PITO

PRIVATE INVESTMENT AND TRADE OPPORTUNITIES

ECONOMIC BRIEF
NO. 15

THE PHILIPPINE
PRIVATIZATION PROGRAM

East-West Center

The *PITO Economic Brief* Series

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December 1993

EAST-WEST CENTER

Program on International Economics and Politics
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THE PHILIPPINE PRIVATIZATION PROGRAM

Felixberto U. Bustos, Jr.*

INTRODUCTION

Since the smooth transition of power in May 1992, the Philippine economy has been relatively stable despite the power shortages which have been reduced to an average of two hours each day.[1] In line with the Ramos Administration's concerns—which include economic development; productivity and growth; and equitable distribution of opportunities, income, and wealth—the government's presence and intervention in private business have been reduced or eliminated through the privatization program. Entities that are affected by the privatization program include banks, hotels, shipping and transportation companies, telecommunications firms, and mining and steel companies.

FORMULATION OF THE PHILIPPINE PRIVATIZATION PROGRAM

The concept and policy formulation of the Philippine privatization program began in the early 1980s in the aftermath of the 1983

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[1] This is in contrast to a high of eight hours of power outage daily during the summer.

economic crisis that was spawned by the assassination of former Senator Benigno Aquino. The program was formalized as part of the World Bank (WB) Structural Adjustment Loan (SAL) for the public sector in 1984.[2] The International Monetary Fund (IMF) likewise incorporated privatization as a requirement of its own stabilization loan package to the Philippines. In the "Enhanced Monitoring Scheme," the progress of privatization was monitored in IMF's annual review of the Philippine's economic and monetary performance.

The foundation of the Philippine privatization program was established in the last years of the Marcos Administration. An extensive study of state-owned enterprises (SOEs) and their role in national development was carried out by the Presidential Commission of Reorganization which was chaired by Armand Fabella (the present Philippine Secretary of Education). The results of this study were two presidential decrees (PDs), PD 2029 and PD 2030, both of which are dated February 4, 1986. PD 2029 laid down the guidelines for the creation and regulation of government-owned and -controlled corporations (GOCCs), while PD 2030 provided for the orderly disposition of certain assets of government institutions and provided the legal basis for the transfer of GOCCs that were deemed not essential to the opera-

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[2] The inclusion of the program in the SAL followed a report by a WB mission which concluded that the bulk of the Philippine public sector's external debt had been extended to state-owned enterprises (SOEs), the majority of which were operating at a loss and could not service their obligations. As a result, the WB recommended a restructuring of SOEs and the adoption of a privatization policy.

tions of government to private hands. This decree became the basis of President Corazon C. Aquino's Proclamation No. 50, dated December 8, 1986, which formalized the Philippine Privatization Program.

Proclamation No. 50 launched a program for the speedy disposition and privatization of certain government corporations and assets. The law also created the two bodies that would spearhead the program, i.e., the Committee on Privatization (COP) and the Asset Privatization Trust (APT). The COP is a cabinet-level committee headed by the Secretary of Finance that decides which assets the APT is to sell. COP approval is required for all privatizations, whether recommended by the APT or other "disposition entities" (these are usually the government agencies which had previously administered the GOCCs slated for privatization; they continued to be responsible for the GOCCs administration/privatization until such time as the COP assigned the task to the APT).

The APT, on the other hand, was created to act solely as a trustee of the national government with respect to assets assigned for privatization. The focus of the APT is mainly the "reprivatization" of nonperforming assets that have been transferred to the government as a result of rehabilitation programs of two state-owned banks, the Philippine National Bank (PNB) and the Development Bank of the Philippines (DNP).[3] The proceeds from

[3] These assets became government-owned as a result of defaults in loan repayments by their private owners.

Table 1 APT Assets by Government Agency of Origin

Government Agency	No. of Assets
Philippine National Bank/ Development Bank of the Philippines	399
Government-owned and -controlled corporations	27
Philguarantee	9
National Development Corporation	11
Total	446

the sale of these nonperforming assets helped to fund the government's Comprehensive Agrarian Reform Program (CARP).

At the start of the program in 1987, 419 nonperforming assets and 27 GOCCs were assigned by the COP to the APT for privatization (see Table 1). Of these 446 assets, however, 44 assets were common to more than one transferring agency (i.e., it had been indebted to more than one government agency). Thus, APT's total portfolio was actually 402 assets, the bulk of which were transferred from the two state-owned banks.

As of June 30, 1993, the program had generated some P56 billion (US$2.05 billion) for the government with the bulk coming from the APT's disposal of some 305 assets at over P34 billion. Among the large GOCCs that were fully privatized are the Commercial Bank of Manila, the Philippine Plaza Hotel, Marina

Properties, and the Philippine Airlines (the government now holds a minority share). Partially privatized were the Union Bank, the Philippine National Bank, the National Shipping Corporation, and the International Corporate Bank (see Box 1: Recent Privatizations). In fact, as noted by the World Bank, the program was "implemented successfully with more than 60 percent of public assets identified for the first stage of privatization having already been offered for sale."[4]

The major thrust of the program, however, which was the "privatization, restructuring, rationalization and divestment of government corporations and their subsidiaries that have proliferated during the Marcos regime," has not been fully realized. After seven years of operation, the bulk of COP approvals have been in the reprivatization of the more attractive nonperforming assets in the APT's portfolio. Of the 122 GOCCs slated for privatization, only 85 had been sold by mid-1993.

The APT's remaining task is the sale/settlement of 162 assets that remain in its portfolio. Of these assets, 65 have already been partially disposed of (see Table 2). Now in its final year, the APT is working on a P2 billion sales target. For the first semester of 1993, the APT disposed/settled 24 assets worth P1.66 billion or 83 percent of its goal for the final year.

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[4] World Bank. 1993. The Philippines: An Opening for Sustained Growth. Report No. 11061-PH.

Box 1

Recent Privatizations

The private placement or strategic sale of PAL shares

In January 1992, 67 percent of PAL shares were bought by PR Holdings, Inc. for P9.78 billion. The partners of the consortium were Antonio Cojuangco of the Philippine Long Distance and Telephone Company with a share of 36.5 percent, the Bank of the Philippine Islands (BPI) with a share of 10.7 percent, and the Sorianos of San Miguel Corp. (SMC) with a share of 6.4 percent. The remaining share of 46.4 percent was held by the government.

It was later determined, however, that tobacco magnate Lucio Tan, an alleged Marcos associate[1] had provided the bulk of the financing for Cojuangco's PAL bid and was, therefore, the majority owner of PR Holdings. The business community and investors expressed great apprehension over the possibility of former Marcos cronies regaining their clout by buying back assets that were put up for sale as part of the privatization movement. This prompted the COP's technical committee to recommend a total ban on the participation of Marcos "cronies" for the bidding of state-owned assets.[2]

The Philippine National Bank (PNB) offering

In May 1989, the Philippine National Bank (PNB) successfully offered 30 percent of its shares to the public at a floor price of P170 per square or P1.836 billion for the entire block of 10.8 million shares. However, the PNB received a substantial amount of criticism about the low price that was set for this initial public offering. Subsequently, when PNB offered another 10 percent of its shares in March 1992, it opted to adopt the open pricing mechanism with the offer price being set only two days before the offering period.

The Union Bank of the Philippines

The consortium controlling the newly privatized Union Bank of the Philippines (UBP) bought the government's share of 93.7 percent in the International Corporate Bank (Interbank) for P2.878 billion in June 8, 1993. UBP had previously bought a 40 percent stake in Interbank from its previous owner, American Express Bank, at US$17.00 or P428 per share.

Before being allowed to buy the 40 percent share of Interbank that was formally held by American Express Bank for US$39.6 million, UBP paid P60 million to NDC, a government-holding company which owned the remaining 60 percent of Interbank, for the state firm's waiver of its right of first refusal. UBP also agreed to a minimum bid price of P520 per share for the government's remaining shares.

The NDC-UBP agreement immediately drew sharp criticisms. Then Finance Secretary Ramon del Rosario pointed out that the compromise removed the "court challenge" that impeded the bank's complete privatization and that the P520 per share minimum offer by UBP would lead other bidders to bid higher for Interbank. However, the only bidder—Rizal Commercial Banking Corporation (RCBC)—bid at the stipulated price of P520 and UBP won with a bid of P530 per share.

Subsequently, the government decided to strictly impose a provision requiring the sale of shares to small local investors of 10 percent of the government's shareholdings before selling the balance to any prospective strategic buyers in a private placement.

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[1] Tan is accused of fronting for the late President Marcos and has some unserved sequestration orders from the Presidential Commission on Good Government (PCGG).

[2] President Ramos noted: "The names of those responsible for all of these misdeeds...must be excluded from further enjoyment of the sequestrations and actions taken by government because they created the problems in the first place." At the same time, however, President Ramos pointed out that the government must also be specific in identifying Marcos' close associates and any charges against them. The COP is currently seeking a ruling from the Department of Justice in defining a crony. Finance Undersecretary Romeo Bernardo tentatively identified a Marcos crony as "one who has a pending case of ill-gotten wealth at the Sandiganbayan; someone who has a pending sequestration order; or who is subject to a sequestration order."

Table 2 Status of APT-held Assets

	Assets	
Status	Number	Share (%)
Fully disposed	240	60
Partially disposed	65	16
Physical	42	
Financial	14	
Equity	9	
Undisposed	97	24
Physical	17	
Financial	63	
Equity	17	
Total	402	100

More recently, President Fidel V. Ramos and his economic advisors have decided to "fast-track" the government's privatization program to help reduce the government's revenue shortfall of P13.7 billion for the first quarter of 1993. Meeting the shortfall assumed even greater importance since the government was about to launch vital infrastructure projects, notably in the energy sector.

The sale of twelve state assets this year is expected to raise P13.4 billion. Besides alleviating the government's cash-strapped position, the early sale of these GOCCs can clinch for the government the IMF's seal of good housekeeping. This will, in turn, pave the way for the release of some US$800 million in loans for the country. Thus, the country's economic recovery could be derailed if the privatization program falters.

Implications for the Philippine Economy

A January 1992 study, which assessed the development impact of the privatization program by looking at the pre- and postprivatization situation of certain APT assets that had been successfully privatized, found that the APT's achievement in revenue generation for the government was remarkable.[5] The sale of 20 assets (study sample) generated P4.3 billion, while additional revenues were generated in the form of income and business taxes. Moreover, the forward and backward linkages that arose from the operation of the businesses in the private sector further contributed to revenue generation. The study also noted that although all 20 assets had been in a depressed state prior to their privatization, after being privatized, there was an increase in economic/technical efficiency.

However, the study also concluded that the program had failed to broaden public ownership of enterprises and to develop the capital market. APT sales were usually conducted through sealed bidding, compared to sales through public offering, and this

[5] The study was designed by Felixberto U. Bustos, Jr., and conducted by a local Philippine accounting/consulting firm. Funding for the study came from the United States Agency for International Development (USAID).

led to less of a diffusion of ownership. Although the sale of assets to different bidders did spread the ownership base across a larger set of individuals, there were a number of instances where the previous owners had reacquired an asset. Recognizing the trade-off between the speed of privatization and the broadening of ownership, the Philippine government through the APT opted for speed and resorted to direct sales. As was concluded in the study, while the APT fulfilled the privatization objectives for accounts over which they had complete and full control, the objectives of privatization were only partially fulfilled for those which required others to participate.

RECENT LEGISLATION AND IMPLEMENTING GUIDELINES

Since the issuance of Proclamation 50 by President Aquino on December 8, 1986, other laws and authoritative pronouncements have been implemented which have had significant effects on the Philippine privatization program (see Box 2: Recently Passed Legislation for a brief synopsis).

Foreign Investments Act of 1991

R.A. 7042, otherwise known as the Foreign Investments Act of 1991, was signed into law by President Aquino on June 13, 1991. It sought to liberalize the foreign investment climate in the country, while maintaining specific safeguards provided for in the Constitution and other laws. It has simplified investment rules by: (1) opening all investment areas and activities to 100-percent foreign equity participation, except for those sectors/activities

Box 2

Recently Passed Legislation (as of June 30, 1993)

Title of Legislation	R.A. No.	Description
Foreign Investments by Act of 1991	R.A. 7042	Sought to promote foreign investments by simplifying investment rules and streamlining registration procedures.
Monetary Board Resolution No. 1230	MB 1230	Changed the implementation of debt swaps
An act extending the life of the COP and and the APT	R.A. 7181	Extended the COP and APT's life until August 31, 1992 and provided an option for another 16-month extension
Restating the policy of the government	EO 37	Extended the appointment of all APT staff and executives as well as restating the privatization policy of the government
Department of Energy Act	R.A. 7638	Created the Department of Energy and vested it with adequate authority
Increase in the capitalization of the National Power Corporation (NPC)	R.A. 7639	Authorized increase in capitalization by P3 billion to allow NPC to build more power–generating plants
Energy Crisis Act	R.A. 7648	Prescribed urgent related measures necessary and proper to effectively address the electric power crisis; provided President Ramos with special emergency powers
Long-term Lease for Investors Act	R.A. 7652	Allows foreign investors to lease private lands for a maximum of 75 years
Central Monetary Authority Bill	R.A. 7653	Creates an independent Central Monetary Authority (CMA) to replace the Central Bank, and formulate and implement the country's monetary policies

specified in a negative list (see Appendix I and II) and (2) further streamlining registration procedures.

Monetary Board Resolution 1230

M.B. Resolution 1230, dated November 16, 1992, changed the implementation of debt-equity swaps such that the net effect was to decrease the effective discount to the buyer. Buyers of the foreign paper could no longer exchange them for pesos (or equivalent peso-denominated assets) at their face value. Instead investors were required to participate in quarterly tender offers in which they submitted an offer to the CB to prepurchase a maximum of US$75 million of debt papers at a discount from its face value (a maximum of 38 percent discount or 62 percent of the face value).

This new monetary policy had and will have a negative effect on the privatization of the remaining assets of the APT. The cost to potential buyers considering financing a purchase through a debt-equity swap effectively increased by the amount of the discount that the investor must offer in the quarterly biddings.

Republic Act No. 7181

With this act, the life of the APT which legally expired on December 8, 1991 as stipulated in Sections 3 and 10 of Proclamation No. 50 was extended to August 31, 1992. This bill, which was passed by the legislature on December 16, 1991 and signed by President Aquino on January 17, 1992, also provided an option to the next President of the Philippines to extend this term for another sixteen months.

In addition, new conditions were set forth in the Act with regard to the implementation of privatization activities during the extension period (see Box 3: New Conditions for Implementing Privatization in R.A. 7181 for a description of these conditions).

Executive Order No. 37

Upon assuming the presidency in June 1992, President Ramos vowed to continue the economic policies of the Aquino government. He extended the appointment of all APT staff and executives and issued Executive Order No. 37 (dated December 2, 1992) which restated the privatization policy of the government. The President also directed the COP and APT to intensify their efforts to sell existing assets so as to bring in more revenues and meet government budgetary requirements. In fact, all designated disposition entities are required to submit a privatization action plan for all GOCCs and assets assigned to them, and to implement the plan within six months from approval of the COP/government. Additionally, the government is strongly encouraging privatization strategies that will access the capital markets (e.g., initial public offerings) in order to broaden the ownership base of GOCCs and transferred assets.

Box 3

New Conditions for Implementing Privatization in R.A. 7181

1. All disposition of any and all assets should be on either a cash basis (whether in a lump sum or installment basis) or Land Bank bonds.

2. Privatization and disposition activities involving the sale of assets should not cause undue dislocation of labor. All disposition entities shall submit to the COP the settlement of employee benefits in compliance with existing collective bargaining agreements and applicable labor laws.

3. The sale of transferred assets to their former owners will not be allowed unless the former owners can show documented proof from the proper government agency or court that they have not been found by final judgement to have mismanaged or diverted the resources of subject assets resulting in loss and bankruptcy. The sale price of the assets to the former owners should not be less than the original transfer price plus accrued interest, less recoveries at the time of sale.

4. In the sale of transferred assets, disposition entities should first offer at least 10 percent of the total shares for privatization to small local investors. In this regard, disposition entities should explore the possibility of requiring an Employee Stock Ownership Plan (ESOP) and public offerings in its privatization strategies. The maximum allowable investment for small local investors, other than through ESOPs or public offerings, shall be one-fourth of one percent of the total shares for privatization or P50,000, whichever amount is lower.

5. The disposition entities should include a loss recovery provision in the sale of an asset where the selling price is lower than the original transfer price less recoveries.

6. The Commission on Audit (COA) shall adopt or impose a temporary pre-audit and other such measures as necessary to correct deficiencies in the control system of the APT.

Laws Addressing the Energy Problem

To address the worsening energy crisis which began in 1990, President Ramos and the Philippine Congress collaborated on the following laws:

1. R.A. 7638 reestablished the Department of Energy which had been abolished by President Aquino because of alleged excesses under the Marcos regime. This highlighted the Ramos Administration's desire to "swiftly address the strategic problems of power and energy under a unified, consistent, and well-managed framework."
2. R.A. 7639 increased the capitalization of the National Power Corporation (NPC)—the state-owned power-generating entity—by P3 billion, allowing it to raise more funds for badly needed power plants.
3. R.A. 7648, the so-called Energy Crisis Act, gave President Ramos emergency powers to act on the worsening energy problems for one year. These powers included: (a) faster processing of environmental clearances; (b) reorganizing the NPC; (c) waiving of public bidding for power projects; (d) authority to order the Philippine Amusements and Gaming Corp. (PAGCOR), the state-owned corporation that operates casinos, to remit 10 percent of its earnings to the NPC; and (e) authority to raise NPC's rate base without the usual lengthy public hearings and consensus building from all sectors.

The Long-term Lease for Investors Act (R.A. 7652)

The 75-year Lease Law is being touted as the backstopper for the Foreign Investments Act of 1991 since the Philippine Constitution prohibits foreigners from owning land. R.A. 7652 allows foreign investors to lease private lands for a maximum of 75 years, with the following conditions: (1) the lease shall be used solely for investment purposes upon agreement of parties, and (2) the leased premises shall include areas which may reasonably be required for investments but subject to restrictions under the Agrarian Reform Law and Local Government Code.

It is envisioned that the Act, which is a variation of the Hong Kong and Anglo-Saxon leasehold system that is prevalent in North America and China, will spur development of industrial plants, housing, tourism, and agricultural real estate.

Central Monetary Authority (CMA) Bill (R.A. 7653)

The CMA bill, which was signed into law on June 14, 1993, replaced the Central Bank of the Philippines with a more independent Central Monetary Authority (Bangko Sentral ng Pilipinas). The CMA will formulate and implement the country's monetary policies through a Monetary Board (MB) that will not be affected by changes in government. The MB is composed of five full-time private sector representatives and two government members.

Another key feature of the law was the transfer of the old CB's liabilities to the national government, allowing the CMA to begin operations with a clean slate. This should allow the CMA to pursue monetary policy that is conducive to lower inflation, lower interest rates, and high economic growth.

RECOMMENDATIONS TO PUSH PRIVATIZATION FORWARD

Concentration of all Privatization Activities in One Agency

The slow progress in the privatization of GOCCs has been attributed to a lack of a "central authority in charge of privatization," limited absorptive capacity of the local capital market, as well as legal and valuation issues that were mostly brought up by the government audit agency, the Commission of Audit (COA).[6]

Thus, one suggestion is for the Philippine government to take a unified approach to privatization. APT's success in the reprivatization of nonperforming assets has not been replicated with the GOCCs, primarily because privatization of GOCCs requires a significant level of interface with other agencies that represent the government in its various roles. To cite an example, when the APT in 1987 initially tried to privatize Patranco North Express, Inc. (PNEI) which was a 100-percent government-owned bus company, it was stopped by PCGG on the grounds that PNEI was illegally acquired from the Philippine National Bank by Gregorio Araneta, former President Marcos' son-in-law (although this transaction had already been rescinded). When this case was favorably settled in APT's favor by the Sandiganbayan, the Department of Transportation and Communications (DOTC) decided to take over the bus company on the grounds that the APT was mismanaging

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[6] World Bank. 1993. The Philippines.

it. Upon its return to APT in a run-down state in 1991, the PNEI again lost market value when the Land Transportation Franchising and Regulatory Board (LTFRB) decided to award franchises to operate the PNEI's area of operations to other bus companies with newer units. Today, the PNB wants to evict PNEI from most of its terminals because it retains ownership over the land. Multiply these inter-agency incidents by the number of government entities assigned to the APT, and the result is a lot of wasted time, money, and effort, but no privatization.

With this suggestion, the Philippine government through the APT should be able to expeditiously dispose of its remaining salable assets and turn its attention to the large GOCCs (Table 3) which have not been privatized by other disposition entities.

Packaging of Vendible Assets

For the vendible assets, the APT should package several of the smaller companies within the same industry and sell them with the same effort, possibly to the same buyer. The APT would be using the same bidding rules and addressing the same group of potential buyers, and the assets would go through the bureaucratic treadmill together.

As was noted in a previous study, the salability of assets is significantly affected by environmental factors (e.g., low world prices, technological obsolescence) and government policy. Since the effects of these variables should be the same for companies within the same industry (except for the residual effect of certain

Table 3 Summary Data on Large GOCCs to be Privatized as of December 31, 1991

Company	Agency in Charge	Total Assets	Total Liabilities	Number of Employees
Petron Corp.	PNOC	42,338	27,422	0
National Steel Corp.	NDC	24,751	16,136	3,410
Philippine Associated Smelting and Refinery Corporation	NDC	18,415	17,551	1,113
Philippine Phosphate Fertilizer Corporation	NDC	10,898	9,716	1,157[a]
Semirara Coal Corporation	NDC	5,259	5,375	1,169
Luzon Integrated Services, Inc.	NDC	14	13	1,817[a]
Philippine Airlines (33 percent)	GSIS	18,227	25,006	9,899
The Manila Hotel	GSIS	484	150	1,046
Bicolandia Sugar Development Corp.	APT	270	830	874[a]
National Sugar Refineries Corp.	DA	1,651	1,647	1,613[a]
Metro Manila Transit Corporation	DOTC	628	566	1,891[a]
Total		122,935	104,412	23,989

Note: a. 1990 figure.

asset characteristics), it will be both effective and efficient for the APT to privatize on an industrywide basis.

Preparation of Industry Studies

Of the 162 assets of the APT as of June 30, 1993, 16 assets have been classified as being hard to sell because of: (1) real and contingent liabilities, which must be assumed by potential buyers of APT's equity holdings; (2) location in areas with serious peace and order problems. In certain instances, values cannot be set because appraisers are afraid to visit the site; (3) the original project feasibility study was faulty and the operations are currently not marketable on an ongoing basis; or (4) the need for a significant amount of government support and goodwill. These are mostly companies which are in extractive industries such as mining and integrated pulp and paper operations. For these APT assets, it is proposed that the APT prepare/commission industry studies. Optimal policies and procedures for sale or disposal should become obvious after the completion of these studies.

Use of Correct Market Valuations

Twenty of APT's assets are assets with "no recoverable value." These refer to companies in industries that are saddled with unfavorable environmental conditions and government policies. Thus, unless there are major changes in the world market and the country's legal framework, these APT assets are deemed to be unsalable (see Table 4).

Table 4 Vendibility of Assets

Asset Vendibility	No. of Assets
Vendible assets	47
Vendible but hard to sell assets	16
Assets subject to legal barriers	45
Assets for foreclosure	14
Assets beyond APT's control	20
Assets with no recoverable value	20
Total	162

For these assets the APT can adopt a more bottom-line realistic approach, focusing on what is realistically recoverable and not on bloated sunk costs. The statement made by the late APT Chief Executive Trustee David Sycip in 1987—"What has been stolen has been stolen; what is recoverable may be lost if the transferred assets are not speedily sold. The legislature should amend the present law for more market-based disposition schemes"—is probably more applicable now than it was then. Under Republic Act 7181, it is almost impossible to sell assets from these industries using a historical cost approach (which includes the interest, penalties, and foreign exchange devaluation effects on top of what is in some cases already a padded amount).

Thus, the Ramos Administration should work to have this law repealed or amended.

The APT should be permitted to sell assets based on current market values. Barring major environmental upheavals and/or government reversals, this would be the only way to get rid of these white elephants and their massive custodial (preventive maintenance, insurance, and security) expenses. Their sale will add to the taxable base of the area in which they are located, and possibly generate incremental employment with all the attendant social benefits and economic multiplier effects.

Establishment of a Special Court to Exclusively Handle APT Cases

Three other categories of APT assets include those with legal impediments (45 accounts), assets beyond APT's control (20 accounts), and assets for foreclosure (14 accounts). In the past, the APT utilized various extrajudicial means so as to put these assets on track, but with R.A. 7181, this is no longer permitted.

While the Supreme Court has upheld the constitutionality of APT's exemption from court injunctions provided for in Proclamation 50,[7] disgruntled bidding losers and former owners of APT assets have delayed implementation of APT dispositions by going from one government agency to another. For example, Mr. Leonardo Ty, former owner of the Associated Bank, has frustrated the awarding of the bank to the Rizal Commercial Banking

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[7] The constitutionality of APT exemptions was upheld by the Supreme Court in its decision in the case filed by Mantrusts (lessee of Bayview Hotel) against the APT.

Corporation by going to the courts, the Monetary Board, and the Securities and Exchange Commission. Having just one venue in which all APT-related cases will be decided will definitely expedite privatization of these three types of APT assets.

If the establishment of special courts does not solve the problem, then assets with legal problems should be returned to the DBP/PNB which have large legal/collection departments and are adept at such procedures. The APT should concentrate on the selling of its assets, a task in which it excels.

Policy Changes for Recent Legislation and Implementing Guidelines

The Aquino government's innovative financing options were heartily welcomed by the investing community, both domestic and foreign, and led to immediate disposal of a significant number of APT assets in its first two years of operation.

However, rather than drawing from these past rich experiences and freeing APT and prospective investors from bureaucratic morass, the legislature and the executive branch have come up with more restrictions on APT's operations. While these changes may have very strong legal bases, the opinion of privatization experts is that they will have a very strong negative effect on the privatization of APT assets. Thus, these restrictions will need to be reviewed by the Ramos Administration if privatization is to be put back on the fast track.

Review of Privatizations Scheduled for 1993

Together with the just-concluded sale of the International Corporate Bank, privatization of the following entities are expected to raise some P13.4 billion for the government in the months ahead. As mentioned earlier, funds to be raised from these big-ticket items are slated to cover the existing budget deficit. Thus there is a strong political and economic pressure to push ahead with their scheduled privatizations.

Petron Corporation

Petron Corp., a subsidiary of the Philippine National Oil Company (PNOC), was the country's largest revenue earner for 1992, and the largest of the three oil retailers in the country. The firm currently controls 40.7 percent of the domestic oil market, with the balance being shared by Pilipinas Shell Corp. and Caltex Philippines Inc.

The President recently ordered the Department of Finance to speed up the sale of 65 percent of its shares of Petron Corp. through public bidding. PNOC has named Salomon Brothers and PCI Capital Corporation as its financial advisors for Petron's privatization. The government intends to retain 35 percent of its interest in Petron to maintain a window to the oil industry.

National Steel Corporation (NSC)

The NSC privatization will be one of the largest the government will undertake. Sale of 66 percent of the company is expected to generate P10 billion, surpassing the P9 billion generated by PAL's sale.

In an attempt not to fall into the trap that PAL found itself in during its privatization, officials of NSC are considering adopting a "lock-up" period after the sale has been made. During this period, private buyers of government holdings may not be allowed to sell the shares they recently purchased. This will discourage short-term, quick-gain players and attract only strategic and long-term investors. Such investors may include raw material suppliers, equipment builders, technology firms, downstream processors, and international trading firms that engage in a substantial volume of trade in steel products.

Energy Sector Build-operate-transfer (BOT) Projects

The country's current energy crisis opened up a need for new power plants to be built on a Build-operate-transfer (BOT) scheme. President Ramos' new powers to address the crisis provide incentives for foreign contractors to enter the field.

Associated Bank

The Committee on Privatization has approved a new privatization plan for the Associated Bank that requires prospective bidders to submit a rehabilitation plan to qualify for the eventual auction of the bank. Rather than set an indicative price for the bank, the

COP opted to let the bidders set the price.[8] This should attract more bidders for the bank.

The Manila Hotel

Cesar N. Sarino, Manila Hotel president and chief executive officer and concurrent Government Service Insurance System (GSIS) general manager, expects the sale of the Manila Hotel to occur by the end of 1993. Mr. Sarino claims that of all of the Government Service Insurance System's investments (it owns 60 percent of the hotel), the Manila Hotel offers the highest returns with yields as high as 25 percent per annum. The hotel has consistently been rated as one of the top ten five-star hotels in the world by international travel and tourism associations and publications.

Bases Conversion Development Authority (BCDA)/
Subic Bay Metropolitan Authority (SBMA)

In a development plan for Clark Air Base, the former U.S. air station will be converted into a major international civil aviation complex and a modern industrial site. Specifically, the BCDA plans to convert Clark into a modern cargo and industrial hub for regional distribution. Clark will be proclaimed as a special economic zone that will provide special incentives to local and foreign investors.

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[8] However, the government wanted to peg the minimum bid price at P671 million, the amount "transferred" to the government by DBP in 1986.

For Camp John Hay, the BCDA plans to form a new company—i.e., the John Hay Development Corporation—to oversee the privatization of portions of this former American facility. The major components of the privatization program are the lease of 4.28 hectares of land to house a 250-room deluxe hotel and a long-term lease of another property for a golf course.

For the former U.S. naval base at Subic Bay, the government created the Subic Bay Metropolitan Authority with former Olongapo City Mayor Richard Gordon as chairman and administrator. The SBMA has been asked to develop the Subic Bay Special Economic and Freeport Zone. The Subic Bay Freeport boasts of US$8 billion worth of infrastructure including an airport, berths, an internal road network, large fuel storage, public utilities, buildings, and residential areas with community facilities. The SBF also has a pool of over 20,000 highly skilled workers that were displaced by the withdrawal of the U.S. Navy. These workers are English-speaking and are familiar with the production-oriented, Western style of management.

PENDING LEGISLATION

As summarized in Table 5, there is pending legislation that is expected to lead to more foreign investments and trade opportunities in the near future.

Table 5 Pending Legislation as of October 15, 1993

Bill No.	Description	Status
H.B. 8391	Provides for a six-year public works and infrastructure program	Pending in the Senate
H.B. 8226/ S.B. 839	Seeks to liberalize the entry and scope of operations of foreign banks	Approved on second reading
H.B. 4656	Magna Carta for long-term savings	Next session
H.B. 362/ S.B. 397	Seeks suspension of nationality requirement for multinational financial institution	Pending in committee
S.B. 355	Amending the concept of condominium to include factories and plants	Pending in committee

Six-year Public Works and Highways Infrastructure Program (H.B. 8391)

H.B. 8391 embodies a multiyear funding project (until 1998) for the development of communications facilities; arterial highways; local and national roads; major bridges, including elevated highways; water conservation; and flood control projects. Completion of these projects is expected to attract foreign investors now concerned about the lack of infrastructure in the country.

Liberalization of the Entry and Scope of Foreign Banks

H.B. 8226 seeks to liberalize the entry and scope of operations of foreign banks in the country. This should lead to increased business lending and lower interest rates. The entry of more banks should also be an additional source of funds to finance future privatizations.

Magna Carta for Long-term Savings

H.B. 4656 seeks to provide more incentives for long-term savings. This should lead to more long-term resources to finance the country's capital investment needs as well as provide a domestic counterpart to funds to finance privatizations/foreign direct investments.

Suspension of Nationality Requirement for Multilateral Financial Institutions (S.B. 387 and H.B. 362)

These bills seek to amend Article 7 (13) of the Omnibus Investments Code of 1987. Regional ASEAN and multilateral financial institutions, such as the International Finance Corp. (IFC) and the Asian Development Bank (ADB), are presently considered "foreign" and are constrained by the 40-percent maximum equity requirement in financing development projects. If passed, these bills will allow a window for an additional 40 percent investment from foreign sources.

Amending the Concept of Condominiums

Presently, foreigners can own units in a condominium up to 100 percent equity, but can only own up to 40 percent of factories and plants. This bill will change this ruling and allow foreign investors to own 100 percent of their factories and plants. Together with the 75-year land lease law, this should be a strong incentive for investors to relocate their factories and plants to the Philippines.

IMPLICATIONS OF THE PENDING PRIVATIZATIONS AND LEGISLATION: OPPORTUNITIES FOR FOREIGN INVESTORS AND FIRMS

The privatization scheduled to take place in the near future and the legislation that is in the process of being passed suggest a number of entry points for foreign investors or firms interested in participating in the Philippine Privatization Program.

Most apparent is the need for financial and technical advisors to assist in the privatization. More and more of the privatizations relate to large and complex transactions that require multi-disciplinary teams of advisors capable of coming up with and implementing Privatization Action Plans (PAP). In the case of Petron and National Steel, consortiums that include foreign financial advisors and industry consultants have been awarded contracts to prepare and implement PAPs.

Second, because of the increasingly large amount of funds required in the upcoming privatizations and the "limited absorptive capacity" of the local capital markets, very few local investors can afford to purchase companies that are up for privatization on their own. Thus, real investment opportunities exist for foreign investor companies that are interested in a quick start-up with local partners.

A third avenue through which foreign investors can participate in the Philippine Privatization Program is to serve as a technical or strategic partner. The case of the Philippine Airlines proved the old saying, "money is not everything," to be true. While a consortium including some of the major firms in the country was able to come up with a winning bid of close to P10 billion, this has not led to a quick turnaround for PAL's operations. The missing ingredient appears to be a partner that is knowledgeable about the operations of an international airline with extensive but marginal domestic routes. The concept of a strategic partner being involved from the very beginning is incorporated in the Petron, National Steel, and Manila Hotel privatizations.

Lastly, foreign investors can play a significant part in the privatizations as stockholders of funds taking a position in the Philippine stock market. The Philippine stock market has been giving impressive returns for the past few years. Up to the limits of the Philippine Constitution and the Foreign Investments Act (see Appendix I), individual foreign investors may participate in the upcoming Philippine privatizations through Philippine country funds (e.g., the NYSE Philippine Fund) or directly through purchases of "B" shares in the local bourse.

Appendix I

Foreign Investment Negative List During the Transitory Period
(Pursuant to R.A. No. 7042)

List A: Foreign ownership is limited by mandate of the Constitution and specific laws

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No foreign equity

1. Mass media (Article XVI, Section 11 of Constitution)
2. Services involving the practice of licensed profession (See Appendix for detailing listing)
3. Retail trade (Republic Act No. 1180)
4. Cooperatives (Republic Act No. 6938)
5. Private security agencies (Republic Act No. 5487)
6. Small-scale mining (Republic Act No. 7076)
7. Utilization of marine resources (except deep sea fishing)
8. Engaging in the rice and corn industry except as authorized by NFA (Republic Act No. 3018; Presidential Decree No. 194)

Up to twenty-five percent (25%) foreign equity

9. Private recruitment, whether for local or overseas employment (Article 27 of the Labor Code)

Up to thirty percent (30%) foreign equity

10. Advertising (Article XVI, Section 11 of the Constitution)

Up to forty percent (40%) foreign equity

11. Exploration, development, and utilization of natural resources
12. Ownership of private lands (Article XII, Section 7 of the Constitution)
13. Operation and management of public utilities (Article XII, Section 11 of the Constitution; Commonwealth Act No. 146)
14. Ownership/establishment of educational institutions requiring authorization of DECS (Article XIV, Section 4 of the Constitution)
15. Financing companies regulated by SEC (Republic Act No. 5980)

Varying foreign equity limitation

16. Construction (see Appendix for detailed listing)

Note: Full foreign participation is allowed through a financial or technical assistance agreement with the President (Article XII, Section 2 of the Constitution).

List B: Foreign ownership is limited for reasons of security, defense, risk to health and morals, and protection of local small and medium-scale enterprises

Up to forty percent (40%) foreign equity

1. Manufacture, repair, storage, and/or distribution of firearms, ammunition, lethal weapons, military ordnance, explosives, pyrotechnics, and parts, peripherals, and ingredients used in the manufacture thereof (Republic Act No. 7042)
2. Manufacture and distribution of dangerous drugs (Republic Act No. 7042)
3. Sauna and steam bath houses, massage clinics, and other like activities regulated by law because of risks they may impose to public health and morals (Republic Act No. 7042)
4. Other forms of gambling, e.g., race track operation, racehorse ownership/importation (Republic Act No. 7042)
5. Domestic market enterprises with paid-in equity capital of less than the equivalent of $500,000 unless they involve advance technology (Republic Act No. 7042)
6. Export enterprises which utilize raw materials from depleting natural resources, and with paid-in equity capital of less than the equivalent of $500,000 (Article XII, Section 2 of the Constitution; Republic Act No. 7042)

List C: Other areas covered by R.A. 7042 and other legislation, administrative regulations, and practices

No foreign equity

1. Ownership, operation and management of cockpit and cockfighting activities (Rules and Regulations to Implement PD 1802)

Up to forty percent (40%) foreign equity

2. Import and wholesale activities not integrated with production or manufacture of goods (Republic Act No. 7042)
3. Services requiring a license or specific authorization, and subject to continuing regulation by national government agencies other than the BOI and SEC which at the time of the effectivity of RA 7042 are restricted to Philippine nationals by existing administrative regulations and practices of regulatory agencies concerned, e.g., travel agencies, tourist lodging services (pension houses and tourist inns), and convention and conference organizers, life and nonlife insurance businesses including professional reinsurance services and insurance brokerage (Republic Act No. 7042)
4. Enterprises owned in the majority by a foreign licensor and/or its affiliates for the assembly, processing, or manufacture of goods for the domestic market which are produced by a Philippine national as of the date of the

effectivity of RA 7042 under a technology, know-how, and/or brand name license from such a licensor during the term of the license agreement (Republic Act No. 7042)

Note: This does not include banking and other financial institutions as they are governed and regulated by the General Banking Act and other laws under the supervision of the CBP.

Appendix II
Foreign Investment Negative List During the Transitory Period

Activity		Foreign Equity Limitation
1.	Licensed professions covered under List A.2	0%
	a. Engineering	
	b. Medical and allied professionals	
	c. Accountancy	
	d. Architecture	
	e. Criminology	
	f. Chemistry	
	g. Customs broker	
	h. Forestry	
	i. Geology	
	j. Marine deck officer	
	k. Marine engine officer	
	l. Master plumber	
	m. Sugar technology	
	n. Social work	
	o. Librarian	
	p. Law	
2.	Activities Covered under List A.15	
	a. Contracts of the construction and repair of locally-funded public works (C.A. 541 as amended by PD 1594; Letter of Instruction No. 630)	25%
	b. Contracts for the supply of materials, goods, and commodities to a government-owned or -controlled corporation, company, agency, or municipal corporation (Republic Act No. 5183)	40%
	c. Private domestic and overseas construction (Republic Act No. 4566 as amended by Republic Act No. 6957)	40%
	d. Contracts for the construction of defense-related structures (e.g., land, air, sea and coastal defenses, arsenals, barracks, depots, hangars, landing fields, quarters, hospitals) (Commonwealth Act No. 541)	40%
	e. Construction of public utilities (Republic Act No. 6957)	40%

3. Investment areas/activities under List B.1 requiring PNP clearance 40%

   a. Firearms (handguns to shotguns), parts of firearms and ammunition therefore, instruments or implements used or intended to be used in the manufacture of firearms
   b. Gunpowder
   c. Dynamite
   d. Blasting supplies
   e. Ingredients used in making explosives: Chlorates of potassium and sodium; Nitrates of ammonium, potassium, sodium, barium, copper (11), lead (11), calcium and cuprite; nitric acid, nitrocellulose, perchlorates of ammonium, potassium and sodium; dinitrocellulose; glycerol, amorphous phosphorous; hydrogen peroxide; strontium nitrate powder; toluene
   f. Telescopic sights, sniperscope, and other similar devices

4. Products covered under List B.1 requiring DND clearance

   a. Guns and ammunition for warfare
   b. Nuclear weapons and ordnance
   c. Military ordnance and parts thereof (e.g., torpedoes, mines, depthcharges, bombs, grenades, missiles)
   d. Gunnery, bombing, and fire control systems and components
   e. Guided missiles/missiles systems and components
   f. Tactical aircraft (fixed and rotary winged), components and parts thereof
   g. Space vehicles and components systems
   h. Combat vessels (air, land, naval) and auxiliaries
   i. Weapons repair and maintenance equipment
   j. Military communications equipment
   k. Night vision equipment
   l. Stimulated coherent radiation devices, components and accessories
   m. Biological warfare components
   n. Armament training devices

SOURCES

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Table 2	Ibid.
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Table 4	First Regular Session of the House of Representatives, 9th Congress. 1993. Speech of Speaker Jose De Venecia, Jr., June 10.
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