of procurement and financial management reforms coupled with institutional strengthening, better local budgeting, and more effective management of human and financial resources and assets. Key areas which need to be addressed to make decentralization more effective include: (i) design of decentralization; (ii) LGU revenue mobilization; (iii) LGU financing; and (iv) LGU budgeting¹⁴.

5.3. Policy and Regulation

5.3.1. Poor, conflicting and inconsistent policies and unnecessarily complex regulations can significantly distort economic signals and markets and add considerably to the cost of doing business. This can lead to substantial misallocation of resources; deter investment, and compromise innovation, diversification and ultimately growth. In the Philippines, the preponderance of regulations (that

MTPDP Thrusts - Bureaucratic Reform:
The main strategies are the: (i) elimination of irrelevant functions; (ii) consolidation of duplicated functions; (iii) improving of salary structure and merit based promotions; and (iv) ensuring of continuity in public sector staffing and reduction in the number of political appointees. Specifically in the agriculture, agrarian reform and natural resources (AARNR) sector, the emphasis of reforms will be on: (i) greater functional compliance with the provisions under the LGC, AFMA and the Fisheries Code; (ii) improving efficiency and convergence and reducing overlaps in the three agencies; (iii) implementing AFMA provisions for rationalization and consolidation of the system of agriculture and natural resources research, development and extension; (iv) integrating various agencies involved in the land titling; and (v) shifting further the orientation of DA toward functional lines and away from commodities.

often facilitate rent seeking, and political and judicial interference in regulatory decisions are detrimental to policy credibility. Conversely, if public sector service delivery is improved and access to economic opportunity enhanced, public confidence in economic policy would strengthen. Furthermore, the willingness of citizens to pay taxes in exchange for improved delivery of public goods and services would also improve. Taxes, expenditures and public services are therefore inextricably linked via a social contract linking economic and governance agendas, providing a sustainable approach to economic and human development.

5.3.2. Policy Reform & Agribusiness: Agribusiness is very high on the agenda for promoting sector and general economic growth in the Philippines. To achieve this will require well functioning markets and an engaged, innovative and competitive private sector. Lowering distortions and price signals (see above) and facilitating efficient agricultural markets will provide the crucial platform for investment and capitalizing on market opportunities. To meet the needs of the private sector, the Government, as discussed throughout this paper, has to be proactive in providing an enabling and stable macroeconomic environment, strong finances and service delivery, a well functioning and transparent regulatory, policy and legal system, and good infrastructure.

5.3.3. The Philippines lags significantly behind many competing countries in providing for these very clear needs, making the country much less competitive and responsive to fast emerging global trade and market opportunities. Unaddressed, the gap will simply get larger. To promote better public/private cooperation and partnership in agribusiness development, the following are advocated15,16:

- The public sector should not do what the private sector can do better (e.g. direct provision or distribution of agricultural inputs - seed or fertilizer);
- Public interventions should go to activities that have the highest potential for economic and social benefits and not where powerful political lobbyists want it to go;
- The use of input and credit subsidies, where they exist, need to be phased out; and
- Greater consultation should be encouraged in preparation and implementation of new rules and regulations related to the agricultural (domestic and international) trade.

MTPDP Thrusts - Agribusiness:
The principal plan goals are to substantially increase aggregate production (2 million hectares), raise productivity, particularly of high value and export crops, and improve access to food markets. The related thrusts are: (i) fostering greater public/private partnership to facilitate the transformation of farming to agribusiness; (ii) implementing specific programs for intensifying crop, livestock and fisheries production, especially high value products; (iii) transforming idle lands and resources into productive agribusiness enterprises; (iv) promoting off- and non-farm enterprises; and (v) making Mindanao the country’s main agro-fishery export zone. In raising productivity the plan focus is to: (i) raise factor productivity — to regional average levels in 6 years; (ii) improve the effectiveness of transport and logistical systems; and (iii) implement critical governance reforms to make the public sector and policy less distortive15 and more responsive to enterprise and private sector needs.

15 World Bank Agriculture Investment Source Book.
16 This includes further rationalization of grain trading and reorganisation of National Food Authority (NFA).
