AN ANALYSIS OF THE PHILIPPINE ECONOMIC CRISIS

Edited by Emmanuel S. De Dios

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A WORKSHOP REPORT

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PREFACE

The following report embodies the results of a series of workshops on the present economic crisis, held between November 1983 and May 1984, in which interested faculty members of the University of the Philippines School of Economics participated. The preparation of this report was coordinated by Rosa Linda P. Tidalgo. Its publication was supervised by Manuel F. Montes.

Discussions held with Professors Felipe B. Miranda and Temario C. Rivera of the U.P. College of Social Sciences and Philosophy, Mr. Christian S. Monsod, and other faculty members of the School of Economics, proved helpful. However, the views and assessments expressed in this report are the sole responsibility of the workshop participants.

The participants finally wish to thank the following for their support: Aleli dela Paz, Evelina Mariano, Ellen Payongayong, Christine Peña and Ma. Liza Tanchico for research assistance; Regina Madriaga for editorial work; Rosemarie Rosali for providing the bibliographic citation; and Magdalena Diaz, Isagani Inovero, Cynthia Ladrazo, Ernesto Razon, Jr., Gilda Rojas, Brando Saulo, and Wilma Solidor for reproduction of the draft.

1 INTRODUCTION

At this time when our people's attention is focused on political matters, we consider it most urgent to review the history and current state of the economy. We believe a frank and factual public discussion of our economic troubles is indispensable. For unless the most important economic issues are squarely confronted, the outcomes of recent and forthcoming political contests would hardly be of any consequence to the daily lives of the majority.

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The organization of the economy, the direction it is taking, its system of rewards and punishments, the legal and moral shell that surrounds it—these are issues that have to be addressed not only by the present government but also by a future one which hopes to supplant it. But what is more important, in our view, is that our countrymen attain such a degree of understanding of economic affairs that they are able to take part effectively in the formation of social decisions in the light of their best interests.

In the following pages are assembled both arguments and evidence, though at times fragmentary, which attempt to answer: what we believe to be the history of the present crisis (Chapter 2); what the underlying causes of the crisis are (Chapter 3); and what we think would be judicious alternatives for our country to take (Chapter 4). One of our basic contentions is that, contrary to what some may suppose, the making of public policy in this country suffers from taking too little—not too much—account of basic, standard economics. Many of these sections were originally written independently by the participants, and modified in a series of workshops held from November 1983 to May 1984. There are differences among us, as must be expected of any group of independent researchers. We feel, however, that the things on which we agree are far more numerous and important than those which divide us.

We have tried to approach this task with the same regard for objectivity and thoroughness as we would have were we writing an academic brief, although with an eye for a wider readership. None of us are politicians, and we have tried to talk of systems rather than persons, of trends rather than events, of behavior rather than motives. The report does not adhere strictly to the tradition of specialization among social scientists. We have chosen to include discussions of politics and institutions where these are deemed needed for a sensible social explanation of economic trends. We are aware that, in doing so, we open ourselves to the charge of speaking beyond the scope of our expertise. Such objections, however, we consider minor, compared to the urgency of a fuller explanation and argument. Even in making evaluations of political and institutional phenomena, we have tried to apply the tools of economic analysis as far as possible, though of course, our efforts will at best seem tentative and incomplete. For the rest we shall leave the elaboration to practitioners in these other fields of social science who will be better equipped to do so. The method that has guided us was well put by one writer who said, "I have tried to be objective; I do not claim to be detached."

2 AN OVERVIEW OF THE PRESENT ECONOMIC CRISIS

2.1 The History of the Present Crisis

Different and often competing explanations have been put forward for the occurrence of the country's economic debacle, among which are, that:

(1) it was entirely or primarily due to external circumstances affecting all developing countries, and over which the present leadership had no control;
(2) it was entirely or primarily due to mismanagement by the present regime;
(3) it was entirely or primarily due to an unforeseen random event which was the assassination of Aquino in August 1983.

While there is some truth to each of these, none of them is a sufficient explanation by itself.

The conclusion reached in this report is that . . . the major explanation (for the crisis) must lie in the character of economic policies and of policy-making by the leadership.

The conclusion reached in this report is that, while external difficulties were certainly a necessary condition for the present crisis, the major explanation for its occurrence must lie in the character of economic policies and of policymaking by the leadership. The Aquino assassination, on the other hand, simply tore through the already-weakened fabric of the economy. Furthermore, the pursuit of policies which led to the crisis would seem to be closely linked to political imperatives suggesting that the leadership would be able to abandon them only with great difficulty.

2.1.1 External Factors

As a middle-income developing country, the Philippines shares many economic characteristics with others in the same category. These common traits undoubtedly represent limits which any leadership, however well-intentioned or reform-oriented, cannot push out too far within a specified period of time. The level of technology, natural resources, the amount of skills possessed by the labor-force, the level of growth of the population, the level of domestic savings in proportion to income, etc. can in general be altered only gradually (say, within a decade) and within certain limits, although rapid changes are not unknown in societies undergoing wars and revolutions.

One historically determined characteristic of many less-developed countries such as the Philippines is their vulnerability to fluctuations in incomes, prices and to changes in policy in the more developed countries.

One historically determined characteristic of many less-developed countries such as the Philippines is their vulnerability to fluctuations in incomes, prices and to changes in policy in the more developed countries. This is due to the large role of trade in the less-developed economies; for the Philippines, trade (exports plus imports) accounts for almost half of gross domestic product (GDP). The recession in the developed economies in 1974-1975 and then again in 1980-1982 cut back employment and incomes in those economies and accordingly meant slower demand, hence, lower prices for the more important exports of the Philippines such as sugar, coconut, and copper concentrates. Tariff and nontariff barriers (e.g., quotas, health and safety specifications) were also imposed on some nontraditional exports, as the developed countries sought to protect jobs and incomes in their receding industries from developing-country exports. In addition to the recession in the developed countries, the two successive increases in the world-price of oil (1973 and 1978) raised the price of oil sixteen times over. For the Philippines, which was, and still is, dependent on oil for most of its energy needs, this meant an increase in the oil-import bill from $187 million in 1973, $651 million in 1974 and $2,078 million in 1982, though the volume had decreased in physical terms. As a result of these factors, the so-called price or barter terms of trade (i.e., the ratio of export prices to import prices) declined from 100 in 1972 to 55.6 in 1982. This meant that in 1982 the country had to export roughly twice the volume of products it did in 1972 in order to obtain the same volume of imports. Despite the deterioration in the terms of trade, however, exports were still able to finance an increasing amount of imports, since the increase in export-volumes more than compensated for the decline in unit-values.

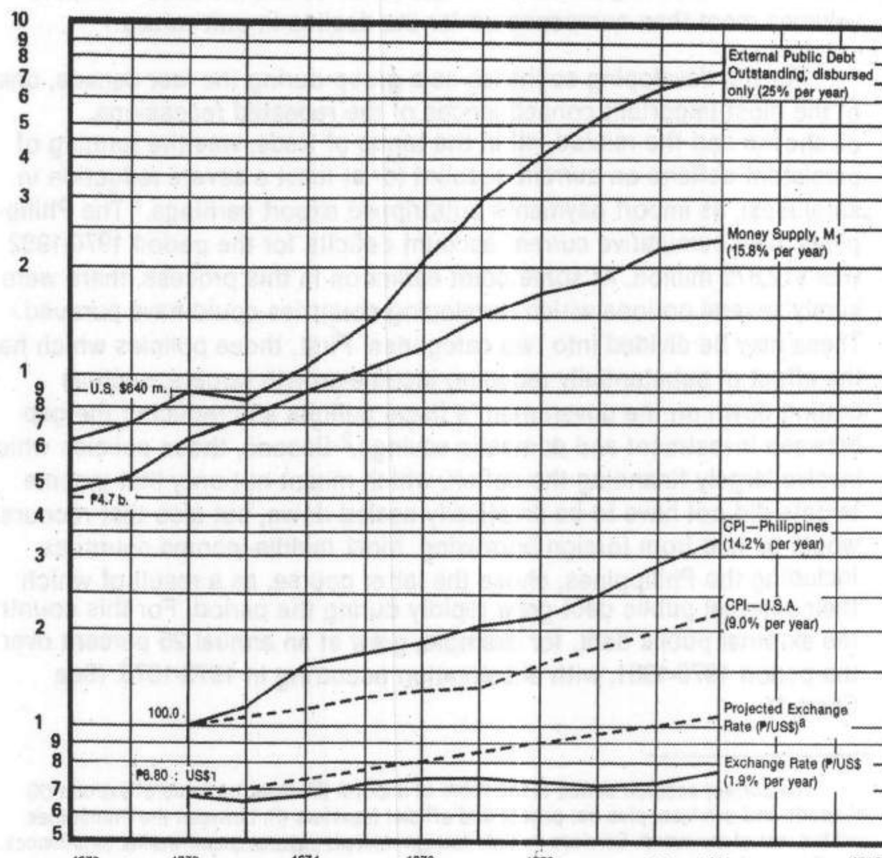
For the developing countries as a group during the last decade, one of the most important consequences of the repeated recessions, oil-shocks and the related fall in the terms of trade, was the running of persistent deficits on current account (or at least a severe reduction in surpluses), as import payments outstripped export earnings.[1] The Philippines' own cumulative current account deficits for the period 1970-1982 was $12,876 million. At some point earlier on in this process, there were surely several options which developing countries could have pursued. These may be divided into two categories. First, those policies which had the effect of substantially reducing income-growth targets, such as cutting down on the government's fiscal deficits and reducing the gap between investment and domestic savings.[2] Second, those policies which involve largely financing the deficit, which meant not only that income targets did not have to be drastically scaled down, but also that recourse would be had from foreign borrowing. Most middle-income countries, including the Philippines, chose the latter course, as a result of which their external public debt grew rapidly during the period. For this country the external public debt, for example, grew at an annual 25 percent over the period 1970-1981, with acceleration occurring in 1973-1976. (See Chart 1).

[1] The *current account deficit* is the value of imports (M) less the value of exports (X) of goods and services, plus net private and official transfers (R) between the Philippines and the rest of the world. Services include foreign interest payments and worker remittances.

[2] It is true as an accounting identity that the *trade deficit* $(M-X)$ is equal to government expenditures (G), less government revenues (T), plus investment (I), less domestic savings (S). That is, $M-X=(G-T)+(I-S)$, or the trade deficit is equal to the government deficit $(G-T)$, plus the investment-savings gap $(I-S)$. Adding net public and private transfers (R) to both sides yields the current account deficit $(M-X+R)$ as being equal to $(G-T)+(I-S)+R$. In effect, by choosing or influencing the government deficit and the investment-savings gap, the authorities may decide how much of a current account deficit to allow.

The option to finance current account deficits bears some brief explanation. During the period covered by the two oil-price shocks (1973-1974, 1979-1980), the surpluses earned by the oil-exporting countries eventually became deposited in large commercial banks, which then "recycled" the funds by lending them out. On the other hand, there were many middle-income countries, whose previous growth performance made them appear to be good credit risks, in dire need of funds precisely to cover their current account deficits. The interest rates charged, especially after deducting for inflation, were low, even negative between 1974 and 1978 (See Section 3.2, p. 56). Hence, the inducement to borrow

Chart 1
PHILIPPINES: EXTERNAL PUBLIC DEBT, MONEY SUPPLY, PRICES AND EXCHANGE RATES
1970 to 1981



Notes: (1) The slopes of the curves on this semi-log graph represent growth rates.
(2) Average annual growth rates are in parentheses.
(3) aExchange rate adjusted for the differential between Philippine CPI and US CPI. Projected exchange rate in 1981 is ₱10.50:$1. which is 33% higher than the official rate.

Sources: *Key Indicators of Developing Member Countries of ADB* (April 1983).

was obvious and understandable. In addition the sustenance of a high growth rate seemed the more politically expedient path for those countries where the highly unequal income distribution could be mitigated only by absolute increases in real income for all. A flagging down of the growth rate might have meant increased social tensions in those countries, especially those where the existence of authoritarian regimes had been legitimized by appeals to supposed enhancement of economic prospects.[3]

A flagging down of the growth rate might have meant increased social tensions in those countries, especially those where the regimes had been legitimized by appeals to supposed enhancement of economic prospects.

Table 1 presents a comparison of total external debt for some prominent developing-country borrowers, together with the percentage of the total debt that originated from commercial sources. In general it will be noted that the fast-growers during the decade were also the heaviest borrowers, as well as those with the largest component of commercial debt. These include countries which have since encountered some debt problems or other, e.g., Mexico, Brazil, Argentina, and the Philippines. On the other hand, one will note that there are some countries which were heavier borrowers than the Philippines, and/or had a larger proportion of commercial debt, which have not, to date, encountered a debt crisis, examples of which would be South Korea, Indonesia, and Venezuela.

Table 1

TOTAL EXTERNAL DEBT FOR SELECTED COUNTRIES, 1983

	Total Debt ($B)	Commercial Debt ($B)	Commercial Debt as Percent of Total Debt
1. Argentina[a]	43.6	27.0	62
2. Brazil[a]	93.0	68.0	73
3. Chile	17.9	11.8	66
4. Indonesia	25.0	14.0	56
5. Mexico[a]	89.0	70.0	79
6. Nigeria	15.0	5.0	33
7. Philippines[a]	24.6	15.2	62
8. Poland[a]	28.0	11.0	39
9. South Korea	40.0	25.9	65
10. Turkey	18.3	3.8	21
11. Venezuela	34.0	28.0	82
12. Yugoslavia	25.5	10.2	40

[a] External debt rescheduling requested.

Source: *United Daily News*, April 5, 1984.

[3] As a corollary, of course, the targeted income growth rate might have been scaled down without engendering social tensions if income redistribution had been possible. However, such a possibility was hardly to be considered by regimes whose main support came from dominant economic interests.

The same question is raised by the data in Table 2, Column 1, where external public debt divided by gross national product (GNP), to allow comparisons across countries, is shown for selected countries in East, Southeast, and South Asia. On the average, Southeast Asia, to which the Philippines belongs, has a lower public debt-GNP ratio than the South Asian countries, but has a higher ratio than the East Asian group. The reason for this may be found in columns 2 and 3 of the same table, which show that East Asian countries were running government surpluses on the average throughout the decade, and had a savings-investment gap only marginally higher than the Southeast Asian nations. This, together with greater inflows of direct foreign investment, obviated the need for further financing.[4] The same reference to columns 2 and 3 would explain the difference in debt-GNP ratio between the South and Southeast Asian groups.

That these other countries have not had to ask for a debt-rescheduling while the Philippines has, calls for some explanation.

Focusing on the Philippines, one finds that its public debt-GNP ratio is lower than South Korea's, Malaysia's, Bangladesh's, Sri Lanka's and Burma's. That these other countries have not had to ask for a debt-rescheduling or moratorium while the Philippines has, calls for some explanation. In the case of the South Asian countries, the public debt is likely to have been less burdensome than the high ratios suggest, since much of it is official and concessional in nature. On the other hand, the governments of many East and Southeast Asian countries could and did participate in the commercial loan markets heavily, e.g., South Korea, Malaysia, and Indonesia. South Korea has performed more creditably than the Philippines, despite the fact that it had a higher public debt-income ratio, had larger investment-savings gaps, and larger current account deficits. The reason is that since the 1960s it had developed a group of very efficient labor-intensive industries which continued to export throughout the 1970s and the previous recession, quite unlike the Latin American countries and the Philippines. Malaysia, on the other hand, also had a higher public debt-GNP ratio, but managed to keep an average positive current account balance for the decade by running surpluses of savings over investment, and trimming down government deficits. Again there were specific reasons for this, in that Malaysia had oil resources, a well-developed agriculture and labor-intensive export-industries. Of course, Indonesia's immense oil resources are also well-known.

It might be said, however, that the comparison between the Philippines and these other countries is a bit unfair, since our country has no oil resources to speak of and was a late-starter in the drive for labor-intensive exports. In this case, then, the comparison with Thailand becomes inevitable. Among all Asian countries, Thailand is most similar to the Philippines in level of economic development, population, and natural endowments. Like the Philippines, it has no oil resources and for long pursued an

[4] Except for South Korea, which ran large government and savings gaps, and thus resorted heavily to foreign borrowing.

industrialization strategy of import-substitution. What is puzzling is that throughout the 1970s, Thailand had to close larger investment gaps, government deficits, and current account deficits than the Philippines; yet by 1982 its public debt-GNP ratio was smaller than that of the Philippines. The conclusion is inescapable that, compared to the Philippines, Thailand has relied much less on foreign financing in responding to external shocks. To put it another way, while both Thailand and the Philippines faced the same external shocks and the same easy opportunities for financing their deficits, the Philippine government seemed to have been more eager and ready to incur foreign debt.

The conclusion is inescapable that, compared to the Philippines, Thailand has relied much less on foreign financing in responding to external shocks.

Table 2

CROSS-COUNTRY COMPARISONS OF EXTERNAL DEBT, INVESTMENT GAPS, GOVERNMENT DEFICITS AND CURRENT ACCOUNT BALANCES (As Percent of GNP)

		Annual Average for the 1970s		
REGION / COUNTRY	1982 External Public Debt Outstanding[a]	Surplus (Deficit) of National Saving Over Domestic Investment	Surplus (Deficit) of Government	Current Account Balance
East Asia	12.9	-2.7	1.0	-5.7
Taiwan	10.0[b]	1.6	1.8	3.9
S. Korea	30.4	-4.3	-0.8	-5.1
Hongkong	1.0	1.7	2.2	—
Singapore	10.0	-9.6	0.8	-16.0
Southeast Asia	22.9	-2.3	-2.2	-1.6
Malaysia	31.0	0.8	-0.7	0.8
Thailand	17.1	-4.6	-2.6	-3.3
Philippines	22.5	-3.1	-1.4	-2.2
Indonesia	21.1	-2.2	-4.2	-1.6
South Asia	26.9	-4.1	-4.6	-2.0
Bangladesh	38.7	-6.3	-6.7	-3.7
Burma	33.2	-2.2	-0.1	-2.6
India	12.1	-2.2	-2.9	0.03
Sri Lanka	38.9	-5.7	-9.2	-1.6
Nepal	11.6	-3.9	-4.2	—

[a] Data excluding short-term non-guaranteed private debt. IBRD World Debt Tables 1983-1984 gives the total amount of 1982 Philippine long and medium debt as $12 billion. Of the $25 billion total debt in 1983, more than one half ($13 billion) are short-term private non-guaranteed debt.

[b] 1980

Source: *Key Indicators of Developing Member Countries of ADB* (April 1983).

It has often been argued, in defense of the country's borrowing programme, that if the foreign indebtedness had been smaller the country would have paid through a reduction in its growth rate. Or, in another context, it has been asserted that, unlike the Philippines, other

Table 3
GROWTH RATES OF GDP PER CAPITA IN ASIAN COUNTRIES, 1950 TO 1980
(Geometric rates in percent per year)

	1950-60	1960-70	1970-80	1950-80
East Asia Simple average	4.6	7.5	5.9	5.9
Pop. weighted average	5.1	7.9	4.3	5.6
1980 & GDP weighted average	6.1	9.4	4.4	6.5
Japan	6.6	10.1	4.1	6.9
China[a]	5.0[b]	7.8[c]	4.1	5.4[d]
South Korea	3.1	6.0	8.0	5.7
Taiwan	4.0	6.3	6.7	5.7
Hongkong	4.5	7.2	6.4	6.0
Southeast Asia Simple average	2.1	3.8	5.4	4.0
Pop. weighted average	2.3	2.8	5.2	3.5
1980 & GDP weighted average	2.3	3.1	5.2	3.7
Malaysia	1.0	3.3	5.3	3.2
Thailand	2.8	4.7	5.1	4.2
Indonesia	1.9	2.3	5.7	3.3
Singapore	1.3[e]	6.7	7.7	6.2[f]
Philippines	3.6	2.2	3.4	3.1
South Asia[g] Simple average	2.2	1.5	1.1	1.5
Pop. weighted average	2.0	2.0	1.1	1.7
1980 & GDP weighted average	2.0	2.1	1.2	1.7
India	1.9	2.2	1.2	1.8
Bangladesh	—	1.1	0.3	0.7[f]
Burma	4.3	1.2	1.2	2.2
Sri Lanka	1.3	2.5	2.3	2.0
Nepal	1.2	0.4	0.4	0.7

[a] Net material product per capita

[b] 1949-1962

[c] 1962-1970

[d] 1949-1980

[e] 1956-1960

[f] 1956-1980

[g] Pakistan is not included in South Asia because it does not belong to Monsoon Asia. Chinese figures in this and other tables may be revised when the population and employment data from the 1982 Census (the first modern population census for China) are completely tabulated.

Source: H. Oshima, "Sector Sources of Philippine Postwar Growth," *Journal of Philippine Development*, 1st Semester, 1983.

Asian countries have avoided a debt-rescheduling only because they have had to content themselves with lower growth. However, such arguments are not obvious from the facts. Table 3 shows growth rates of per capita gross domestic product in some Asian countries for three decades. It confirms what is already a stylized fact, namely that the countries of East Asia, on the average, grew more rapidly over the period 1950-1980 than the countries of Southeast Asia, but that the latter grew faster than South Asia for the same period. Among the Southeast Asian countries, however, the Philippines registered the lowest per capita GDP growth rates over the last three decades (an annual rate of 3.1 percent in 1950-1980, as against the subregional average of 4.0 percent). While the Philippines started with the highest growth rates for the subregion in 1950-1960 (3.6 percent annually), it lagged behind its neighbors in 1960-1970, growing only at 2.2 percent while the subregional average was 3.8 percent. The gap widened further in 1970-1980, when the country grew only at 3.4 percent yearly while the subregion was growing at 5.4 percent. In particular, the Philippines was doing much more poorly than Thailand, which was growing at 5.1 percent. Hence, going by comparisons across countries, it cannot be maintained that slow growth is the necessary consequence of low indebtedness.

Hence, going by comparisons across countries, it cannot be maintained that slow growth is the necessary consequence of low indebtedness.

All the foregoing suggest that, while it is useful at some level of analysis to treat developing countries as if they were an undifferentiated whole, and while it is true that they have numerous common problems, it becomes necessary at some point to distinguish the peculiarities of the economic policies of each country, especially if one is to explain a concrete historical event.

2.1.2 Internal Factors

An important question that must be answered, therefore, is why Philippine economic growth has slowed relative to that of its neighbors. To answer it really involves inquiring into society's internal political and economic structure For we have seen that, while the Philippines experienced more or less the same external shocks as other developing countries, there is a residual variation in its performance and response which makes it fall below the average for countries in its class. To explain this "residual," one can no longer appeal to the influence of external shocks—which have been averaged out—but must look into internal political and economic arrangements.

An important question that must be answered, therefore, is why Philippine economic growth has slowed relative to that of its neighbors.

The sequence of events culminating in the present debt crisis may be traced to the late 1960s, which also broadly coincides with the accession to power of the present government. (Chart 1 and Table 4 are referred to in the following discussion.)

The periods previous to 1956-1960 were characterized by moderate economic growth, as the country attempted to recoup its losses in the last war, and new manufacturing enterprises were established under a regime of import-substitution[5] through quantitative controls on imports and foreign exchange. Eventually, however, income growth began to peter out as the import-substitution programme encountered increasing difficulties,[6] so that beginning 1962 it was in the process of being dismantled, with the abandonment of foreign exchange controls and the devaluation of the peso under the Macapagal administration. The years under the Marcos administration saw the continuation of the process that shifted the emphasis of trade and development strategy from one of import-substitution towards an increasing commitment to export-promotion.

Much has been written attributing the differences in the growth performance of countries to their adoption of different trade strategies, e.g., either outward- or inward-looking, etc. In the case of the Philippines, what were initially considered high growth rates in the 1970s were attributed to the Marcos administration's greater acceptance of the virtues of export-promotion. With the same assumption in mind, some critics of the present regime attribute the present economic failure to the pursuit of the same export-promoting strategy. Although cognizant of many potential problems in the implementation of an "outward-looking" strategy,[7] we do not share the view that it alone is sufficient to explain the crisis, or otherwise it should primarily have been the export-oriented economies of East and Southeast Asia which faced debt crises, rather than the more inward-looking economies of Latin America. But this is obviously not the case.

. . . we argue that the main characteristic distinguishing the Marcos years from other periods in our economic history has been the trend towards the concentration of power in the hands of the government. . . .

Without belittling the importance of trade policies, we argue that the main characteristic distinguishing the Marcos years from other periods in our economic history has been the trend towards the concentration of power in the hands of the government, and the use of governmental functions to dispense economic privileges to some small factions in the private sector. In turn, this sufficiently explains the more outward

[5] In particular the import- and foreign-exchange restrictions effectively penalized exporters, thus discouraging an expansion of the export sector. This had severe consequences on the strategy, since the new import-substituting industries themselves were import-dependent for their inputs, relying on the earnings of the export sector for a continuing supply of these materials. At the same time, further stages of import-substitution (e.g., substitution for imported inputs and capital goods) could not be achieved owing to the narrowness of the domestic market. The latter condition was aggravated by severe inequalities in income and wealth, which the import-substituting strategy itself reinforced.

[6] See, for example, Power and Sicat (1971), Baldwin (1975), and Bautista, Power, et al. (1981).

[7] In theory the so-called "export-promoting" strategy necessitates the adoption of an unbiased price structure, implying the need to adopt exchange rate flexibility, abandonment of quantitative restrictions on imports and foreign exchange, and a more uniform, generally lower, tariff structure. In practice, however, many countries adopt a positive *bias* for exports through various fiscal incentives, investment in infrastructure, and legislation which erodes the social support for labor. While the Philippine government was verbally committed to an "export-oriented" strategy, there are indications that such strategy was never fully implemented as witness the overvalued currency for most of the 70s.

manifestations which have disturbed many observers of the recent economic scene, namely, (a) the generally expansionist fiscal and monetary policies over the past two decades; (b) the increasing role of the government in markets for products and financial assets; and (c) the trend towards a monopolistic structure in important sectors of the economy.

Table 4

SELECTED ECONOMIC DATA ON THE PHILIPPINES, 1950 TO 1982

(Annual average in million except percent)

	1950-1955	1956-1960	1961-1965	1966-1970	1971-1975	1976-1980	1981-1982
1. Private consumption (in current pesos)	6,810.5	9 513.6	14,739.4	24,166.8	53,419.0	126,145.2	
2. Government Consumption (in current pesos)	624.7	929.8	1,688.6	2,864.4	7,141.0	16,757.2	
3. Government Construction (in current pesos)	130.3	198.8	273.8	525.6	2,047.8	10,547.2	
4. Private Construction (in current pesos)	630.2	832.4	1,463.0	2,014.4	3,979.6	14,156.8	
5. Share of Government in Total Construction (%): (3) ÷ ((3) + (5)) × 100	17.1	19.3	15.8	20.7	33.9	42.7	
6. Overall Deficit of Central Government (in current pesos)	—	—	516.4	889.0	842.3	2,252.0	13,180.0
(in 1972 pesos)	—	—	—	—	1,124.0	1,708.0	3,585.0
7. Government Expenditure Share* in GNP (%)	—	—	9.65	9.89	12.37	14.54	15.79
8. Government Deficit Share in GNP (%)	—	—	0.97	1.18	1.11	1.26	4.12
9. Excess of Investment Over Savings (in current pesos)	—47.3	47.6	—129.8	294.2	1,900.0	9,100.00	20,550.0
10. Current Account Deficits (in US$)	—	—	22.0	213.6	105.2	1,320.4	2,820.0
11. Growth of Narrow Money Stock (M_1) (%)	4.4		10.0	9.7	16.8	17.0	0.0
12. Inflation Rate (%) Based on CPI	0.8		4.7	6.0	16.1	11.7	10.10

Sources: *NEDA, Philippine National Account Statistics and Key Indicators of Developing Member Countries of ADB* (April 1984)

*For 1976-1980 and 1981-1982, the figures refer to the proportion of government expenditure and net lending to GNP.

As Table 4 suggests, the period 1966-1970 which also encompassed the present administration's rise to power, represented a watershed in many respects. Compared to the immediately preceding five-year period, 1961-1965, the late 1960s witnessed a marked increase in the overall deficit of the central government (Table 4, Line 6) which was 72 percent higher compared to the average annual level in the previous five-year period. (In what follows, all references to levels of variables for subperiods are annual averages, unless otherwise stated.) This was due mainly to a surge in government construction expenditure, which increased 92 percent compared to 1961-1965 (Line 3). It will be recalled that the government then staked its reputation on a programme of vast infrastructure projects (e.g., roads, bridges and schoolhouses). The annual gap between investment and savings also widened dramatically (Line 9), from an excess supply of savings in 1961-1965 to an excess of investment over savings at a level of ₱294.2 million yearly. As expected, these changes were reflected in the annual current account deficits, the levels of which

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increased almost tenfold (i.e., from \$22 million to \$213.6 million between the two periods). As a result of these developments, total short-term public debt doubled, and outstanding public external debt rose from \$447 million to \$822 million between 1965 and 1970, or by 84 percent.

The pattern of aggressive government spending with resort to foreign borrowing was fundamentally maintained even in 1971-1975, although the floating of the peso and the oil-price shock of 1973-1974 compelled the government to trim the deficits somewhat to levels lower than the previous period (Line 6). Nevertheless, government construction expenditures increased 289 percent at a time when steadier components of income such as private and government consumption grew only 121 and 149 percent, respectively (Lines 1-3). Once more, short-term public debt doubled, while external public debt increased 214 percent, or from \$822 million to \$2,586 million between 1970 and 1975.

. . . it was the massive government deficits in the last years of the 1970s (1976-1980), and in particular the large capital outlays which set the stage for the difficulties in the 1980s . . .

The hypothesis maintained here is that it was the massive government deficits in the last years of the 1970s (1976-1980), and in particular the large capital outlays which set the stage for the difficulties in the 1980s, when world recession came and exports were hit hard. While the pattern of deficit-spending and foreign borrowing had been firmly established even before this time, the Philippine financial system might have survived the 1980s were it not for huge borrowings for such outlays. On the other hand, there may have been overwhelming reasons relating to the ruling group's imperatives for political dominance which made the choices it took appear inevitable in their minds.

As Table 4 and Chart 1 show once more, the second half of the 1970s was attended by the quadrupling of expenditures on both government and private construction, from ₱6 billion annually in the first half of the 1970s to ₱25 billion (Lines 3-4), at a time when other components of national expenditure (personal consumption, government consumption, and equipment expenditures) were about doubling (Lines 1-2). A large part of private construction was also financed by government money through loans from government financial institutions (GFIs). At the same time, government construction itself constituted an increasing portion of total construction (Line 5).

The heavy spending increased government deficits from ₱0.8 billion per year to ₱2.3 billion (Line 6), which however could not be covered by domestic savings.[8] The gap between investment and domestic savings widened further from ₱1.9 billion to ₱9.1 billion annually (Line 9). This gap had to be made up by foreign borrowings, which rose from \$2.6 billion to \$10.5 billion between 1975 and 1980, or a quadrupling of the debt within five years. This situation was undoubtedly abetted by the government's practice of guaranteeing foreign loans made to certain select groups

[8]In real terms this was an increase of 52 percent, or from ₱1.1 billion to ₱1.7 billion in constant 1972 pesos, using the GNP deflator.

in the private sector. Hence, the almost fivefold increase in the investment-savings gap between the two periods. To the extent that the same circle benefitted from the expansion of government expenditure which resulted in the large fiscal deficits, as well as the selective financing of investment projects in the private sector, the public-private distinction is artificial and illusory in analyzing the main contributors to the large external debt. The actions of the same social group may have been responsible for both. The effect was an increase in the annual level of the current account deficits, from \$105.2 million in 1971-1975 to \$1,320.4 million in 1976-1980, or an increase of nearly twelve times (Line 10).

Of course other countries have managed to run up large deficits by government as a proportion of GNP without having to resort to foreign borrowing (e.g., Japan). But this was possible only because domestic savings had been growing to fill the gap.[9] In turn, domestic savings is ultimately bound up with increases in productivity per person. The lesson, of course, is that the process of growth via government deficits can be sustained without huge increases in foreign indebtedness only if the expenditures are validated by increasing productivity per worker. For then the higher savings made possible by higher productivity could offset the effect of the budget deficit on the balance of payments. Hence, it is of utmost importance to ensure that such resources are invested efficiently and in the most productive areas.

. . . the process of growth via government deficits can be sustained without huge increases in foreign indebtedness only if the expenditures are validated by increasing productivity per worker.

In any event this was not what occurred in the Philippines. In Japan and the newly industrializing countries (NICs) where productivity per worker was rising at some five to six percent annually in the 1960s and 1970s, savings rose to finance a large part of domestic investment (with the exception of South Korea). But productivity per worker in the Philippines in the 1960s and 1970s increased only at a rate somewhat less than two percent, the slowest not only in East Asia and ASEAN but even slower than India and Nepal.[10] Hence, the rapid growth of government spending and private investment became reflected in wider current account deficits and increasing reliance on foreign financing.

The country's money supply was allowed to triple between the first and the second halves of the 1970s. As a result of this, but also partly due to the oil-price shock of 1978-1979, the average level of prices (i.e., consumer price index) doubled between the two periods and exceeded the inflation rate in the U.S. and Japan, the country's two major trading partners. On the other hand, the foreign exchange rate during this period

The country's money supply was allowed to triple between the first and the second halves of the 1970s.

[9] In our accounting framework, which should probably be familiar by now, $M-X=(G-T)+(I-S)$. An increase in the budget deficit $(G-T)$ which threatens to increase the trade deficit $(M-X)$ may be offset by a rise in S, for a given level of investment I.

[10] Data on productivity are taken from Oshima in "Sector Sources of Philippine Postwar Growth," in *Journal of Philippine Development,* First Semester, 1983, p. 9, Table 2.

remained virtually unchanged (see Chart 1), with the authorities presumably lulled by the comfortable levels of international reserves being constantly replenished by fresh foreign loans. Adjustments in the nominal exchange rate during the period, though already being resented by the masses whose living standards were being eroded, were nonetheless insufficient in compensating for the much higher inflation domestically than abroad. Ironic as it may sound, considering the hardships suffered by the people, the peso was then still overvalued in real terms[11] as a consequence of policies pursued by the government.

Since the country had, in the meantime, committed itself to an export-promoting strategy, the overvalued peso became a drag on exports and prevented these from making a larger contribution to growth. It also partly explains the influx of imports, especially of nonessentials and other consumer items, which had been increasing at this time.[12]

If foreign funds flow in and the money supply expands, such a situation does not have to lead to inflation—and ultimately the need for further depreciation—if in the process these add to the current supply of goods and services to match the purchasing power they create. Additions to current supply could take the form of direct imports of consumables or support to domestic production via imports of capital goods.

However, insofar as their allocation was guided by other than purely economic criteria, the bulk of construction and other capital outlays in both the private and public sectors were not very productive and many were outrightly wasteful. In the public sector, highways, schoolhouses, waterworks, flood control, large public buildings, involvement in the hotels, not to mention monument-construction yielded little or no cash returns to the government or to government corporations, if they ever contributed to current output at all, while the returns on others, e.g., irrigation, harbors, rural electrification, railroads, etc. were meager in the immediate years after construction. In a number of instances, though the outward purpose of projects might be endowed with some plausible economic or social justification, a more urgent reason for pursuing them was the opportunity to use government activity as a vehicle for private gain, whether pecuniary or political. Examples would be overdesigned

In a number of instances, though the outward purpose of the projects might be endowed with some plausible economic or social justification, a more urgent reason for pursuing them was the opportunity to use government activity as a vehicle for private gain...

[11] This means that in order for our exports to have maintained their competitiveness in U.S. markets, for example, exchange rate depreciation should have allowed for the fact that inflation was higher in the Philippines than in the U.S. (i.e., 14.2 versus 9 percent per year from 1972 to 1981). To do this the peso would have had to be allowed to depreciate by 30 percent more, on the average (Chart 1).

[12] In its verbal commitment to export-promotion, the Philippines has been engaged in dismantling the previous system of tariffs and quotas. Had the exchange rate been maintained at competitive levels, there would have been no added incentive to import. However, reduced tariffs plus an overvalued currency constituted a powerful impulse to increase imports.

bridges, highways, public buildings or large energy projects designed to secure a political constituency, to get a commission, or to corner a contract.

Some private-sector construction was also apparently ill-chosen, e.g., the boom in hotel facilities, although even this was partly initiated by the government and supported by its financial institutions. The government's practice of extending guarantees on loans made to selected corporations and its encouragement of the growth of monopolies also served to erode the incentive to become efficient. Under such a system, high returns to agents could be had not by investing judiciously in the most economic projects, but simply from funnelling corporate resources into private hoards or consumption.

Though sorely needed, a full documentation of the effect of economic concentration and government intervention on the productivity of investment would be beyond the scope of this paper. One might mention that the incremental capital-output ratio (ICOR),[13] whose reciprocal might be regarded as an index of the productivity of investment, rose from 4.2 in the 1960s to 5.0 in the 1970s. By the 1980s, ICOR had risen even further to 9. To what extent can this rise be attributed to the incentive structure established, which encourages the maximization of activity rather than of results? While price variables—which are often underlined—are doubtless also important, nonprice considerations, such as the industrial structure and the institutional framework, must also have mattered, if not more so.

One particular point needs explanation. It has been argued that the projects for which most of the foreign loans had been spent were in fact economically justifiable, since the creditors always set stringent criteria for lending, especially for infrastructure. The first point is that this is not always true, especially for commercial loans extended to the private sector and guaranteed by the government. In such cases, the basis for the loan having been granted may rest predominantly not on the soundness of the project, per se, but on the fact that the government or monetary authorities are backing it up. The second point is subtler: in order for waste and inefficiency to have occurred, it is not necessary that foreign loan proceeds be wasted or spent on inefficient projects. It is sufficient that they offset or replace domestically available resources, which could then be spent on projects of more dubious social value. Hence, because loans financed government spending for infrastructure, domestic resources could effectively be released to be spent on the military, to bail out favored corporations, to build palaces, etc. It could be said that, in effect, foreign loans "financed" waste indirectly. If foreign loans were not available,

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[13] This ratio expresses the amount of investment associated with a given increase in output. E.g., if it takes ₱9 to achieve an annual output of ₱1, ICOR is said to be 9. Obviously, the lower the ICOR, the more productive capital formation is.

perhaps policymakers might have been constrained to use domestically generated resources more efficiently.

In any event, by the closing years of the 1970s, the government found it increasingly difficult to pay the interest on the foreign debts and had to resort increasingly to short-term borrowings, which rose as a proportion of total external debt, from 29.8 percent on the average in 1971-1975 to 36.1 percent in 1976-1980.

In the early 1980s,... the government persisted in its previous policy of borrowing heavily domestically and abroad...

In the early 1980s, despite the ongoing worldwide recession and concomitant declines in export earnings, the government persisted in its previous policy of borrowing heavily domestically and abroad, instead of reducing its deficits. It even accelerated government spending as it ran annual deficits *six times* larger than in the past period (i.e., ₱13.2 billion in 1981-1982 versus ₱2.2 billion in 1976-1980). As a result, the share of government in total expenditures rose to almost 16 percent, while the share of its deficits reached an unprecedented 4.12 percent (Lines 6-8). The investment-savings gap also more than doubled (Line 9) from ₱9.1 billion to ₱20.6 billion annually, as the private sector was able to obtain foreign loans—often guaranteed by government—to pursue ambitious projects. Annual current account deficits were running at $2.8 billion, or 114 percent higher than those in the previous period. The resulting increase in foreign indebtedness further added to the interest burden and required more borrowings for repaying interest. Large government expenditures generated inflation and the consequent overvaluation of the peso. Before Aquino's assassination, capital flight and dollar-salting had already been accelerating. His death aggravated matters.

2.1.3 The Aquino Assassination

From the previous sections, it becomes apparent that there was a downward drift in the country's economic performance and hence any major exogenous shock was bound to provoke a crisis.

There is no doubt that, viewed as a historical event, the Philippines' economic crisis was precipitated by the assassination of former Senator Benigno S. Aquino on August 21, 1983. This is not to say, however, that anything less disastrous would not have had the same result. From the previous sections, it becomes apparent that there was a downward drift in the country's economic performance and hence any major exogenous shock was bound to provoke a crisis. Prior to the Aquino assassination, the Philippines had still been relying heavily on borrowing for financing its deficit on trade and payments, in a strategy of "riding out" the recession without making drastic changes in its target income growth. The difference now was that, as a result of a tightening of international credit markets and lower world-inflation since 1979, as well as the country's own large exposure to international banks, it had to pay a higher real interest rate on new borrowings and get them on increasingly shorter terms. In addition, amortization of previous debt became increasingly burdensome as interest rates rose and loans fell due. In 1982 net interest expenses came close to $2 billion, and were responsible for 46 percent of the current account deficit. With exports making a comeback only during the third quarter of 1983, the increasing demands for foreign exchange for imports and debt-servicing could be met increasingly only through the availability of short-term loans which constituted about 43 percent of total external debt on the average in the period 1981-1983. With Aquino's assassination, a crisis of confidence in the present government seized the foreign banks, which simply refused to renew the short-term financing that the authorities had hitherto taken for granted. Without replenishment from short-term borrowings, international reserves fell drastically from \$2.54 billion at the start of 1983 to \$1.43 billion by the end of September that year, according to official statistics.[14] In October 1983, the prime minister announced that international reserves had been reduced even further to \$430 million, owing to what was termed "capital flight," although it was later learned that the level of reserves had been overstated.

The government then declared a 90-day moratorium on payments of principal on its foreign-exchange liabilities and imposed foreign exchange restrictions, stopping all dollar trading and requiring all export revenues to be constituted into a foreign-exchange pool. Oil and other priority imports, as well as the quarterly payments of interest on existing debt were then to be financed from this pool. At the same time, the government began negotiations with its private creditor banks and the IMF for a debt-rescheduling and additional financing of \$3.6 billion for 1984. In October 1983, the peso was devalued from ₱11 to ₱14 to a dollar; reserve requirements were raised in an attempt to reduce money supply growth; and budget cuts for 1984 were announced. These efforts were widely perceived to be related to conditions attached by the IMF to the grant of new credit. However, questions regarding the international reserves led to delays in debt negotiations. The government has since renewed the moratorium twice.

The government then declared a 90-day moratorium on payments of principal on its foreign-exchange liabilities and imposed foreign exchange restrictions. . .

The immediate effect of foreign exchange controls was to restrict effectively the flow of imported material inputs to many industries, causing numerous firms to cut back production, lay off or rotate workers, or simply close shop. The October devaluation also triggered inflationary expectations, which further raised prices and encouraged hoarding and speculation. As it evolved, however, the system of foreign exchange allocation became a de facto two-tier exchange rate system, since non-priority imports were allowed provided they obtained foreign exchange from anywhere except the CB pool. The foreign exchange rate at the curb was, of course, much higher than the official rate, hence such a system effectively represented a transfer from the exporters to importers and consumers of priority imports.

The May 14, 1984 elections and the campaign period preceding them witnessed a sharp break in the trend towards adjustment as government borrowings from the Central Bank accelerated. The sudden increase in

The May 14, 1984 elections and the campaign period preceding them witnessed a sharp break in the trend towards adjustment as government borrowings from the Central Bank accelerated.

[14] CB Governor's Report to the President (Third Quarter 1983).

liquidity caused renewed inflationary pressure, and posed yet another obstacle to the debt renegotiation process, which called for strict limits to monetary growth. In an attempt to meet the targets for fiscal deficits and monetary levels for the rest of the year despite the election bulge, the government levied various taxes, mostly for revenue purposes. In addition to the eight percent ad valorem surcharge on all imports, specific taxes on gasoline and other petroleum products were hiked.

On June 5, 1984 the government announced a change in the system of foreign exchange allocation; the peso would again be put on the float, and foreign exchange trading by banks would again be permitted. At the same time new taxes were levied; the ad valorem tax on imports was increased to 10 percent; a 10 percent tax on all foreign exchange trading was imposed; and a 30 percent tax on differential export receipts was announced, to be gradually reduced until 1985. The readoption of the floating rate would effectively lead to the peso's depreciation and another round of adjustment of domestic prices, especially in petroleum, which used to obtain foreign exchange at a preferential rate. In principle, the raising of revenues through specific rather than income or wealth taxes is ojectionable because such taxes penalize the poor more than the rich (e.g., through higher prices) as well as cause distortions in the economy. In the meantime, however, the new taxes on oil, trade, and foreign exchange transactions will place a huge amount of resources at the government's disposal. What it chooses to do with the revenue will determine the further effects of such measures on the economy. On the one extreme, the government could regard the new revenues as further license to expand government expenditures, to the extent of maintaining or even enlarging the budget deficit. On the other, it could take the opportunity to scale down its expenditures drastically and in the proper places, run a budgetary surplus and, in effect, use the new revenues simply to mop up excess liquidity. Although we are not in favor of the collection of the new specific taxes in principle, given that they have already been collected, we would advocate that they be regarded as government savings while expenditures are curbed.

2.2 The Distribution of Income and the People's Welfare

The previous section sketched the economy's faltering growth record and showed that, relative to its neighbors and to its potentials, the Philippines has done rather poorly, having experienced the lowest growth rates of GDP per capita in the region for the past two decades.

It is one thing to say, however, that output growth has been relatively low—quite another to conclude anything about the material well-being of the majority of Filipinos. For if the ultimate aim of economic development is to improve the material lives of the greater number of Filipinos, then surely this may be achieved even with decelerating growth if only the sharing of increases in output were to favor the majority. In fact, some defense of the country's poor economic record has come in the form of disavowing any claims to "growthmanship" and alleging that redistribution (people-orientedness, etc.) is the main thrust of the administration's policies. By this reckoning, one ought not to judge the country's performance by its economic record, since it was allegedly never the government's intention to concentrate solely on economic growth, but rather judge it by what it has done for "the people," presumably meaning the majority of Filipinos.

Of course, such a perception of the government's goals is far from unanimous, and it would take some effort to convince some observers that this was not simply an ex post facto excuse for poor economic performance. The more widespread perception is that the economic development effort pursued by the government has in fact focused on maximizing growth, although, as mentioned, this effort has not entirely succeeded. The optimistic view held has been that benefits from output growth will eventually trickle down to the lowest socioeconomic classes.

However, whether the government has, in fact, been stressing mainly economic growth or redistribution (or neither), it would always be a fair question to ask whether the material welfare of Filipinos has been improving. Are Filipinos able to meet at least the basic needs? Is it possible to call the existing distribution of income, wealth, and social services fair or just? Have there at least been significant improvements in the trend of distribution?

Are Filipinos able to meet at least the basic needs? Is it possible to call the existing distribution of income, wealth, and social services fair or just?

A person's material welfare depends on the income he derives from owning such productive inputs as labor power, entrepreneurial ability, capital and land. If ownership of productive inputs is unequally distributed, income disparity would follow as a result. Those who own only labor power would earn less than those who own more besides, while those who are less-skilled would earn less than those who are more highly skilled. Furthermore, the distribution of income and wealth is influenced by the pattern of distribution of government fiscal policy (e.g., spending and taxation) which may either modify or reinforce the existing structure of inequity.

The distribution of wealth in the Philippines, even in the absence of hard data, can be said to be unequal. Most Filipinos own little more than their labor power. And even among these, their skills vary, with the majority falling under the category of "less-skilled." The highly skilled tend to own more wealth, while it is also the more wealthy who can generally afford to develop their skills, say through education. When labor supply exceeds the demand, high unemployment and underemployment occur, as a result of which wages stagnate or even fall. Even labor's ability to improve its income share and working conditions through collective bargaining is constrained because the government intervenes in union-organizing and union-bargaining. The government's industrial relations policy has been concerned with ensuring the continuity of economic activity, and whether

The government's industrial relations policy has been concerned with ensuring the continuity of economic activity, and whether the terms of employment are acceptable or not to workers is generally a secondary concern.

the terms of employment are acceptable or not to workers is generally a secondary concern. Its view on wages is similar to that held by management, i.e., wages are mainly a cost of production rather than the determinant of laborers' claims to output. Wages, therefore, have to be held down both as an incentive for the entrepreneurs to undertake investment and to enhance the international competitiveness of Philippine exports. Most adjustments to exchange-rate depreciation have therefore been borne by workers and other fixed-income recipients, whose incomes have not kept pace with price increases.

2.2.1 Income Distribution

. . . the income distribution worsened between 1971 and 1979.

Estimates based on the 1971 National Census and Statistics Office (NCSO) survey on family income and expenditure and the 1979 integrated survey of households (ISH) show that the income distribution worsened between 1971 and 1979.[15] The poorest 60 percent of total households, which received only 25.0 percent of total income in 1971, suffered a further decline of their share to 22.5 percent in 1979 while the richest 10 percent of households increased their share of total income from 37.1 percent in 1971 to 41.7 percent in 1979 (Table 5).

Other evidence confirms the worsening income distribution. The gap between incomes earned in industry, on the one hand, and in agriculture and services, on the other, has widened. While the value of product per worker in industry was 2.6 times that in agriculture in the 1960s, this increased to 2.8 times in the 1970s. Likewise, where in the 1960s product per worker in industry was 0.9 times that in services, in the 1970s this increased to 1.2 times (Table 5).

Some indicators point to a similar trend of widening income differentials within each of the three major sectors. For instance, in agriculture from 1971 to 1980, the number of farms increased from 2.4 million to 3.4 million but the average size of farms declined from 3.6 to 2.6 hectares. The growing population increased small farms relative to larger farms, thereby widening income gaps in agriculture. In addition, a comparison of labor force surveys for the first quarters of 1971 and 1983 shows a 75 percent increase in agricultural wage-workers, the lowest-income workers in the country (from 0.8 million to 1.4 million). Another major low-income group in rural areas, the small fishermen, also doubled in number (111.3 percent increase) from 1970 to 1980 (1980 Census of Fisheries). Since commercial fishing units more than doubled (177.7 percent increase) during the same decade and, if as widely believed by fishery experts, capital-intensive

[15] The 1971 NCSO-FIES and 1979 ISH are not directly comparable since the former is collected on a quarterly basis, while the latter represents a sample of annual incomes. However, the estimate presented already takes this problem into account and thus minimizes the problem of households "jumping around" from one quarter to the next. See Oshima (November 1983).

Table 5
INCOME

1. Income Distribution	Percentage Share in Income		
	1971		1979
Six lowest income deciles (poorest 60 percent)	25.0		22.5
Highest income decile (richest 10 percent)	37.1		41.7
2. Value of Product (at current prices) per worker	1960s		1970s
Industry[a]/Agriculture	2.6		2.8
Industry/Services[b]	0.9		1.2
3. CB Index of Average Monthly Earnings in Selected Nonagricultural industries in the Philippines (1972 = 100)		1980	
Money earnings			
salaried employees		274.7	
wage earners		255.5	
Real earnings (1972 prices)			
salaried employees		93.2	
wage earners		86.7	
4. CB Wage Rate Index for Laborers in Industrial Establishments in Manila and Suburbs (1972 = 100)		1980	
Money wage rates			
skilled		180.9	
unskilled		151.5	
Real wage rates			
skilled		63.7	
unskilled		53.4	

[a] "Industry" includes mining and quarrying, construction, manufacturing, utilities and transport, storage and communication.

[b] "Services" includes commerce, government, community, business and recreational services, domestic services, personal services other than domestic and industry not reported.

trawlers are increasing their catch at the expense of small fishermen, it is highly likely that much of the increase in fishery output has gone to the commercial fishing operators.

In the nonagricultural sector, the 1971 and 1978 NCSO-ISH data provide evidence that the lot of the lowest-income workers has fallen badly relative to that of the higher paid workers. The real cash earnings of blue-collar workers (in farming and industry) declined more than those of white-collar workers (professional and technical men, managers, administrators, etc.). During the period, some workers (sales and service workers) in the service sector fared better with some increase in real cash earnings due possibly to the growth of tourism and related industries. However, the lowest-paid in the services sector (mainly in the large informal sector

. . . the 1971 and 1978 NCSO-ISH data provide evidence that the lot of the lowest-income workers has fallen badly relative to that of the higher paid workers.

where unemployed workers from farming and industry go) have not fared as well as the services sector as a whole.

The CB wage/salary series for 1972 to 1980 also shows that real incomes have declined more for wage earners than for the salaried, and for the unskilled more than the skilled (Table 5). The index of average monthly money (nominal) earnings (1972 = 100) in selected nonagricultural industries in the Philippines indicates that nominal incomes increased by 174.7 percent for salaried employees and 155.5 percent for wage earners between 1972 and 1980. Because of inflation, however, monthly real earnings were always lower than the 1972 level, with the differential being larger for wage earners than for salaried employees. The monthly real earnings of salaried workers in 1980 were 93.2 percent of their 1972 level while that of wage workers was only 86.7 percent. Earnings of the lower-paid workers deteriorated more rapidly than those of the better-paid. The real wage of skilled laborers in Manila in 1980 was only 63.7 percent of its level in 1972 while that of the unskilled was even lower, 53.4 percent.

Of course, these unfavorable wage trends could have been offset by increasing days, weeks, and months of work, adding up to larger annual family incomes. One who works for a lower wage could conceivably earn more than one who works for a higher wage, by simply working longer. But the (NCSO-ISH) unemployment rate increased from 5.2 to 5.9 percent of the labor force rising yearly by 2.5 percent in the last five years, 1978 to 1983 (Table 6). The unemployed increased from 0.8 million to 1.2 million. More important, underemployment rose *three times* from 10.2 to 29.0 percent of the labor force, or grew by 25.5 percent annually during the same period. This meant an increase of the underemployed from 1.6 million in 1978 to 5.6 million in 1983. Of this total, the visibly underemployed (those working less than a full-time work standard of 64 days per quarter, and wanting additional work) increased from 0.8 million to 3.4 million. On the other hand, the invisibly underemployed (those working at least 64 days per quarter but still wanting additional work) climbed from 0.7 million to 2.2 million. These figures pertain to periods even prior to the third quarter of 1983. The occurrence of the debt crisis will undoubtedly have aggravated the situation.

More important, underemployment rose three times from 10.2 to 29.0 percent of the labor force, or grew by 25.5 percent annually during the same period.

A feature of Philippine labor supply is its unusually high annual growth rate after the mid-1970s—3.8 percent in 1971-1974, 5.6 percent in 1978-1979, and 4 percent in 1978-1983. Much of this increase was due to the higher number of females working or seeking work. One explanation for this may be found in the fall of real wages of heads of households to levels below the customary subsistence: this could compel housewives to seek work to help bring family incomes up to subsistence levels. If this has been the response of low-income families to falling real wages of household heads, the increased number of earners per family could mitigate the decline in total family incomes. But this will not fully offset the decline since not all who seek work succeed in finding employment.

Even if we assume that all of the increments to the growth rates of labor force participation were additions to earners per family, they would benefit no more than one to two percent of total families each year.

The distribution of employment among sectors was equally bad for labor.

The distribution of employment among sectors was equally bad for labor. Agriculture's share of total annual employment has been declining very slowly in the 1970s (Table 6), while that of industry has been increasing, though at a very slow rate. It has been the services sector which assumed the major role of absorbing excess labor from agriculture. The problem is that agriculture and services have been lower productivity sectors and, hence, lower income sectors relative to industry.

Table 6
EMPLOYMENT

	1978	1983
	(First Quarter)	
1. Unemployment as a proportion of labor force	5.2%	5.9%
2. Unemployed (million)	0.8	1.2
3. Underemployment as a proportion of labor force	10.2%	29.0%
4. Underemployed (million)		
Total	1.5	5.6
Visible	0.8	3.4
Invisible	0.7	2.2

5. Annual sectoral distribution of employment (percent)	1957-1964	1964-1971	1971-1978	1st Qtr. 1983
Agriculture	60.5	55.8	52.9	50.1
Industry	18.2	18.7	19.0	14.8
Services	21.3	25.4	28.1	34.9

Source: NCSO, *Integrated Survey of Households,* for the dates indicated.

Although a breakdown in the incidence of joblessness among occupational groups is not available, it is highly likely that when labor supply increases faster than demand, it is the material well-being of the less-skilled workers which comes under greater threat. Their greater number and easy replaceability make their job tenure irregular and insecure.

Despite the various problems in the data, the implication of these findings needs to be taken seriously. The overall rise in income inequality is already cause for grave concern; that the rise in this inequality came almost entirely at the expense of the lower-income deciles is even more alarming.

2.2.2 Material Welfare

This section focuses on the lower income sectors whose subsistence is constantly threatened by even slight disturbances in the economy.

The need for legislated minimum wages indicates the existence of wages lower than the prescribed minimum. In the absence of published data on current wages and salaries actually earned, however, the legal minimum wages will be used to assess the possible material welfare of the lower income sector. The concept of subsistence income as that level affording minimum consumption of basic necessities has been estimated for families of given characteristics for the Philippines. This income is also called the "poverty threshold," below which a family is considered poor. Table 7 lists the legal minimum wages for different sectors as of February 1984 and also some poverty-threshold estimates at February 1984 prices. The lowest poverty threshold estimate of ₱1,082.43 per month (Tan-Holazo) is not reached even by the highest nonagricultural legal minimum wage of a worker who is the sole breadwinner in a six-member household. All other poverty threshold estimates are much higher than the minimum wage for the national capital region. Furthermore, there are reasons to believe that even the legislated minimum wages are not widely enforced. Hence, there are many low-skilled workers both in rural and urban, and formal and informal sectors earning wages and salaries below subsistence. These households need more than one breadwinner, another job for the main breadwinner, and/or dole-outs. Undoubtedly, this does not hold true only for the low-skilled since we find relatively skilled workers whose pay would be close to the poverty thresholds. Eligibility for welfare services from the Ministry of Social Services and Development can only be availed of at much lower monthly family income cut-off levels of ₱350 to ₱450.

All other poverty threshold estimates are much higher than the minimum wage for the national capital region.

The erosion of labor income in the 1970s has already been mentioned in the earlier section on income distribution. The CB data (1972 = 100) indicate that the erosion of real wage in selected industrial establishments in Manila and suburbs in the 1970s was greater and faster than in the earlier years. The real wage rate index for skilled laborers dropped from 135.7 in 1957 to 100.0 in 1972; it declined even faster from 1972 to 1980 as it fell from 100.0 to 63.7. The case for the unskilled laborers was worse. Their real wage rate index declined from 113.4 to 100 in 1957-1972 and from 100.0 to 53.4 in 1972-1980.

The case for the unskilled laborers was worse. Their real wage rate index declined from 113.4 to 100 in 1957-1972 and from 100.0 to 53.4 in 1972-1980.

The NCSO household survey data on real weekly cash earnings of wage and salary workers indicate improvements during the 1957-1969 period for both sexes in all occupations. However, the reverse happened in 1971-1978 except in the case of male sales and manual workers and the female sales, agriculture, and service workers whose earnings were lowest in absolute level.

Table 7
LEGISLATED MINIMUM WAGES, POVERTY THRESHOLDS AND INDIGENCY INCOME LEVELS, FEBRUARY 1984

	Monthly (₱)
A. Legislated Basic Minimum Wage and Supplements— National Wage Council (December 31, 1983)	
1. Nonagricultural	
a. National Capital Region— ₱42.07/day	1,062.27[a]
b. Outside National Capital Region—₱40.99/day	1,035.00[a]
2. Agricultural	
a. Plantation—₱34.42/day	869.10[a]
b. Non-Plantation—₱25.90/day	653.98[a]
B. Poverty Threshold	
1. Abrera (1974): 6-member household	
a. Manila and Suburbs	2,997.85
b. Other Urban Areas	2,487.76
c. Rural	2,171.74
2. Center for Research Communication (January 1982): 5-member household	
Threshold Family Income—Metro Manila	3,515.12
3. Tan-Holazo (1975): With Food Variety; 6-member household	
a. Metro Manila	1,306.36
b. Philippines	1,082.43
4. World Bank (1975): 6-member household— "Least Cost" Consumption Basket	
a. Urban	3,469.92
b. Rural	2,613.12
c. Philippines	2,784.48
C. Indigency Income (July 7, 1982)—Ministry of Social Services and Development[b]	
1. Urban	
a. 6-member household or less	400.00
b. more than 6-member household	450.00
2. Rural	
a. 6-member household or less	350.00
b. more than 6-member household	400.00

[a] As of December 31, 1983 to April 30, 1984; Daily wage multiplied by 25.25 days per month (NWC formula).

[b] MSSD Administrative Order No. 115, Series of 1982.

These observations, on the whole, tell the story of labor incomes which fell in real terms because nominal increases were not sufficient to catch up with inflation, especially as consumer prices nationwide trebled between 1972 and 1983 (301.5 percent increase). Of course, it is possible that wages were falling because labor productivity was also falling. Hence, one must ask what was happening to labor productivity or output per worker during this period. Labor productivity from 1957 to 1978 was positive and increasing from ₱2,980 per worker in 1957 to ₱4,200 per worker in 1978 (Table 8). It increased annually for the whole economy by 2.12 percent, and for industry by 5.10 percent in 1971-1978[16] when the erosion of real earnings of workers was largest. The labor sector, on the average, was not only unable to share in the productivity increases in the 1970s but even suffered cuts in its share of output, a trend which one can speculate will continue and even worsen in the 1980s.

The labor sector, on the average, was not only unable to share in the productivity increases in the 1970s but even suffered cuts in its share of output...

Table 8

LABOR PRODUCTIVITY[a]

Year	All Sectors	Agriculture	Industry	Services
	Labor Productivity (peso per worker)			
1957	2,980	1,740	4,320	5,280
1971	3,620	2,370	5,170	4,640
1978	4,200	2,420	7,390	5,180
	Annual Growth Rate of Labor Productivity (percent)			
1971-1978	2.120	.300	5.100	1.570

[a]Output per person employed is estimated by dividing national income (in million ₱) at 1972 prices by employment in thousand.

Source: R.L. Tidalgo and E. Esguerra, "Philippine Employment in the 1970s," PIDS Working Paper 82-02, 1982, Table A-6.

2.2.3 Other Socioeconomic Indicators

Apart from the distribution of income and wealth, there are non-economic variables which affect the quality of the people's lives. If the past debates regarding the meaning of "true" development have pointed out anything, it is the inadequacy of relying on economic measures alone

Apart from the distribution of income and wealth, there are noneconomic variables which affect the quality of the people's lives.

[16]The Philippines had the lowest growth in productivity per worker among the East and Southeast Asian countries for 1960-1979. H. Oshima, "Sector Sources of Philippine Postwar Growth," *Journal of Philippine Development*, 1st Semester, 1983.

in assessing the level of the people's welfare. Some ardent defenders of current policies have seized on this fact and sought to excuse the economy's poor performance by suggesting that the people's condition as indicated by these noneconomic variables (which might be measured by something as elusive as "smiles") has improved, although the economy has failed. On the other hand, it is undeniable that under a system of market-exchanges (and there has been no real indication that the Philippines is in danger of becoming socialist in the near future), a person's well-being, material and otherwise, is intimately associated with the amount of productive inputs over which he disposes, and the monetary value which the market places on those inputs. Under such circumstances, the distribution of income and wealth becomes the crucial socioeconomic indicator.

Nevertheless, this section inquires into the validity of the claim that, if not in anything else, the present policies have resulted in an improvement of other noneconomic measures of the quality of life, among them health, personal security and dispensation of justice.

Improvements in the quality of health have been evident in the Philippines (as in all developing countries) even during the 1950s and 1960s, and they continue to the present. This has been due to such secular trends as the improvement in the quality of drugs and medicine, knowledge regarding health and sanitation practices, as well as increasing levels of education and income. For the period 1953-1958, life expectancy at birth was estimated to be at about 47.5 years (Lorimer 1966). In 1960 and 1970, life expectancy was 52.8 and 55.8, respectively, while by 1975 it was 59.4 years, according to the Office of Population Studies. These figures would suggest that there was already a trend towards the lengthening of life expectancy even before the advent of present policies. Therefore, such improvements could not be naively attributed to authoritarianism without further qualification.

The same trend of health improvement even before martial rule was also evident for infant mortality (or, more correctly, the probability of death between birth and age one). Estimates (Flieger, et al., 1981) show that in 1950, infant mortality was 160, meaning that out of 1,000 live births 160 died before reaching age one. This statistic fell to 113 in 1960, 93 in 1970, and by 1975 it was down to 76. Data for the 1980s, however, were not available. What is disturbing, however, is that based on rough estimates using vital registration data, infant mortality had risen to 78 in 1977 compared to 76 in 1975. Considering that the 1980s will definitely be more difficult economically than the late 1970s, a worsening of infant mortality is distinctly possible. One might conclude, therefore, that it is difficult to identify an independent contribution by the present system to the improvement of health. On the other hand, the government's commitment to the direct improvement of health as measured by these

What is disturbing, however, is that based on rough estimates using vital registration data, infant mortality had risen to 78 in 1977 compared to 76 in 1975.

indicators has come under question, considering the decreasing share of health services in the budget.

The negative impact on health, albeit indirect, of such economic factors as declining real incomes, unemployment and rising food prices is all too transparent. Insofar as the regime's policies have directly caused or exacerbated such economic difficulties for the people, one must question how high on the government's scale of priorities the people's health really ranks.

Another social dimension worth examining is peace and order. According to Philippine Constabulary data, the national crime rate, defined as crimes committed and reported per 100,000 population, stood at 247 in 1971. In 1972, the year martial law was declared, it fell to 236 and continued to decline to 183 in 1976. Thereafter, the peace and order situation deteriorated. The national crime rate climbed continuously from 183 in 1976 to 279 in 1980. We note that the reported national crime rate in 1980 was higher than in 1971. It rose further to 313 in 1982 according to an article in *Fookien Times Yearbook 1982-1983* written by PC Chief General Fidel Ramos.

The national crime rate climbed continuously from 183 in 1976 to 279 in 1980. We note that the reported national crime rate in 1980 was higher than in 1971.

Data on crimes suffer, of course, from gross underreporting. Hence, the reported national crime rate underestimates the true level of criminality in the country. The trend nevertheless conforms with our perception of the situation. While some improvement in peace and order was experienced until 1976, the succeeding years showed significantly deteriorating conditions. It should be pointed out that increasing criminality is also partly related to increasing economic hardships. Crimes against property are a form of (illegally) redistributing wealth; economic stresses can lead to mental disturbances which induce individuals to commit crime, etc. As alternative legal economic activity becomes less and less rewarding, the risks and costs associated with a life of crime *pro tanto* seem smaller. Against this logic, the "containment" of criminality by threats, force, and punishments by the state machinery can succeed only partially and temporarily.

The worsening peace and order situation can be further gleaned from the data on media-reported military-dissident encounters collected and analyzed by Miranda (1984). The reported military encounters with dissident groups stood at 245 and 268 in 1977 and 1979, respectively. Between 1980 and 1982, it rose dramatically from 377 to 852.

The deteriorating peace and order conditions, while themselves partly caused by economic difficulties, in turn, feed back into economic conditions by causing greater uncertainty, and insecurity, discouraging investments and economic activity in general.

The improvement in the peace and order situation has always been claimed as one of the major benefits from authoritarianism. The data clearly show, however, that such benefits were temporary. The country in fact appears to be worse off now than before the advent of authoritarian rule as far as peace and order is concerned.

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One of the raging issues confronting Philippine society is the question of justice. We are not now in a position to fully discuss this matter, though we are deeply concerned over the increasing number of reports regarding summary execution of persons, popularly known as "salvaging." In addition, we take note of the deterioration in the disposal rate of court cases and the tremendous increase in the backlog of pending cases. Data from the Ministry of Justice and the Supreme Court reveal that the annual rate of disposal of court cases was slightly less than 47 percent in 1962. During the years 1969-1971, it was close to 48 percent. When martial law was declared, the disposal rate rose dramatically to 68 percent in 1973. Since then, however, it has declined continuously. By 1980 the disposal rate was already less than 46 percent, the worst since 1962.

From 1962 to 1974 the backlog of court cases hovered between 242,000 and 263,000. Between 1975 and 1980, however, the backlog rose from 273,000 to 493,000 cases. These data indicate that if the wheels of justice ground slowly before authoritarian rule, they are grinding ever more slowly today. ?

3 AN ANALYSIS OF THE ECONOMIC CRISIS

3.1 Fiscal and Monetary Policies

The present administration's extended second term, beginning in 1969 and lasting to the present, introduced not only a highly centralized system of government but also major changes in economic policy...

The present administration's extended second term, beginning in 1969 and lasting to the present, introduced not only a highly centralized system of government but also major changes in economic policy, which could be summarized as follows: (a) a break from the fairly conservative monetary, fiscal and trade-financing policies of the previous two decades; (b) an unprecedented expansion in the role of government in financial and product markets; and (c) an industrial reorganization of important economic sectors which tended to create greater economic concentration. In the financial markets, these changes were reflected in the rapid acceleration of foreign borrowing and of Central Bank lending, both to finance the growing share of government in total expenditure; the new prominence of state banks, i.e., Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP); the grant of monopoly advantages, subsidized credit, and other privileges to new government corporations and selected private (including financial) enterprises; and the enforced mergers of commercial banks through higher capitalization requirements.

The following is a discussion of some aspects and consequences of these policy changes, especially as these relate to the present crisis.

3.1.1 Departure from Conservative Monetary and Fiscal Policies

The break with the conservative policies of the 1950s and 1960s that the present administration pursued in the 1970s can readily be seen in the movement of economic variables...

The break with the conservative policies of the 1950s and 1960s that the present administration pursued in the 1970s can readily be seen in the movement of economic variables as shown in Table 4. Throughout the 1970s the authorities permitted money supply (M_1) to grow annually at 17 percent on the average, i.e., 16.8 and 17.0 percent for 1971-1975 and 1976-1980, respectively. (See Table 4, Line 11.) This is to be compared with monetary growth of 4.4 percent annually in the 1950s and around 10 percent throughout the 1960s.[17] These increases in the money stock were largely traceable to Central Bank credit, including the credit used to finance the government budget. Now it has been plausibly argued that there is certainly scope for monetary expansion in the context of any growing economy, if only because a greater volume of transactions is associated with increasing real output. However, unless monetary expansion is sooner or later accompanied by increases in the output of goods and services, it would simply be dissipated through inflation. It is not at all evident that the higher growth of money stock during the 1970s could be sufficiently justified by citing the higher growth of real output in the 1970s vis-a-vis the 1950s and the 1960s. Indeed empirical analyses

[17] The abrupt curtailment of monetary growth in 1981-1982, shown in the same table, already reflects the consequences of previous policies, as the government's actions were increasingly hamstrung by conditions imposed by its creditors, particularly the IMF, which set ceilings on monetary growth.

show monetary expansion to be an accommodating, if not causal, factor in Philippine inflation during the 1970s.

In contrast with more recent history, inflation was negligible during the 1950s, averaging less than one percent (Table 4, Line 12) despite the high growth rates of real output registered during the period. In the next two periods (1961-1965 and 1966-1970), however, the growth of real output declined as the import-substitution regime lost its steam. In the meantime, monetary growth had accelerated to finance both private and government spending, often in unproductive ventures, e.g., election campaigns (Valdepeñas and Bautista, 1977, pp. 218 ff). This, together with the discrete changes in the exchange rate that occurred in 1962 and 1970, explains the somewhat higher rates of inflation during the 1960s, although from hindsight even these were dwarfed by the double-digit inflation throughout the 1970s, averaging 16.1 percent per year for 1971-1975 and 11.7 percent for 1976-1980. The increased inflation rates have been attributed to the turbulent external conditions, in particular, the oil-price shocks and worldwide inflation through the 1970s. Moreover, it was claimed that such policy-responses were in some sense inevitable if growth was not to be arrested.

Apart from implementing statistical tests of causality, one manner of approaching the issue is to compare the Philippines' performance with that of countries in a similar situation. Thailand's economic performance serves as a good reference point. Over the same period of adverse external conditions, Thailand pursued a generally more conservative monetary policy than the Philippines did, with monetary growth at 12.6 and 15.5 percent for the periods 1971-1975 and 1976-1980, respectively, compared with the Philippines' 16.8 and 17.0. Consequently Thailand's inflation rate was markedly lower than that of the Philippines: 9.0 as against 16.1 percent in 1971-1975, and 10.5 as against 11.7 percent in 1976-1980. Neither was it true that a more conservative monetary policy would necessarily have led to lower growth, for in the same two periods Thailand's growth of real GNP exceeded even that of the Philippines, i.e., 6.3 as against 6.1 in 1971-1975, and 7.6 as against 6.3 in 1976-1980. Such comparative data suggest that the Philippines' higher inflation or lower economic growth could have been avoided and could be attributed, not to the general problems of a developing country, but to the character of the policies of the present government. There is empirical evidence suggesting that lax fiscal and monetary policies exacerbated the inflationary pressures exerted by the rise in the prices of tradeables, particularly oil. During the 1980s the gap between the performance of the country and that of its ASEAN neighbors widened further. While the onset of world recession perceptibly affected growth rates of real output in all countries, the Philippines posted the most serious declines. This happened despite the government's decision to pursue a "countercyclical" policy. While

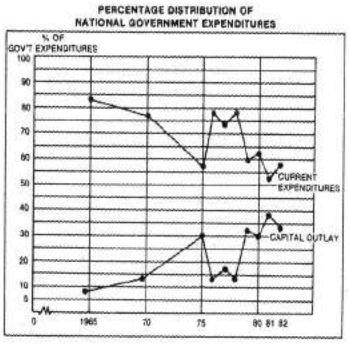
Such comparative data suggest that the Philippines' higher inflation or lower economic growth could have been avoided and could be attributed, not to the general problems of a developing country, but to the character of the policies of the present government.

monetary growth was low during this period,[18] most of the new credits were nevertheless used to finance unprecedented government deficits (Table 4, Lines 6-8), which constituted almost four percent of GNP. Consequently there was no significant easing up in the inflation rate, which would otherwise have occurred normally during a recession.

Capital expenditures or "investment" seem to occupy a higher level on the government's scale of social priorities than current expenditures or "consumption."

It has always been considered an achievement of sorts by the present government that they have managed to run a surplus on current expenditures. Overall deficits by the government are then justified (again plausibly) by the fact that they have in effect been incurred for capital outlays, i.e., infrastructure, equity contributions to government corporations, and others. Capital expenditures or "investment" seems to occupy a higher level on the government's scale of social priorities than current expenditures or "consumption." Hence, a peso would be better spent on a bridge or building rather than in raising public schoolteachers' salaries. However, such a presumption is not self-evident. If the current or potential gains to be had from an investment project are to be enjoyed mainly by the wealthy or, even worse, if the project itself is obviously wasteful, then it might be better socially to allocate the resources to consumption by the poor rather than to sink them into the project.

PERCENTAGE DISTRIBUTION OF NATIONAL GOVERNMENT EXPENDITURES



A significant amount of the government's capital expenditures would seem to have been allocated to low-productivity uses, or those which contributed insignificantly to the supply of goods and services. While they created demand, especially as they involved construction or the establishment of new bureaucracies, they produced little output, and this has led to inflationary pressures quite apart from those contributed by external shocks. To some extent, all investments are initially inflationary, whether they prove ultimately productive or not, since by definition, these involve the expenditure of available resources in anticipation of output that will be available (if ever) only in the future. However, the defense that the present difficulties arose only because such investments were of "long gestation by nature" or had a "long payback period" is untenable. In the first place, the period under investigation is more than a decade and hence, there is sufficient time for prospective returns from such prospects—if any had indeed been forthcoming—to be reflected in increases in real output. That the government's program of investments has, as a whole, been unable to keep up with payments on loans taken out from domestic and foreign creditors is an indicator that the majority of them were badly placed. Of course the only decisive manner of settling this issue is to review carefully the whole borrowing program of the government and the uses to which the borrowings were put. Unfortunately for the independent researcher, no complete listing of

[18] Growth of M_1 in 1981-1982 was zero, but broad money (M_2) grew by 16 percent nonetheless, with net claims on the government (which reflects borrowing by the government) increasing by 53.6 percent.

projects has been forthcoming from the government, though such a list should be a matter for the public record.

Secondly, the cultivated popular impression is wrong that the bulk of the government's capital expenditures has always gone into the more conventional infrastructure (e.g., roads, bridges, schools, irrigation, etc.) which might come to mind when thinking of projects with "long gestation" or a "long payback period." Table 9 lists the amounts and shares of capital expenditures that went into infrastructure, corporate equity, and "other capital outlays" for the years 1970-1983. Between 1970-1976,

The cultivated popular impression is wrong that the bulk of the government's capital expenditures has always gone into the more conventional infrastructure . . .

Table 9

CAPITAL OUTLAYS OF THE NATIONAL GOVERNMENT

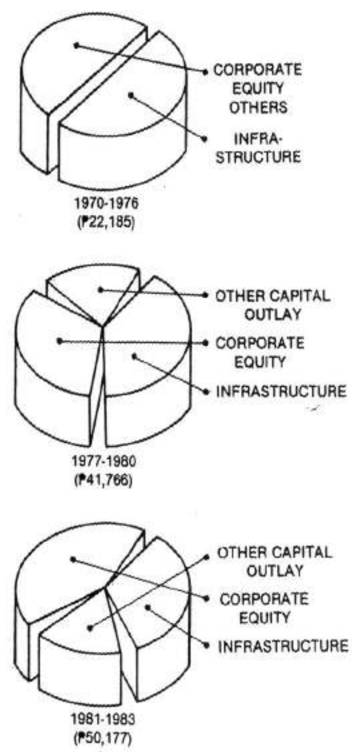
(Million Pesos)

	Infra-structure[a]	Corporate Equity Investment	Other Capital Outlays[b]	Total
FY 1970	433	293	—	726
FY 1971	425	392	—	664
FY 1972	679	532	—	1,211
FY 1973	1,111	1,172	—	2,288
FY 1974	1,877	2,981	683	5,336
CY 1975	4,089	1,693	978	6,760
CY 1976	2,700	2,000	500	5,200
Average Share for 1970-1976 (Percent)	(50.2)	(49.8)		(100)
CY 1977	2,900	2,300	1,200	6,400
1978	3,919	2,770	1,887	8,576
1979	5,229	3,907	2,356	11,492
1980	6,956	5,351	2,991	15,298
Average Share for 1977-1980 (Percent)	(45.5)	(34.3)	(20.2)	(100.0)
1981	6,148	10,809	2,385	19,342
1982	5,447	8,702	2,245	16,394
1983	6,346	4,346	3,749	14,441
Average Share for 1981-1983 (Percent)	(36.3)	(46.4)	(17.3)	(100.0)

[a]For FY 1970-1973 infrastructure outlays include expenditures of MPWTC and MPH and equity contributions of the national government to government corporations engaged in infrastructure projects. After 1974, this includes only MPWTC and MPH capital expenditures.

[b]For FY 1970-1983, this is called "non-infrastructure outlays" and includes equity contributions to government corporations involved in activities other than infrastructure and capital expenditures, and capital expenditures of ministries other than MPH and MPWTC. From 1974, non-infrastructure projects were broken down into "capitalization" and "other capital outlays."

CAPITAL OUTLAYS OF THE NATIONAL GOVERNMENT



infrastructure, it is true, constituted 50.2 percent of total capital outlays. However, this type of expenditure became increasingly less important from then on, being only 45.5 percent in 1977-1980 and 36.3 percent in 1981-1983. The category "other capital outlays," which included construction by ministries other than MPH and MPWTC, became more prominent after 1976, accounting for about one-fifth (20.2 percent) of total capital outlays in 1977-1980, where it had been negligible before. This was also the period, it will be recalled, when government construction expenditures were more than quadrupling (Table 4, Line 3). Eventually the construction expenditures carried out under this category would come to include the Manila Bay reclamation and building complex, the Batasan building, numerous official residences, building for NEDA, PNB, MWSS-LWUA, BIR, the Manila Governor's Office, the Central Bank Mint, Population Center, University of Life, and the three showcase medical centers, among others. The Philippines thus stands out in the region for the proliferation of government office buildings, many of which are overdesigned by Asian and developing-country standards. Office space has expanded partly to house a proliferating bureaucracy, and partly as a perquisite or amenity to high bureaucrats.

A different trend altogether emerged in 1981-1983, when corporate equity investments became the single most important capital outlay, exceeding the share of infrastructure . . .

A different trend altogether emerged in 1981-1983, when corporate equity investments became the single most important capital outlay, exceeding the share of infrastructure (46.4 as against 36.3 percent). This was largely related to the government's attempts to bail out certain large private firms which had gone under during the period, as well as some large nonfinancial public corporations which were themselves experiencing financial difficulties. Equity contributions went to the CB, PNB, Land Bank, and NDC to allow the takeover or the extension of new loans to the distressed and/or privileged firms. Nonfinancial public corporations themselves were recipients of equity contributions because of large deficits in their operations. The deficits of thirteen nonfinancial public corporations[19] alone in the period 1981-1983 averaged 3.8 percent of GNP. These deficits had to be financed by equity contributions from the government (which widened the overall budget deficits) or through foreign borrowings by these corporations themselves, which became part of public external debt.

The proliferation of new government corporations and various bureaucracies is another reason for the prominence of equity investments as a form of capital outlay. Especially where these have been established either to interfere extensively in various markets or to compete directly

[19] Namely: Philippine National Oil Company (PNOC), National Power Corporation (NPC), National Electrification Administration (NEA), Philippine Ports Authority (PPA), Philippine National Railways (PNR), Metro Manila Transit Corporation (MMTC), Light Rail Transit Authority (LRTA), National Irrigation Administration (NIA), Metropolitan Waterworks and Sewerage System (MWSS), Local Water Utilities Administration (LWUA), National Housing Authority (NHA), Export Processing Zone Authority (EPZA), and National Development Company (NDC).

with the private sector (See Section 3.1.3 on monopolies), it would be difficult to justify the new bureaucracies by any large economic contribution. On the other hand, an independent corporate structure could provide the financial flexibility and greater freedom from budgetary scrutiny on which bureaucrats could place a premium. Considering the overlapping responsibilities of many offices, red tape and plainly observable idleness, it is doubtful whether the size of the civilian bureaucracy is matched by its productivity.

The government's changing priorities are reflected in the budget allocation, which has altered drastically in the last twelve years (Table 10). The shares of so-called "economic services," public administration, and military spending have grown at the expense of social services. Education, which obtained as much as one-third of the budget in the 1950s and 1960s, got approximately twelve percent throughout the 1970s and early 1980s. Health has continuously been given a small allocation, five percent in 1970 and four percent in 1975. Where in 1965 social services accounted for 44.24 percent of the budget, in 1982 its share had fallen to 23.36 percent.

The shares of so-called "economic services," public administration, and military spending have grown at the expense of social services.

The idea that the state exists in order to deliver goods which markets cannot provide, or can provide only insufficiently to the poor, e.g., education, health-care, technical extension, etc., has been abandoned in favor of a concept where the state interferes prominently in markets for products, services and assets. This explains the apparently lower priority accorded social services by the government, compared to "economic services." The resemblance to socialism, however, is more apparent than real. The state's prominent economic role has not been accompanied by any social levelling but, as previously suggested, a worsening of the lot of the poorest in society. On the other hand, the expanded role of the state has encouraged its use as a tool to dispense economic privileges to private interests.

The potential for social conflict which the implementation of such an agenda could engender might explain why it entailed an expansion of the role of the military and its share of the budget.

The express commitment of the government to the alleviation of income inequality is hardly reflected in its fiscal policies. The tax structure continues to rely heavily on indirect taxes, which are regressive, or which penalize the poor more than the wealthy. Fiscal spending, on the other hand, has emphasized areas of doubtful mass benefits, such as the military, public buildings and monuments, subsidies to a few private firms, maintenance of large bureaucracies, tourist structures, etc. Progressive expenditures such as education and health have suffered a large drop in share from 33.5 percent in 1970 to 21.5 percent in 1982. Even within the social services budget there is increasing allocation to the less

The tax structure continues to rely heavily on indirect taxes, which are regressive, or penalize the poor more than the wealthy.

Table 10

PERCENTAGE DISTRIBUTION OF NATIONAL GOVERNMENT EXPENDITURES

National Government Expenditures	1965[a] 100.00	1970 100.00	1975 100.00	1976[a] 100.00	1977 100.00	1978 100.00	1979[a] 100.00	1980[a] 100.00	1981[a] 100.00	1982[a] 100.00
A. *By Economic Classification*										
1. Capital outlay	14.57	19.16	38.66	18.82	20.94	18.50	35.88	34.14	43.14	38.16
2. Current expenditures	85.43	80.84	61.34	81.18	79.06	81.50	64.12	65.86	56.86	61.84
a) Personal services	55.77	46.75	23.55	26.96	27.79	26.89	24.95	26.23	23.58	24.55
b) Maintenance and other expenses and transfers	24.66	28.08	32.78	49.13	43.95	46.50	30.18	28.83	26.04	28.55
c) Debt service	5.00	6.01	5.01	5.09	7.32	8.11	8.99	10.80	7.23	8.74
B. *By Sectoral Classification*										
1. Economic services	16.74	31.66	45.52	35.47	34.53	38.70	40.51	42.36	43.23	42.42
2. Social services	44.24	34.86	18.98	20.80	21.97	22.15	20.84	20.24	22.68	23.36
a) Education	36.54	27.95	11.61	12.34	12.27	12.95	10.96	11.76	12.73	12.44
b) Health, housing and population	6.18	5.58	4.12	5.00	5.57	6.10	8.13	6.64	8.21	9.03
c) Others	1.53	1.33	3.24	3.46	4.13	3.10	1.76	1.84	1.74	1.83
3. National defense	16.74	15.17	20.90	17.56	22.66	12.88	14.36	12.00	10.61	11.22
4. General public service (including debt service)	22.28	18.31	14.59	26.17	20.83	26.26	24.28	25.39	23.48	33.00

[a]Government expenditures for these years differ for the two classifications, with the economic classification having generally higher values.

Source: *NEDA Statistical Yearbook*, 1982 and 1983.

progressive programs, such as higher versus elementary education, glamorous medical centers rather than primary health care with a wider clientele, plus such miscellanea as the University of Life.

3.1.2 The Government's Role in Financial Markets

As the government's share in total expenditures has risen over the last two decades, its role in the financial market has also expanded.

As the government's share in total expenditures has risen over the last two decades,[20] its role in the financial market has also expanded.

The government participated directly in this market through the state-owned banks and other government financial institutions (GFIs)—PNB, DBP, Land Bank, GSIS and SSS. Indirectly, it exerted its influence through the selective monetary policy adopted by the Central Bank (CB) which has ceased to be an independent institution from the administration, and through the special relationship between the government and some private banks, hereafter referred to as "political banks" or PBs[21] Under selective credit control the Central Bank extended rediscounting

[20]From less than 10 percent in 1961-1965 to almost 16 percent in 1981-1982.

[21]A term borrowed from Patrick and Moreno (1982).

privileges and loan rates differentiated so as to favor "priority activities." Rediscounting and the extension of CB credit to the government have been the most common means of expanding credit, and many banks, particularly those owned by the government, have become heavily dependent on CB credit as a regular source of funds. Only one-fifth of the loanable funds of PNB and DBP have come from deposits and other intermediated sources. Such a setup is thus partly to blame for the failure to mobilize sufficient savings, since the government and private financial institutions which could do so, found CB credit easier to obtain than attracting deposits or other forms of borrowing from the public.

Until the early 1970s the bulk of Central Bank loans to financial institutions (i.e., about 70 percent, Table 11) went to private commercial banks and rural banks. As CB credit was allowed to grow faster in the late 1970s, however, an increasing proportion went to the two state banks, PNB and DBP, as a result of which their share rose from less than 30 percent (1971-1975) to 45 percent (1981-1982). Most noticeable was the growth of DBP borrowing from the CB, beginning modestly at ₱20 million in 1960, rising to ₱74 million in 1970, then growing almost sixfold to ₱4.2 billion by 1980. This jumped further to ₱7.0 billion in 1982. On the other hand, PNB has always been a large CB borrower, absorbing about 20 percent of CB loans through the last three decades; its debts have thus grown parallel to the total, starting at ₱111 million in 1960 and reaching ₱7.5 billion by 1982.

Apart from CB borrowing, these GFIs also obtained a large share of the fast-growing external debt. In addition, PNB was the depository of the national treasury's cash account, while DBP issued bonds held by the CB and other financial institutions. All these developments led to the concen-

All these developments led to the concentration of loanable funds in the government banks and, therefore, their direct control by the ruling group in government.

Table 11

PERCENTAGE DISTRIBUTION OF CENTRAL BANK LOANS AND ADVANCES

	DBP and LBP	PNB and PVB	Rural Banks	Private Commercial Banks	Private Thrift Banks and Others	Total
1965	6.4	20.2	12.6	58.1	2.7	100.0
1970	5.9	20.1	10.3	59.7	4.0	100.0
1971-1975	10.2	16.8	18.0	50.2	4.8	100.0
1976-1980	20.5	19.1	16.3	27.6	16.5	100.0
1981-1982	22.8	22.3	11.6	31.4	11.9	100.0

Sources: *CBP Factbook: Philippine Financial System*, 1978-1982.
CBP, *Statistical Bulletin*, 1976-1980.
CBP, *Financial Statistics*, Vol. IV, 1981.

tration of loanable funds in the government banks and, therefore, their direct control by the ruling group in government. The combined assets of four GFIs (DBP, PNB, LB, PVB) amounted to ₱113 billion in 1982, compared to the ₱143 billion assets of twenty-eight private commercial banks.

To assess properly the extent of concentration in the financial system, one must also consider the political banks or PBs which, by virtue of their special relationship with the group in government, could be presumed to respond to broadly similar imperatives as the government financial institutions. There are at least eight such banks which are considered here. They control 27 percent of total private commercial bank assets. The total assets of the political banks and the government financial institutions make up at least 53 percent of the assets of the entire commercial banking system, and may be regarded as a measure of concentration.

While Central Bank credits to individual commercial banks are not clearly reported in financial statements, they are embedded in the account "Bills Payable." Six banks show extraordinarily large "Bills Payable" in their liability portfolio, with a range of 29 to 63 percent.[22] Apart from one which has a tieup with a multinational, the others either have links with the present administration or are failing banks which were rescued by the CB through an infusion of new credit. Those political banks which seem to be meeting with success, on the other hand, have been able to do so based on either a previous accommodation by the Central Bank (e.g., exceeding the rediscount ceiling by three times), a monopoly over the financial resources of an industry which its affiliates control, or a takeover of various enterprises owned by a powerful oligarch before martial rule.

What is of concern from an economic viewpoint, however, is not the legality or morality of the origins of wealth accumulation but the uses to which such investible resources are put, as well as the resources exhausted in trying to capture such wealth.

What is of concern from an economic viewpoint, however, is not the legality or morality of the origins of wealth accumulation but the uses to which such investible resources are put, as well as the resources exhausted in trying to capture such wealth.

A common feature of industrial structure in many developing countries is its organization according to large "Groups" or conglomerates whose interests could include foreign trade, extractive industries, or manufacturing, usually with their own banks (Leff 1979). In the Philippines, Doherty (1980) has documented the existence of such groups by looking at interlocking directorates. In effect the favored banks who are members of such conglomerates act as conduits of cheap credit from the Central Bank and foreign banks to their affiliated enterprises. Relative to other firms in the industry, therefore, those belonging to these conglomerates were privileged in having a cheap source of

[22] Namely: Republic Planters Bank, International Corporate Bank (Interbank), Philippine Bank of Communications, Union Bank, Associated Bank and City Trust.

credit. The behavior of the GFIs did not seem to be significantly different from that of the political banks, and the conglomerates have obtained privileged credit not only from their own politically connected banks but also from the government's financial institutions. Loans by the GFIs to favored borrowers tended to be large, reaching the billions, such as in the case of the Marinduque Mining Company's ₱15 billion debt, Delta Motors' ₱2 billion debt, or the four-billion peso rescue of a handful of privileged enterprises (among them, CDCP, etc.). Inevitably such favored borrowers absorbed a disproportionately large part of the GFIs' loan portfolio.

The implicit guarantee of existence independently of one's economic performance, which monopoly implies, encourages bad decision-making, and it can only be fortuitous that the grant of such privileges will coincide with economic ability and business acumen. As it has turned out, many of the favored clients of both the GFIs and the political banks encountered severe business difficulties, and when these companies failed, both the GFIs and the political banks involved also got into trouble financially. Examples are the failures of the Disini, Cuenca, and Silverio groups of companies. Apart from the waste of resources, bankruptcies reduce the supply of credit to new borrowers, which should normally come from repayments. In the past, poor performance of the GFIs' portfolio tended to be made up for by infusion of fresh CB credits or by foreign borrowing, so that to some extent new borrowers could still be accommodated. Under the present circumstances where CB credits are to be restricted, however, the supply of new loans will definitely have to be reduced. Whether the already restricted supply will even be used to indiscriminately grant favors to some entities is still an open question.

As it has turned out, many of the favored clients of both the GFIs and the political banks encountered severe business difficulties, and when these companies failed, both the GFIs and the political banks involved also got into trouble financially.

Such financial mismanagement has exacted a large toll on the economy. Inefficient enterprises managed by entrepreneurs untested by business experience crowded out higher-productivity activities. The cost of inefficiency and waste may be seen in the rise in the incremental capital-output ratio and the deceleration of output growth relative to that of other countries long before the present crisis occurred.

Finally the impact of such policies on the distribution of income and wealth must be noted. The government's expressed objective of evening out sectoral imbalances which contribute to income inequality through such programs as extending financial support to small and medium as against large firms, and to agriculture as against industry does not seem to jibe with the lending practices of the GFIs. Credit in DBP and PNB has been channelled heavily to large industrial enterprises and in the form of nonagricultural loans. At DBP the share of small loans (₱50,000 and below) was only five percent in 1980, while that of large loans (over ₱1 million) was 80 percent. The distribution is likely to be similar at PNB which is also reportedly heavily committed to large favored borrowers. The share of agricultural loans out of total loans at DBP dropped from

30 percent annually in 1973-1977 to 10.6 percent in 1978-1982. In the case of PNB, it dropped from an annual average of 15.1 percent in the first period to 8.5 percent in the second period.

3.1.3 Government-Mandated Monopolies

The present government has encouraged and, in many instances, directly participated in the deepening monopolization of various sectors of the economy, including the most vital ones.

The present government has encouraged and, in many instances, directly participated in the deepening monopolization of various sectors of the economy, including the most vital ones. On the one hand, it is true that government intervention and monopoly have a valid place in the corpus of economic theory. Where a process requires large-scale operation but is otherwise economically viable; where a project yields a social benefit yet cannot be made to produce a private profit (e.g., pure research); or where an infant industry makes losses in initial years which are, however, compensated by expected future earnings—in all these and in a few other cases, government intervention and/or monopoly have a role to play. Otherwise, the majority of economists would look with suspicion upon such departures from market competition. Unless the contrary could be explicitly justified, it would be presumed that such departures from competition would lead to losses in efficiency and a greater inequality.

The monopolist or monopsonist may, in the meanwhile, reap a higher than average profit from such transactions, or may choose to utilize its privilege in the form of inefficiency and inertia.

The short-term losses from monopolization have long been familiar and comprehensible to the public. For the consumer who has to confront it, monopoly means higher prices that must be paid, or inefficiency, or low quality. The producer who confronts a monopsony (a sole buyer) finds he is paid less for his goods, or is able to sell less of them. The monopolist or monopsonist may, in the meanwhile, reap a higher than average profit from such transactions, or may choose to utilize its privilege in the form of inefficiency and inertia. Over the long haul, an economy plagued by monopolies could discover that its prospects for growth have been narrowed by the loss of the qualities of entrepreneurship and innovativeness. Historically, one of the more progressive aspects of early capitalism was its abolition of the privileges of feudal monopolies and privileges which stifled competition and caused a drag on productive efficiency. The variety and ubiquity of the assignment of economic privileges in the country at present give one cause to ponder what economic system (not to mention historical era) actually obtains.

Appendix 1 lists 688 presidential decrees and 283 letters of instructions which represent government intervention in the economy in one form or another. One could only argue with difficulty that the majority of instances of government intervention which granted some privilege to some public or private corporation could be justified by an appeal to either economic efficiency or equity. If not, then what might be a plausible social-scientific explanation for such massive intervention? One hypothesis is that this has been the result of the concentration of decision-making in the executive and the domination of certain private interests over the government. This argument is corroborated by the fact that the great majority of such grants of privileges have been accomplished through actions of the executive, i.e., presidential decrees, letters of instructions, hence, without benefit of discussion even in the compliant interim Batasan. The issuance of exclusive rights to import, export, or exploit certain areas, the collection of large funds which are then privately controlled and expropriated, and the preferential treatment of certain firms in an industry for purposes of credit or credit-restructuring are among the many instruments that have been utilized in the process. One good example is the assignment of the exclusive right to import peroxide to Peroxide Philippines (LOI No. 1255).

In some instances, a governmental regulatory authority such as the Philippine Sugar Commission (Philsucom) or the Philippine Coconut Authority (Philcoa), controlled by selected segments of the industry, has been the basis by which monopolistic control over the industry has been achieved.

Government decrees or LOIs have also been applied to exempt some corporations, including public corporations, from the laws of the land itself. Tariff exemption for the importation of sugar production equipment (PD 924), for the PHIVIDEC Industrial Authority (PD 538), tax exemption for the Security Printing Plant (PD 783) or NIVICO's exemption from tariffs on imported TV sets are examples of this operation. The tariff exemptions are a special cause for concern, since they result in the loss of control over the trade balance. A task for research is to inquire into the extent such exemptions from import duties have contributed to the overall propensity to import non-oil products, which has been observed to grow in recent years. Such exemptions may also lead to overestimation of the actual level of protection. Of course, such privileges also grant unfair advantage to favored firms in terms of lower costs of imported components.

The tariff exemptions are a special cause for concern, since they result in the loss of control over the trade balance.

In other instances, the setting up of public corporations (e.g., Philippine Cotton Corporation, PD 1063; the National Fertilizer Corporation, PD 992; the Philippine Aerospace Development Corporation, PD 696) are the instruments of intervention. That their activities seem to be in direct competition with private enterprises and that their operations are apparently sustained only through the continuation of government subsidies should be the object of anxiety. In general, independent private sector initiatives should be preferred since they tend to result in more permanent contributions to development.

Finally the effect of the monopolization process on income distribution needs to be pointed out. The grant of monopolistic privileges will almost certainly have enriched those who obtained them. Whether this has been at the expense of the businessmen, the middle class, the workers or farmers in the affected industries should be the object of a deeper study.

. . . an inordinate amount of social and economic power has been transferred into the hands of a small group in society, as a by-product (if not the objective) of the imposition of an authoritarian regime.

What is not in doubt at the moment, however, is that an inordinate amount of social and economic power has been transferred into the hands of a small group in society, as a by-product (if not the objective) of the imposition of an authoritarian regime.

The rest of this section discusses the process of monopolization and its consequences in the sugar and coconut industries, which have been chosen because of their importance, and also because they are illustrative.

3.1.3.1 The Sugar Industry

But where other countries tend to subsidize the sugar producer by buying domestically at high prices and dumping the excess on the world market, the net effect of Philippine sugar policies, particularly from 1974 to the present, has been to penalize the producer.

Government intervention in the sugar economy is not unique to the Philippines. Sugar has been the target of stabilization schemes in many countries and it is this very intervention that has caused unusually large fluctuations in the international free market prices of the commodity. But where other countries tend to subsidize the sugar producer by buying domestically at high prices and dumping the excess on the world market, the net effect of Philippine sugar policies, particularly from 1974 to the present, has been to penalize the producer.

The extent of direct government intervention has increased over the years. It started with the simple allocation of sugar output between exports and domestic use (Act #4166, 1934). Then government decided to regulate production and consumption in order to stabilize prices (RA 632, 1951). Direct market intervention through the imposition of price ceilings at all points of the marketing chain (Philippine Sugar Order #2, Series of 1966-1967), was the next step. Then, in 1974, the government started its monopoly, effectively nationalizing sugar trading, both domestic and export (Circular Letter #24, Series of 1973-1974, PD 579, 1974),[23] with the disposition of sugar needing the prior approval of the President of the Philippines. Finally, the government also got involved in sugar milling (PD 1890, 1983).

The question that must be posed is: what was the gain enjoyed or the loss suffered by the sugar producers as a result of the government's increased intervention, i.e., its monopolization of the sugar trade?

The question that must be posed is: what was the gain enjoyed or the loss suffered by the sugar producers as a result of the government's increased intervention, i.e., its monopolization of the sugar trade? To answer this, one can compare what producers would have received if they had been able to sell at free market price with what they actually received under the monopoly (first from PHILEX and then from National Sugar Trading [NASUTRA]) in both the export and domestic markets. The time period under consideration covers crop years 1974-1975 to 1982-1983.

In the export market, the average revenues received by the sugar producers under conditions of free trade may be computed as the US #11

[23] PD 388, the Philippine Sugar Commission Decree, was enacted earlier than PD 579, which made the Philippine Exchange Company (Philex) sole buyer of sugar from sugar mills and sole exporter of sugar. However, Philsucom did not commence operations until 1977.

spot prices, less 10 percent trading charges to cover freight, insurance, taxes, etc.[24] If the difference between the price paid by NASUTRA (monopoly price) and the "free trade" price was positive, this would imply a subsidy to producers, and if negative, would imply a tax. These differences, multiplied by the corresponding export volumes were then summed up algebraically, and the result constitutes an estimate of the total gain or loss to producers.

Two estimates were made based on different assumptions regarding the trading behavior of producers. The first estimate assumes that producers would trade at the monthly average of the current "free trade" price, except for crop year 1982-1983 (Assumption I). In that year the U.S. allocated a renewed quota of 343,000 metric tons to the Philippines at a price of $0.1992. This was much higher than the U.S. spot price, and so a weighted average of the two prices was used.

Under these assumptions, sugar producers suffered a net loss of ₱2.6 billion in the period, as shown in Table 12. Although the monopoly price was higher than the "free trade" price in six of the 10 time periods studied, the small positive differences were not enough to compensate for the large negative differences in the other four periods.

The second estimate assumes that producers, if left alone, would have made the same trading decisions as NASUTRA, i.e., entered a four-year contract starting in January 1981, to export 620,000 metric tons at an average of $0.235/lb. (Assumption II). Table 13 shows that under these circumstances, the loss to producers as a result of government trading monopoly of exports amounted to a much larger ₱5.4 billion for the period 1974-1983. This is because the monopoly price exceeded the free trade price in only four of ten time periods, and these positive differences were very small.

Turning now to the effect of government monopoly in the domestic market, the gain/loss to the producers is computed in a similar manner as above. The difference between the government's buying price for domestic sugar and what the producer could have received if he were able to sell in the free market constitutes his gain or loss.

Table 14 shows that because the domestic sugar prices were set lower than the export prices, the sugar producers suffered even more losses. The estimate of this loss, over the nine-year period, amounts to ₱9 billion. One should note that this is an underestimation of the total

[24]From interviews with firms and individuals connected with international sugar trading before the government monopoly, the usual trading charges are eight percent.

Thus, the monopolization of the sugar trade which took place in 1974 has resulted in a loss to the sugar producers of anywhere from ₱11.6 billion (₱2.6 + ₱9.0 billion) to ₱14.4 billion.

Table 12
GAINS (LOSSES) OF SUGAR PRODUCERS DUE TO MONOPOLY OF EXPORT TRADE, CROP YEARS 1974 TO 1983, ASSUMPTION I[a]

Period[b]	Free Trade Price[c] (per picul)	Monopoly Price[d] (per picul)	Difference	Total Gain (Loss) (million pesos)
		PHILEX		
10/17/74—5/5/75	₱334.23	₱180.00	(₱154.23)	(₱1,941.7)
5/5/75 —3/22/76	138.65	130.00	(8.65)	(136.7)
3/22/76—12/2/76	108.03	125.00	16.97	291.6
12/2/76 —6/13/77	81.77	90.00	8.23	175.7
		NASUTRA		
6/13/77—3/30/79	71.86	90.00	18.14	733.0
3/30/79—8/31/79	76.48	90.00	13.52	114.8
Crop Year 1979-1980	199.17	135.00	(64.17)	(1,638.2)
Crop Year 1980-1981	239.69	172.50	(67.19)	(1,647.4)
Crop Year 1981-1982	107.30	168.00	60.70	1,058.8
Crop Year 1982-1983	145.93[e]	168.00	22.07	422.7
TOTAL GAIN (LOSS) (PHILEX & NASUTRA)				(₱2,567.4)
TOTAL GAIN (LOSS) (Under NASUTRA operations only)				(₱ 956.3)

[a] This assumes that producers would have sold at the average of U.S. spot prices.

[b] Periods are divided according to effectivity dates of liquidation prices per Sugar Orders from the relevant government agency (PHILEX and the NASUTRA).

[c] U.S. #11 spot prices as taken from *ISO Sugar Yearbook,* less 10% allowance for trading charges.

[d] Before July 1977, prices set by Sugar Quota Administration for PHILEX; after July 1977 prices set by NASUTRA.

[e] Weighted average of U.S. spot and U.S. quota prices of $0.2204/lb. for 343,000 metric tons.

Sources: NASUTRA files; Free Trade Price is U.S. #11 spot price as taken from International Sugar Organization (ISO). We thank Alfredo T. Villa for pointing out the typographical error that appeared in this table in the draft.

producers' loss, because the volumes used are those for sugar consumption, rather than for sugar production minus exports.[25]

Thus, the monopolization of the sugar trade which took place in 1974 has resulted in a loss to the sugar producers of anywhere from ₱11.6 billion

[25] One reason for choosing consumption is that the estimated amount would be an approximation of the consumers' subsidy. (This is essentially the approach taken by Nelson and Agcaoili). A confidential World Bank Report estimates consumer subsidy for the years 1979-1981 to average 81 million pesos yearly. The other, more practical reason is that production figures could not be found which were comparable to export figures.

(₱2.6 + ₱9.0 billion) to ₱14.4 billion. Such losses may or may not have served as a disincentive to greater productive effort. What is evident in the sugar statistics is that the area planted to centrifugal sugar between 1974 and 1982 decreased very slightly, as did total production, with yield per hectare increasing although also slightly.

In terms of the domestic marketing chain, the nationalization of the sugar trade effectively added at least one more link since the producers could no longer sell directly to the traders, but had to sell output to PHILEX, and later, to NASUTRA. The government agency then allocated

In terms of the domestic marketing chain, the nationalization of the sugar trade effectively added at least one more link...

Table 13

GAINS (LOSSES) OF SUGAR PRODUCERS DUE TO MONOPOLY OF EXPORT TRADE, CROP YEARS 1974 TO 1983, ASSUMPTION II[a]

Period[b]	Free Trade Price[c] (per picul)	Monopoly Price[d] (per picul)	Difference	Total Gain (Loss) (million pesos)
		PHILEX		
10/17/74—5/5/75	₱334.23	₱180.00	(₱154.23)	(₱1,941.7)
5/5/75—3/22/76	138.65	130.00	(8.65)	(136.7)
3/22/76—12/2/76	108.03	125.00	16.97	291.6
12/2/76 —6/13/77	81.77	90.00	8.23	175.7
		NASUTRA		
6/13/77—3/30/79	71.86	90.00	18.14	753.0
3/30/79—8/31/79	76.48	90.00	13.52	114.8
Crop Year 1979-1980	199.17	135.00	(64.17)	(1,638.2)
Crop Year 1980-1981	235.11	172.50	(62.61)	(1,525.2)
Crop Year 1981-1982	175.36	168.00	(7.36)	(128.4)
Crop Year 1982-1983	237.82	168.00	(69.82)	(1,337.3)
TOTAL GAIN (LOSS) OF PRODUCERS UNDER NASUTRA				(₱3,761.3)
TOTAL GAIN (LOSS) UNDER PHILEX				(₱1,611.1)
TOTAL GAIN (LOSS) FROM CY '74 TO CY '84				(₱5,372.4)

[a] Assume that the traders would have signed the same long-term contracts signed by NASUTRA of $0.235/lb. for crop year 1980-1981 to crop year 1983-1984 involving 620,000 metric tons annually.

[b] Periods are divided according to effectivity dates of liquidation prices per Sugar Orders from the relevant government agency (PHILEX and the NASUTRA).

[c] U.S. #11 spot prices as taken from *ISO Sugar Yearbook*, less 10% allowance for trading charges.

[d] Before July 1977, prices set by Sugar Quota Administration for PHILEX; after July 1977 prices set by NASUTRA.

Table 14
GAINS (LOSSES) OF SUGAR PRODUCERS DUE TO MONOPOLY OF DOMESTIC TRADE, CROP YEARS 1974 TO 1983

Period	Consumption of Sugar (metric tons)[a]	Difference Between Domestic Price and Free Trade Price (pesos per picul)[b]		Gains (Losses) (million pesos)
1974-1975	874,986	(284.43)		(₱3,927)
1975-1976	723,168	(72.06),	(60.26)	(755)
1976-1977	911,650	(60.26),	(30.86)	(655)
1977-1978	874,203		10.15	140
1978-1979	1,086,708	10.15	25.02	301
1979-1980	1,103,176		(111.30)	(1,937)
1980-1981	1,041,312		(156.30)	(2,568)
1981-1982	1,050,706		20.78	348
1982-1983	1,100,000		2.85	49
TOTAL LOSS				₱9,009

[a] *ISO Sugar Yearbook.*

[b] Parenthesis refers to negative difference.

the sale of sugar to domestic traders. No official information on the domestic sugar allocations can be secured, nor can the criteria for allocation be identified. Charges of using sugar allocation as a means of dispensing political favors or distributing largesse cannot therefore be properly investigated. If these were true, the effect would be to lengthen the marketing chain by still another link, since the "paper" traders could then turn around and sell their allocations to actual traders. The end result would most likely be either an increase in the consumer price because of additional mark-ups, a redistribution of income from actual traders to paper traders, or some combination of both.

In the export trade, government agencies have displaced international traders. If the government agencies have obtained better terms for sugar export than private traders, there would be a net national gain and the takeover of trade might be justified. Hence, it is valid to ask: What has been the trading performance of the government agencies? How efficient have they been?

The first question can be answered by comparing the average US #11 spot price with the actual export unit value (FOB) of sugar for the period under study. The trading performance can be considered average, better or poorer than average depending on whether the export unit values are the same, higher, or lower than the U.S. spot prices. For the whole period under consideration, the trading performance of the government agencies was slightly poorer than the market average, so that their existence did not result in higher prices than could have been obtained on the average in the world market. There was a slight loss in foreign exchange earnings as a result of their operations.

For the whole period under consideration, the trading performance of the government agencies was slightly poorer than the market average, so that their existence did not result in higher prices than could have been obtained on the average in the world market.

The efficiency of the government trading agencies, on the other hand, might be gleaned from their operating performance. NASUTRA's trading costs were at least 18 percent of purchase price in 1978. It is assumed that "cost of sales" was the amount paid to producers, and trading costs include expenses other than administrative and general expenses. For crop years 1979 and 1980, NASUTRA pegged trading costs of U.S. 2¢/lb., and for the succeeding crop years, at 3¢/lb. This represents a range of from 8 to 17 percent of their average selling prices, and from 11 to 21 percent of the purchase price from producers. The industry average, prior to monopoly, was eight percent.

With respect to operating profits, reports state that NASUTRA assumed an outstanding loan of ₱1.887 billion from PHILEX, which implies operational losses on the part of the latter. This cannot be divorced from Nelson and Agcaoili's finding that PHILEX's stocks were largest when world price was highest, while its sales were largest when world price was lowest.

NASUTRA's operating performance is indicated in Table 15. The total operating loss of NASUTRA for the calendar years 1978-1981 was over ₱1 billion. This is in spite of the fact that gross profit on exports (as measured by export revenues minus purchase costs) for the comparable period amounted to ₱1.25 billion, implying that overhead costs must have exceeded gross profits from export sales by ₱2.25 billion. Worse, foreign exchange in the amount of $377 million was used to finance their operations.

The total operating loss of NASUTRA for the calendar years 1978-1981 was over ₱1 billion.

Table 15
NASUTRA'S OPERATING PERFORMANCE, 1978 TO 1981

	CY 1978	CY 1979	CY 1980	CY 1981	Total
Total Income (million)	₱2,983.86	₱3,694.49	₱6,932.32	₱7,113.50	₱20,724.17
Total Expenses (million)	3,568.48	4,297.76	6,890.72	6,977.18	21,734.14
Net Income (loss)	(₱ 584.62)	(₱ 603.27)	₱ 41.60	₱ 136.32	(₱ 1,009.99)

Source: Commission on Audit.

To conclude, the presence of monopoly in the sugar trade has resulted in the following:

a) a loss to the producers of between ₱11 billion and ₱14 billion over the period under consideration;

b) an addition to the marketing chain resulting in either more mark-ups, a redistribution of income from actual traders to favored "paper" traders, or both;

c) no increase in trading efficiency, and therefore no increase in foreign exchange earnings (total export revenues are even slightly less than total revenues that would have accrued to producers in the free market);

d) a loss of foreign exchange due to the financing of operations through foreign loans; and

e) a loss to the economy because of the operating losses of the agencies, in spite of estimated gross profits enjoyed from the differential between export revenues and purchase costs.

Since 1966, at least a dozen sugar mills (out of the total of 42 in the country) have been constructed by foreign companies at government-approved costs. At the time they were built, questions were raised in the Senate Blue Ribbon Committee regarding 1) the wisdom of contracting with Japanese firms which have no previous experience in mill construction; and 2) the disparity between the contracted costs of mill construction in this country and mills of equivalent capacity in other countries.

The effects of government intervention in milling are the following:

a) an increase in foreign debt by $508 million, represented by letters of credit issued by PNB for the mills' construction;

b) losses of the mills due to insufficient cane supply (excess capacity), poor infrastructure and minimal capital investment of owners; and

c) adverse effect on PNB's liquidity position because of overdue loans amounting to ₱1.5 billion.

The latest government move with respect to the sugar mills has been the creation of the Philippine Sugar Corporation, in recognition of "obligations of sugar mills acquired at heavy financing cost . . ." and as part of the declared "governmental policy to continue assisting the sugar industry through a government corporation especially charged and empowered to design and implement a program for sugar mills, refineries, and other sugar facilities" [PD 1890, November 14, 1983].

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The latest presidential decree with respect to the sugar trade makes export trading through NASUTRA a voluntary matter starting in crop year 1984-1985. The impact of this move has yet to be studied, but the initial reaction of planters, which may be justified, is that unless they deal through NASUTRA, they might find it difficult to obtain their crop loans. So although the move is ostensibly toward free trade, there may be no actual change in practice.

3.1.3.2 The Coconut Industry

The program to "rationalize" the coconut industry has resulted in a monopsonization of the industry to the detriment of the producers, and inefficiencies in marketing operations with a consequent reduction in national earnings. On the other hand, it has yet to generate significant positive net benefits.

The program to "rationalize" the coconut industry has resulted in a monopsonization of the industry to the detriment of the producers.

The material basis of the program was the collection of the coconut levy (legally defined as private contributions to a stabilization fund) at an average annual rate of ₱1 billion. This fund was supposed to have been applied to the replanting and other development programs in the coconut industry.

Because it is a private fund, it is not subject to public audit even though it is collected by force of law for the purpose of a national program. For the replanting scheme, the contract for supplying the new seed nuts was awarded to a single firm, Agricultural Investment Inc. (AII). To date, the replanting program has had no significant impact.

Another stated purpose of the fund is to generate direct benefits exploitable from a large pooled fund for its contributors, the coconut farmers. However, the benefits that have been available from this fund have been limited to contingent benefits—benefits that are available only if certain criteria are met such as life insurance, educational scholarships, and the cooking oil subsidy. The great majority of the contributors to the fund are not qualified to benefit from the fund (Clarete and Roumasset, 1983).

The fund has been used mainly to purchase the United Coconut Planters Bank (UCPB) and to organize the United Coconut Oil Mills, Inc. (UNICOM), a private milling and marketing company for coconut products. The UNICOM has captured over 75 percent of the country's milling capacity. The unorganized coconut farmers, while nominally 70 percent owners of UCPB, have really no effective control over UCPB and UNICOM, the latter being the company that buys most of the industry output.

Because of monopsonization of the local coconut trade, UNICOM paid 9-15 percent below the price it would have paid under competitive conditions to coconut farmers (based on Clarete and Roumasset, 1983). The evidence is very strong that the burden of the levy has been borne by the Filipino farmers and has not been passed on to the international buyers.

Because of monopsonization of the local coconut trade, UNICOM paid 9-15 percent below the price it would have paid under competitive conditions to coconut farmers.

Thus the country's coconut farmers, the front-line producers of the industry, have experienced losses in two ways. *First,* the levy was collected into an abstract fund which they theoretically but not effectively controlled. This fund has not improved their productive capacity because of the leisurely conduct of the replanting program; neither has it provided significant direct benefits. *Second,* the fund was applied to the monopsonization of the industry which has resulted in lower selling prices and incomes for the farmers.

Although it is conceivable that the sacrifices that have been contributed by the farmers will pay off in the long run when the ultimate objective of improving productive capacity has been achieved, the past record has not been exactly encouraging.

The concentration of the marketing operations in the UNICOM had been justified as a measure to increase marketing leverage in the international market. However, evidence for such an advantage has not been forthcoming in the case of coconut products. On the contrary, the attempt by UNICOM to exploit its limited monopoly power in the international market resulted in substitution away from coconut oil, and depressed national earnings.

However, the appropriateness of collecting the rehabilitation fund from farmers is extremely questionable.

On the other hand, the purchase of the milling capacity had been justified as a means of rehabilitating mills that experienced financial difficulties, many of which had outstanding obligations with government banks such as the DBP and the PNB. In many cases, the purchase had the intended effect of reducing the public exposure to these mills. However, the appropriateness of collecting the rehabilitation fund from farmers is extremely questionable. It would have been more advantageous to have sold the mills even at a loss to entrepreneurs who *either* would have operated them efficiently in a non-monopsonistic manner *or* would have disposed of the excess capacity.

Government intervention in the coconut industry illustrates many of the elements such intervention has had elsewhere:

1. use of the law to create and support private monopsonies and monopolies,
2. imposition of the burden of the program on the many small producers or users,
3. rehabilitation of selected financially distressed operations using public or quasi-public funds,
4. half-hearted commitment to the true objective of the program, and
5. use of mechanisms that prevent public accountability.

. . . these policies introduce developmental bottlenecks and unnecessary inefficiencies . . .

The combination of regulation, levies, and monopolization applied to many other industries such as cigarette filters, and even importation of books and journals is reminiscent of the granting of monopolies by special appointment of the king in feudal systems long ago transcended by many countries. While such policies might have enhanced stability and provided material support for state control in feudal societies, these policies introduce developmental bottlenecks and unnecessary inefficiencies in a developing country such as the Philippines because they result in:

1. the control of industries by persons and organizations who have no proven capability or commitment in their operation, and consequent periods of inefficiency, slow development and outright failures (very often, as in feudal times, the decisive qualification has been fealty);
2. private monopolization and monopsonization which impose losses on everyone, as was illustrated in the case of the coconut industry; and
3. the weakening of risk-taking activities backed up by hard work and earnest effort, as a result of the perverse and unpredictable assigning of rewards and incentives.

3.2 Foreign Trade and Foreign Debt

Why the country has incurred so much debt but does not have the capacity to repay is what the present government must explain to the people. The standard official explanation is that the crisis was due entirely to uncontrollable foreign events which raised import prices much more than export prices. This section, on the other hand, will try to show that government's response to external shocks left much to be desired and probably magnified the harmful effects on the economy of the deterioration in the terms of trade.

Why the country has incurred so much debt but does not have the capacity to repay is what the present government must explain to the people.

Two major oil price hikes in 1973-1974 and in 1979-1980 raised our fuel bill from $187.6 million in 1973 to $2.2 billion in 1980. The first major oil shock raised our fuel bill to over $600 million in 1974 but initially did not cause balance of payments problems because overall export prices increased faster than overall import prices (with 1972 = 100, the export price index in 1974 was 242 while the import price index was 211). However export prices fell after 1974. They had barely returned to 1974 levels in 1980 when they fell again after 1980. Meanwhile average import prices increased continuously with large jumps in 1979 and 1980 due to the oil price hikes (see Table 16).

There is, therefore, some truth to the assertion that the crisis would not have occurred were it not for uncontrollable external forces. Few developing countries which depend heavily on trade can suffer more than a 40 percent deterioration of their terms of trade over a span of 10 years without experiencing major economic difficulties. Yet we cannot put the blame completely on the rest of the world. Other countries—South Korea, Taiwan, and Thailand—also faced deteriorations in their terms of trade but are not in the same trouble this country is in.

Part of the reason we are now having greater difficulties than most of our neighbors is the manner the country's leadership responded to the external shocks. Exports might have been boosted, or imports curtailed

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Table 16

UNIT VALUE OF EXPORTS AND IMPORTS, 1973 TO 1981

(1972 = 100)

	Philippines		Exports of[a]		
	Exports	Imports	Industrial Countries	Oil Exporting LDCs	Non-oil Exporting LDCs
1973	145.1	128.8	109.8	125.7	121.1
1974	242.3	211.6	135.3	380.2	166.8
1975	192.8	219.6	150.4	395.5	163.4
1976	168.8	217.2	158.8	442.1	184.2
1977	171.3	241.1	169.4	479.3	208.0
1978	193.7	245.8	178.4	449.1	204.2
1979	236.2	270.1	200.0	638.1	232.6
1980	246.0	358.6	225.4	1,008.9	276.8
1981	240.6	398.6	237.7	1,222.8	303.1

[a]In SDR, figures were obtained by compounding year-to-year percentage changes in unit values.

Source: *NEDA Statistical Yearbook*, 1983.

more, but instead there was heavy reliance on foreign loans to pay for higher volumes of imports.

There was modest success in raising export volumes, which allowed the purchase of greater amounts of imported goods, despite the rapid increase in import prices. Two commodities contributed substantially to the increase in nontraditional exports—electronic products and garments. These two products accounted for 65 percent of the increase in nontraditional exports ($1.5 billion out of $2.3 billion) between 1972 and 1982. In addition, foreign workers' remittances grew from $111 million in 1976 to more than $1 billion in 1983.

That these three sources accounted for most of our new foreign exchange receipts from nontraditional sources is indicative of how the economy responded to the external shocks. It relied very heavily on sources that used relatively cheap Philippine labor but did not have strong linkages with the rest of the economy. Work was either done abroad, in export processing zones, or in factories designated as bonded warehouses, earning dollars for our country without disturbing or interacting with older, established industries.

As mentioned earlier, exports grew but failed to keep pace with imports because the prices of principal and traditional exports (copra, sugar, copper, etc.) lagged behind those of imports. The share of exports of goods and services in GNP reached a peak of 22.3 percent in 1974, fell to 18.6 percent in 1975, and exceeded 20 percent only once after 1974 (Table 17). The share of imports of goods and services, on the other hand, rose from 18.6 percent in 1972 to 26.2 percent in 1983 and was more than 25 percent in four years out of ten after 1973.

It cannot be said that the increase in the share of imports in GNP was due solely to higher import prices. At constant 1972 prices, the average share of imports rose from 18.8 percent in 1972-1977 to 20.3 percent in 1978-1983. Hence, quite apart from the fact that the country was paying higher prices per unit of imports, it was importing more per peso of real income.

Hence, quite apart from the fact that the country was paying higher prices per unit of imports, it was importing more per peso of real income.

The growth in the volume of non-oil imports despite the continuous depreciation of the peso in nominal terms is a point that needs dwelling on. As was already mentioned in Chapter 2, the nominal adjustments in the peso's value could not fully compensate for the fact that domestic inflation was much higher than that in the rest of the world. Nominal exchange rates fell only by 1.5 percent annually between 1973 and 1980, while inflation was running at 13 percent yearly during the period. It has also been argued here that the aggressive fiscal and monetary policies of

Table 17

SHARE OF EXPORTS AND IMPORTS IN GNP, 1972 TO 1983

(Percent)

	Exports/GNP		Imports/GNP	
	In Current Prices	In 1972 Prices	In Current Prices	In 1972 Prices
1972	17.8	17.8	18.6	18.6
1973	22.2	18.6	18.7	17.7
1974	22.3	15.4	25.4	19.9
1975	18.6	14.5	25.4	19.7
1976	17.5	16.4	24.0	18.8
1977	19.0	18.2	22.5	18.1
1978	17.7	16.8	23.2	19.7
1979	18.8	17.4	24.3	21.5
1980	20.4	19.1	26.1	21.5
1981	19.1	18.1	24.5	19.6
1982	16.7	17.7	23.6	19.8
1983	19.6	17.8	26.2	19.1

Sources: *NEDA Statistical Yearbook*, 1983.

NEDA National Accounts Staff, "Advance Estimates as of 27 December 1983: The National Income Accounts, CY 1981-1983."

the administration were primarily responsible for domestic inflation being above what was prevailing worldwide. In any event, the result was that, non-oil imports did not lose their attractiveness and, in some instances, they became even cheaper, relative to domestic substitutes.

In a sense, the half-hearted attempts to shift the country's trade strategy towards greater openness aggravated the very problem of deficits it attempted to solve.

In a sense, the half-hearted attempts to shift the country's trade strategy towards greater openness aggravated the very problem of deficits it attempted to solve.[26] The relaxation of some export barriers (e.g., quotas and tariffs), under the export-oriented strategy, was supposed to ease conditions under which export-industries obtained their materials and to enable them to price their products competitively abroad; the end in view of course was to expand exports and eventually narrow current account deficits. The presumption, however, was that all other price variables would also be competitively determined. However, combined with an overvalued currency, such a shift provided a sufficient stimulus to increase imports, and thus contributed to widening rather than narrowing the deficits. A related fact was that the new export industries established used a lot of imported inputs.

Finally, one must mention the various mandated privileges extended to both private and public entities in importing products duty-free. Domestically, the effect of these privileges was to yield some monopoly advantages to those who received them. The impact on the external sector, however, was to increase the country's propensity to import. To the extent that these entities were exempted from the usual tariffs and duties, their activity could only be minimally influenced by a change in the structure of protection in the economy.

The energy self-sufficiency program has always been cited as one of the administration's major successes and one of the reasons the country had to borrow abroad. To give credit where credit is due, the drastic reduction in the growth of oil imports must be acknowledged as one of the brightest spots in the government's record. Even this reduction in oil imports, however, could have been achieved at a much lower cost. The nuclear reactor, for example, cost more than $1.8 billion, not counting interest expense,[27] constituting nearly 8 percent of the country's external debt, but has yet to make a contribution to oil import-substitution.

The government exacerbated the effects of the external shocks on the magnitude of debt by running huge deficits and by allowing its financial institutions to guarantee foreign debts of private firms.

The government exacerbated the effects of the external shocks on the magnitude of debt by running huge deficits and by allowing its financial institutions to guarantee foreign debts of private firms. How much of the debt proceeds went to projects that were simply wasteful or to projects that have long gestation periods cannot be precisely esti-

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[26] A case of what economists call "the theory of second best."

[27] We thank Minister Geronimo Velasco for providing this information to correct the figures in the draft of this Report.

mated. One cannot escape the fact, however, that the interest costs are now being incurred, while the returns from the projects have yet to be realized. Net interest expense (i.e., interest expense less interest income) grew from $76 million or 8.2 percent of the current account deficit in 1975 to over $1.5 billion, or 46.2 percent of the current account deficit in 1982.

Since 1976 the national government has been running huge deficits in spite of growing surpluses in its current operations. An increasing amount of these capital outlays found their way not into the usual types of infrastructure but into corporate equity investments and capital expenditures of ministries other than public works and highways. These capital outlays were partly funded through foreign borrowings, hence it is not coincidental that foreign debt grew rapidly after 1975 (Tables 18 and 19). In 1975, total external debt was $3.8 billion; current account deficits for 1976-1979 and 1980-1983, on the other hand, were $4.6 and $10.4 billion, respectively.[28] In other words, the accumulation of debt accelerated with such rapidity that, since 1979, the debt accumulated during the four most recent years has exceeded all the debts accumulated during all previous periods.

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Table 18

SHARE OF NET BORROWINGS OF NATIONAL GOVERNMENT IN TOTAL NET BORROWING FROM ABROAD, 1976 TO 1982

	(1) Net Borrowing from Abroad (Billion Pesos)	(2) National Government's Surplus on Current Operations (Billion Pesos)	(3) Net Borrowing of National Government (Billion Pesos)	(4) (1)-(3)	(5) (3)/(1)
1976	7.8	2.5	2.7	5.1	34.6%
1977	4.8	3.3	3.1	1.7	64.6
1978	8.4	6.6	5.3	3.1	63.1
1979	9.8	10.1	3.9	5.9	39.8
1980	13.6	11.4	5.3	8.3	39.0
1981	14.7	11.1	10.9	3.8	74.1
1982	20.9	12.6	10.1	10.8	48.3
TOTAL	80.0	57.6	41.3	39.7	51.6

Source: *NEDA Statistical Yearbook*, 1983.

[28] The sum of the 1975 debt and the total current account deficits from 1975 to 1983 is $18.8 billion, a figure close to official estimates of total external debt prior to the upward revision of the official figure by $6-7 billion. The upwardly revised figure is then termed "total foreign exchange liabilities." The revision was probably made to account for Filipino-owned assets abroad, capital flight or errors in the estimation of the current account and the international reserves.

What can be clearly seen from official data is that the government borrowed abroad not simply to finance oil imports but also to finance government projects and private investments which were, in turn, encouraged by government guarantees. This practice probably made sense until 1978 when world inflation rates were high and interest rates were low due to the recycling of surplus liquidity from the OPEC. With inflation factored in, real interest rates were low and even negative until 1978. At such favorable terms, the crucial question was simply whether the funds would be invested prudently or not.

The second oil shock in 1979 drastically altered such conditions. Loanable funds from the oil-exporting countries did not increase since the developed countries were experiencing major recessions due to tight-money policies of their central banks. Hence, at that point, oil prices and real interest rates were rising, while export prices were sagging. The conditions for continued external financing had clearly become worse.

Faced with this situation, however, the country's policymakers chose to go on business as usual (or perhaps even more than usual). Total capital outlays of the national government exceeded ₱50 billion

Table 19

TOTAL EXTERNAL DEBT, 1975 TO 1982

(Million dollars)

	Level	Change from Previous Year	Current Account Deficit	Public External Debt
1975	3,798.7	—	—	1,978.6
1976	5,517.2	1,718.5	1,062	3,132.1
1977	6,562.7	1,045.5	752	3,132.4
1978	8,195.3	1,632.6	1,173	4,167.7
1979	9,778.3	1,583.0	1,576	5,311.3
1980	12,700.5	2,922.2	2,051	6,769.4
1981	14,826.5	2,126.0	2,293	8,582.0
1982	17,475.5	2,648.5	3,347	—
1983[a]	18,864.0[b]	1,389.0	2,707	—
TOTAL	—	15,065.3[b]	14,961[b]	—

[a]1983 figure from unpublished CB data.

[b]Note that the sum of current account deficits from 1976 to 1983 is quite close to the increase in reported debt from 1975 to 1983, prior to the upward revision of the 1983 official debt figure by $6.8 billion.

Source: Central Bank of the Philippines (1975-1981 as reported in the *NEDA Statistical Yearbook*), 1983.

from 1980 to 1982. On purely economic criteria alone, it is difficult to understand why the authorities continued to pile up debts even after real interest rates started to rise. Perhaps it was assumed that loans would keep flowing in or that export prices would soon recover. Unfortunately, the world economic recovery came late and rather weakly, as was predicted by many independent economists in the developed countries. Moreover the influx of foreign loans dwindled.

While the Aquino assassination certainly explains why the loans stopped abruptly, it is quite likely that the loans would have slowed down to a trickle anyway, for few private lenders would have continued extending loans to debtors that had difficulty paying interest on previous loans. Whatever the reason for piling up debts after 1978, it now seems that the short-run consequences on the economy after 1983 were staggering. To assess the long-run effects, however, one must know how the funds were used.

Slightly more than half of the external debt is accounted for by deficits of the national government (Table 18). A large amount went to highways, ports, bridges, and schoolbuildings. An even larger part, however, went to corporate equity investment and other capital outlays. In the period 1980 to 1982, ₱32.2 billion out of ₱51 billion, or 63 percent of total capital outlays, went to these two classifications. As the section on monetary and fiscal policies argues, however, many projects carried out under these two headings could scarcely be called productive. One need only cite the magnitude of equity contributions to the government financial institutions, on the one hand, and the large number of failed corporations in their portfolio, on the other, to realize how poor the prospects are that the country's foreign obligations may eventually be met by the expected "future output" of these projects. If and when these "projects" into which foreign funds have been sunk eventually prove unproductive (i.e., no output would be forthcoming), there will have to be cuts in the people's future consumption (e.g., in the form of lower real incomes, higher taxes greater exports, etc.) to pay off foreign obligations (should it be decided to pay them). Such is the real burden of the debt.

Thirty percent of long-term and medium-term external debts went directly to the private sector. However, more than 45 percent of the debts could be classified as private debt if funds from the public sector which eventually went to private firms through government financial institutions were treated as private expenditures. A substantial part of the foreign debt was either guaranteed by or channelled through government financial institutions. Unfortunately, but perhaps not coincidentally, many of the firms that received the loans or the guarantees (e.g., CDCP, MMIC, the hotels, etc.) are doing badly. Some of these bad investments may well have been honest mistakes. However, it would certainly be easier to commit mistakes if one did not have to suffer the consequences of one's actions. The government's practice of guaranteeing private debt, and converting defaulting loans to equity tended to reduce the losses

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Slightly more than half of the external debt is accounted for by deficits of the national government.

What might have been limited failures and corporate tragedies confined to private persons become transformed into a national economic crisis. . .

to these private agents. What might have been limited failures and corporate tragedies confined to private persons become transformed into a national economic crisis, and the burden of paying the debts of the few was passed on to the entire nation.

By 1982 the effects of these monetary policies were already beginning to weigh heavily on the economy. Net interest payments to the rest of the world more than trebled between 1979 and 1982 (Table 20), and the country was surviving only by virtue of its availment of very short-term loans at high interest rates. Growth and employment-generation were faltering and inflation hardly abating. The stoppage of foreign financing in 1983 merely exposed the already-existing weaknesses in the fabric of the economy. The country's immediate and long-term prospects have, in short, been clouded by past excesses and mistakes.

Of course, we will survive, but not as well as if we did not have the debt, or if we had invested the loan funds frugally and efficienctly.

It has often been asserted bravely that there is, after all, no question that the country and its people will survive the present crisis, that no country can ever really be bankrupt. The skills and creativity of the workers plus our natural resources would serve as the "assets" on which we can always fall back, and which no bank can take away. Hence, it is argued, the country is in a sense only "illiquid" but not "insolvent"; future output is always forthcoming. In this sense, then, any crisis is temporary, and all things must pass. Of course we will survive, but not as well as if we did not have the debt, or if we had invested the loan funds frugally and efficiently. We have permanently lost the potential returns to wasted resources and have therefore to begin from a lower base.

Table 20

INTEREST EXPENSE AND INCOME REPORTED IN THE BALANCE OF PAYMENTS, 1975 TO 1982

(Million dollars except percent)

	Interest Expense					
	Foreign Currency Deposits	Foreign Loans	Total	Interest Income	Net Interest Expense	Net Interest Expense as % of Current Account Deficit
1975	11	223	234	158	76	8.2
1976	13	246	259	125	134	12.6
1977	17	224	236	138	98	13.0
1978	43	397	440	179	261	22.3
1979	90	536	626	200	426	27.0
1980	197	778	975	336	639	31.2
1981	218	1,156	1,374	519	855	37.3
1982	261	1,650	1,911	365	1,546	46.2

Source: Central Bank of the Philippines.

Furthermore, while resources may be an important factor in growth and development, they are not decisive in themselves. Perhaps even more important are the relationships which men establish between themselves, and the rules and institutions which they set up to govern the use of and claims over such skills and resources as are at hand. What may restrain a country's progress is not the amount and quality of the resources it possesses, but the fact that its institutions do not foster further development, and that the system of economic allocation and decision-making it follows is prone to waste and inefficiencies. In such cases, merely citing the "innate genius" or "native resourcefulness" of the people as the basis for future improvement in their station sounds hollow. For it is the institutions, rules and leadership which are in need of change. The final question then is: how are economic decisions and policies made, and who makes them?

What may restrain a country's progress is not the amount and quality of the resources it possesses, but the fact that its institutions do not foster further development...

3.3 Institutional Framework

Of the many political themes that have been advanced to explain the economic crisis of 1983, the greatest emphasis has been given to the weak or nonexistent system of checks and balances on a wide range of actions and decisions by the incumbent political power, and the limited liability enjoyed by bureaucrats when policies that they enunciate fail.

The declaration of martial law in 1972 set into motion a political process—unprecedented in Philippine history—leading to a system of government where the president could exercise legislative power indefinitely. Initially, this was achieved by invoking the extraordinary powers of the executive under conditions of martial law. But subsequently such powers were made a permanent feature of the system through a constitutional amendment (i.e., Amendment 6). This was in clear contrast to previous arrangements where power had been separated between the branches of government to maintain a system of checks and balances. In addition, the restrictions on press freedom and information, the climate of fear engendered by the prominent role given the military, and the imprisonment of many opposition leaders effectively weakened the processes of democratic politics.

Under the new system, the president hired managers or bureaucrats in running the affairs of government. Most major economic decisions were formulated and approved by a rather small circle of people—consisting of so-called technocrats as well as political and business allies—gathered around a powerful chief executive.

Most major economic decisions were formulated and approved by a rather small circle of people...

The plausible intellectual justification for such an arrangement in a political regime officially described as "constitutional authoritarianism" was that it eliminated much of the costs of decision-making and transactions associated with checks and balances. The latter system was held to be cumbersome, time-consuming, and prone to manipulation by special-interest minorities and hence "inefficient." Some allusion was also inevitably made to authoritarian governments of the so-called "new industrializing countries," or NICs, and a connection drawn between decisiveness of policy in those countries and their corresponding economic success. Often the case would be put even more strongly by saying that a developing country could not "afford" democracy, that a tradeoff existed between political rights and "democratic trappings" on the one hand, and growth and economic security, on the other.

There are many virtues claimed for authoritarianism, among which are that, compared to normal democratic procedures, authoritarian decision-making is more timely and flexible. The proposition in economics known as Arrow's "impossibility theorem" would also imply that authoritarianism can be "consistent"[29] whereas a democratic voting rule may not. In other words, authoritarianism, it could be argued, avoids many of the "costs" incurred by a normal democracy. The cost of not being timely or flexible may be measured in terms of foregone opportunities; the cost of being inconsistent lies in having to undo commitments of resources. Despite such arguments, however, there is a widespread perception that authoritarian decision rules have failed in practice, and the virtues of democratic decision-making would now seem evident.

. . . there is a widespread perception that authoritarian decision rules have failed in practice, and the virtues of democratic decision-making would now seem evident.

We would now attempt to delineate some abstract features of authoritarianism and its effects on resource-allocation by proceeding from some reasonable hypotheses regarding social behavior. The truth and usefulness of such hypotheses must ultimately be judged by the reader on the basis of whether they generate predictions which correspond to readily observable phenomena.

Unless one ascribes noble and unselfish motives to everyone, it must be supposed that public officials have objectives of their own, and possess the ability to act on them. In a democratic setting, the people's welfare, however defined, would tend to restrict their actions. For if these officials purport to be agents of the people, then they are constrained not to let their constituents' welfare fall below some acceptable minimum level. Otherwise, they may find themselves voted out of office.[30] In the absence of an operational democratic process, however, the level of the people's welfare would not be an effective consideration.

The "price" that must be paid for a wrong decision is reduced. Rather than asking whether an act is likely to cause political displacement, say an electoral defeat, one needs to ask only if it is likely to reach the threshold of active insurgency. In effect authoritarianism alters the composition of the officials' constituency, shifting the locus of their accountability from a more broadly based electorate to the smaller group

In effect authoritarianism alters the composition of the officials' constituency, shifting the locus of their accountability from a more broadly based electorate to the smaller group to whom they owe their tenure . . .

[29] I.e., transitive in the sense that, if society prefers alternative A to B and B to C, it prefers A to C.

[30] The potency of the electoral process would be even greater in theory under a parliamentary system, since elections may be called at any time regarding issues of confidence.

to whom they owe their tenure, whether it be the president, his prominent business allies, the military, and the foreign governments and banks. It is rather the imperatives of this new constituency, not that of the majority, which would constrain the directions of economic policymaking.

The absence of accountability to the majority in such a system of government would introduce severe distortions in resource allocation, for incentives to economize and look for the cost-efficient project would not exist. The official who ordered the project would risk neither his money nor his job. Such a problem is, of course, always present in some degree in any relationship between a principal (or owner) and an agent (or manager). It becomes qualitatively more pronounced, however, when the odds of the agent being penalized for misjudgement and wrongdoing have been virtually eliminated as a result of the monopoly of power. Monopoly in politics, as in economics, generally leads to waste and inefficiency as well. Since the taxpayer's welfare is not effectively considered in the officials' actions, it would not be surprising to observe abnormal cost-overruns and substandard work for projects. In the Philippine setting, this might be illustrated by cost-overruns for the nuclear plant, the light-rail transit system, and most highways. In the particular case of the size of the external debt, the elimination of the need for legislative scrutiny and approval—which might presumably have reflected taxpayers' concern more closely—would seem, from hindsight, to have facilitated the availment of foreign loans beyond what might be considered reasonable levels. The growth of bureaucracies might also be explained by an incentive structure that encourages the increase in the size of staff and corresponding amenities (e.g., office space, expense accounts). Savings typically cannot be appropriated but have to revert to some general fund. However, such funds may be effectively appropriated by increasing the size of staff, justifying the expenditures on amenities and perquisites by bureaucrats. For example, a large staff might imply a larger building, which in turn might justify a thicker carpet, a larger desk, an expense account, or an antique collection.

However, the most damaging economic consequence of political monopoly is the potential abuse of the state machinery and its functions to dispense economic privileges and position to certain private entities. To the extent these private interests are an identifiable social group which is substantially able to influence the direction of government policies, they have an abiding interest in seeking the continuation of political monopoly and the expansion of the state's economic role. For government intervention in behalf of private interests would give the latter awesome advantages vis-a-vis their competitors. Hence it might be a mistake to view the expansion of the government's role in recent years as an instance of "creeping socialism," or to regard the essence of the economic debate as being about the virtues of public intervention versus private enterprise. On the contrary, it could well be a conflict

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between different groups in the society, being distinguished only in that one group has obtained exclusive access to the government.

Given such premises, therefore, it would be natural to observe that the government's role in the economic sphere has expanded and, second, that this wider economic role would be attended by government's inefficiency, and waste. For after all, the interest in the activity would attach not to the enrichment of the government but the gain of the private individual; not to the efficient attainment of the results, but to the expansion of purchases and activity; not to the provision of public goods, but to the transformation of public resources into privately appropriable surplus. Then what might appear from the public viewpoint as government waste and inefficiency might in reality be gain and profit for private interests.

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Concentration of political power could also affect resource allocation through the role of information and uncertainty. The efficiency in decision-making which authoritarianism affords (e.g., consistency, timeliness, flexibility) may be presumed only if the data informing decisions are always the best available. Then, at least, the rulers could act consistently and in a timely fashion according to their interests, although these may differ from those of the majority. However, a major shortcoming of authoritarianism, especially insofar as it rests on a weak social consensus,[31] is that it is not conducive to objectivity and the free flow of information, thus rendering it prone to mistakes. The process of forming coalitions based on trustworthiness and loyalty to some strong political personality hardly encourages the assembly of the most complete and correct information set.

If popular support for the regime is, at best, precarious, it could be induced externally to emphasize "unity," "loyalty," etc. But internally it may suspect differing opinions as being potential threats to its existence. The fuller disclosure of preferences and information which is a by-product of regular democratic decision-making processes would be harder and costlier to achieve under unpopular authoritarian regimes. For instance, if access to mass media is restricted for fear that unfavorable reports might fuel popular resistance, an independent system of gathering information, not for public consumption, would have to be set up, e.g., research agencies, military intelligence, secret polls, etc. Such methods are often more costly and at times unreliable. As another example, the information-processing capability of schools and universities, is often underutilized under authoritarianism either because the information made available is poor in quality, or because it is not available at all. Again this fear that information will be used as a basis of criticism is traceable to the narrow social basis of many authoritarian regimes.

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[31] Hereafter we use "unpopular" to refer to that type of authoritarianism which rests on a "weak social consensus" or a narrow base of social support.

In the local context, the most formidable obstacle to an independent researcher in objectively assessing social conditions is the revisions, reworking or withholding of important public statistics, often with a generally cosmetic effect. The problem is undoubtedly due in part to inefficiency or backwardness in statistical work. But one might ask how significant a portion may be due to "disinformation" or "management by illusion." In Appendix 2, we discuss how some common data on employment, wages, inflation, external debt, and international reserves must be carefully interpreted if one is not to be misled into gaining an unwarranted favorable impression.

It is typical of information that if it can be made available to someone, it can be made available to everyone else at little extra cost. It is precisely this "externality" of information which is suppressed under unpopular authoritarianism. Hence it is ironic that, while the alleged superior virtues of authoritarianism require it to generate correct information for each decision, its narrow social basis could erode such claims of superiority since the information would be costlier and harder to generate. The quality of decisions, of course, suffers as a result.

Under an authoritarian system, therefore, the majority may be penalized by actions of the ruling group, first, if their interests are divergent and, second, because of mistakes which the rulers might not subjectively wish to make, but are disposed to make nonetheless. The dilemma of an unpopular authoritarianism lies in that, while it may be politically expedient to eliminate dissenting opinion to ensure its dominance, it may eventually require such opinions to assess the real situation. In local experience, the unfortunate decision to continue financing huge deficits in the midst of world recession and rising real interest rates might not have been taken (or might at least have been scaled down) if there had been sufficient public debate on the issue. The same might be said of other decisions such as the successive reversals of policy regarding the coconut levy, the decisions establishing the sugar commission, giving dole-outs to failing companies, and incentives to hotel construction.

In short, the easy and flexible manner of changing policies which is claimed as authoritarianism's chief virtue is potentially also its weakness. It would be optimal to change policies often if one could always find the correct response to changing conditions. However, when information is wanting or is costly (due perhaps to authoritarianism itself), correctness cannot be guaranteed. Hence the ease and flexibility of decision-making under authoritarianism could just as likely facilitate the commission of mistakes. Often enough, what might be called "flip-flopping" decisions could result, as the authority seeks to amend or reverse earlier mistaken decisions when better and politically irresistable information becomes available. The possibility and actual occurrence of such drastic policy-reversals introduce an inordinate degree of uncertainty and risk for

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those who have to live under the system. Adding to uncertainty is the finiteness of the central personality's working (not to mention absolute) lifetime, although this may be mitigated by rules of succession (e.g., dynasty, as in a monarchy) that are broadly accepted. By contrast, normal democratic procedures are admittedly slower and more circuitous, but by being so, they tend to elicit more information before a decision is taken (e.g., through discussion and debate), and discourage drastic policy-changes (e.g., through compromise, horse-trading, logrolling, etc.).

The economic effects of such risk and uncertainty upon the private sector are likely to be: shortened economic planning horizons, a higher premium on quick returns, and fewer longer-term investments. Local and foreign businesses which have obtained special privileges under the system could resort to predatory behavior, since it is precisely these privileges which would be in danger of being withdrawn with a change in regime. In the Philippines, this might explain the failure of many favored corporations, whose principals nevertheless enriched themselves. An added disincentive effect of uncertainty might also be felt by those unprivileged firms which may, in fact, be efficient but which are wary of expanding lest they be "raided" or taken over by some privileged conglomerate. For favored firms, the business slogan might be, "Make hay while the sun shines," while for the unprivileged it might read, "Half a bird in the hand is better than no bird at all." The extreme consequences of uncertainty were experienced last year in the form of disinvestment and capital flight.

From another viewpoint, the contrast between authoritarianism and democracy would appear to be one regarding the form but not the substance of social rule. It would seem obvious that what matters most for development is the social interests to be promoted and the indicated economic agenda. In contrast, the political forms through which such agenda are to be pursued must seem of secondary importance. Indeed abstractly, some of the faults associated with authoritarianism might be mitigated by postulating its basis on a broader constituency, or a stronger social consensus. Then, by hypothesis, the issue of conflicting interests between the ruler and the ruled would be removed or at least reduced. Even the information defects might be removed, insofar as the greater coincidence of interests between the authority and the rest of society obviates the need to withhold information from each other. This could be one way of explaining the phenomenon of the newly-industrializing countries, where certain types of elites, working through an authoritarian system but with some apparent measure of social support, were able to accelerate economic growth, with strong links to the world economy. This discussion should suggest that there is no necessary connection between authoritarianism and economic success, without reference to the agenda the leadership would push through.

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Some students of Philippine history and politics have offered explanations for the emergence of authoritarian rule which seem to accord well with the behavior of economic variables described earlier. According to at least one such hypothesis, the shift to more authoritarian forms may be traced to the agenda of a certain social faction to use the state machinery in building up its economic power within a relatively short period, and to break away from a traditional "oligarchy" which, through its economic influence typically dominated political outcomes under a democratic regime. To overcome the resistance of this "oligarchy," the social faction in question would have to first of all neutralize and eventually dismantle the social and political organs through which the "oligarchy" traditionally exerted its influence (e.g., the legislature and the mass media); secondly, unable to count on the support of the "oligarchy," it would have to build its own bases of support. Initially lacking substantial economic power but being in control of the government, the social faction in question could build up its own loyal constituency through dispensing privileges to some new, hitherto minor, private interests using the government's functions. These, in turn, could develop into a "new oligarchy" supporting such a regime. (Before its own oligarchical base is consolidated, this social faction might cultivate the military as a political support to obviate active challenges from the traditional oligarchs.) Especially where direct foreign intervention is a possibility, it could also seek to cultivate foreign support by attracting foreign investment and, loans, insofar as these increase the stake of foreigners in the domestic economy.

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It is not difficult to see how such political changes might be reflected in an increase in the government's economic role and in heavier industrial concentration. The use of government resources and activities to build a loyal constituency would enlarge government expenditures and fiscal deficits, with a resulting rise in public indebtedness; pressures to raise monetary growth through selective credit allocation would increase, and privileges given to supporters might easily be developed into monopolies. Such trends could not but have an adverse economic impact in spawning an economic crisis.

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One contribution to analysis made by this excursus is that it may not always be sufficient to evaluate economic policies solely by using the criteria of efficiency or equity, which economists often find important. For otherwise, the impression might be gotten that such policies were always addressed to such objectives when in truth one must allow that they were possibly responses to quite different, perhaps political, imperatives. Consequently, the researcher's assessment of the ease or difficulty of changing economically "wrong" policies would greatly differ, depending on whether he perceived such policies as technical miscalculations or as goal-oriented behavior.

In our emphasis on the importance of economic agenda, the reader may have gained the impression that the question of political regime is one that we choose to leave unsettled, and that we could just as well advocate authoritarianism provided it is "popular" or has the "right" agenda. Such an impression would be wrong. In the real world, the choice of political rules occurs only under conditions of great uncertainty and, once made, is often difficult to reverse. Here, true agenda and preferences would not necessarily be revealed, since there would be no guarantee against misrepresentation. Opting for authoritarianism solely on the basis of the announced agenda would be hazardous, since once endowed with political power, a dictator could be removed only with difficulty and could well choose to implement a "hidden agenda."

Groups in society may press for the adoption of certain political rules not because of any inherent desirability in those rules themselves but because they stand to benefit from such rules. Of course each group in society might conceivably be better off if it found an authoritarian regime which served its interests exclusively. Where uncertainty prevails, however, the crucial question is the probability that such a search will be fruitful. Choosing the "right dictator" must be fortuitous, at best. A regular democratic regime is superior to an authoritarian one, regardless of the social group to which one belongs, in the sense that it minimizes the risk of any group making an irreversibly wrong political decision, with harmful effects on everyone else, but especially the poorer classes. When, as in real life, conditions on extreme risk and uncertainty prevail, it may actually be futile and excessive for society to strive for "best;" it might do well to make do with what is "good enough."

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4 AN ALTERNATIVE AGENDA FOR RECOVERY

The foregoing analyses already contain implicitly what is required, in our opinion, to halt the downward drift in the economy and lay the foundations for future improvement. In this chapter those proposals are made explicit and compared with those put forth by other sectors in society. These proposals may be classified into those that deal with structural problems, i.e., those that are more strategic and pertain to the country's long-term development prospects, and secondly, adjustment problems, i.e., those that relate to the immediate causes and consequences of the present crisis. In formulating these proposals, we were motivated, first, by a concern for economic realities and second, by a judgment that the measures to be implemented should be least burdensome to the poorest.

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4.1 *There must be a change in the system of government towards less centralized political and economic decision-making and greater public accountability. To allow a more meaningful participation by the public in national affairs, their access to relevant and good-quality information should be improved, and their organization in behalf of their interests should be encouraged.*

After carefully considering the crisis in its various aspects, we conclude that the most crucial element in any plan for long-term recovery of the economy would be a change in the system of government. In particular the country must move in the direction of more liberal-democratic politics and greater public participation in decision-making. For it has primarily been the authoritarian system, without effective checks and balances and accountability, which facilitated the economic excesses and mistakes of the past. The waste and inefficiency entailed by economic concentration in both the private and public sectors have been abetted by the concentration of political power.

Small groups have been able to use the government's legitimate functions as a vehicle for their private interests. The frequent identification of the government's activities with such private interests has led to the unprecedented expansion of the state's role in an economy supposedly founded on free enterprise, with disastrous consequences upon resource allocation. Moreover, the technocrats were neither able to guide the economy to greater socioeconomic development, as initially expected, nor were they able to moderate the excesses of the dominant interests.

However, it is not sufficient merely to establish a liberal-democratic regime to promote a fuller socioeconomic development. What would be necessary is to replace the present economic agenda with one that engenders greater economic competition, encourages entrepreneurship, and promotes greater equity. It is even conceivable that a civilian or military dictatorship, or perhaps even the present leadership, could announce its willingness to pursue such a new agenda. However, the alternative of a "reformed" or "enlightened" authoritarianism, which was incidentally how the current regime portrayed itself, must be rejected. Apart from the drawbacks of authoritarianism deriving from its heavy information requirements and breeding of uncertainty, there really exists no guarantee that, once it had secured preeminent political power, an authoritarian regime would not proceed to implement a totally different agenda. Finally, regardless of the real or imagined economic benefits such an authoritarianism may promise, it is valid to ask whether its cost in terms of human life, human dignity and intellectual development is not too high to pay.

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We do not perceive that there is a need to trade off human rights for economic well-being. The present historical juncture is unique in that a shift to democratic procedures and institutions would yield improvements in both efficiency and equity, if only because it would allow the articulation of interests by a larger number of groups in society. In this fashion, most of the major excesses of the past, which culminated in the present crisis, would be checked and curtailed. Concerned citizens could organize and lobby for limits to the size of government deficits and the public debt. A too-rapid expansion of the money supply, inflation which precipitates devaluation, and the deterioration in real wages would have to contend with protests by workers who are free to organize in their own interests. The excesses of both domestic and foreign monopolies could be exposed by the clients they purported to serve, while edged-out business competitors would object to the extraordinary privileges granted a few and exercise their own countervailing power. Miscalculations in economic policy and decisions could be reduced with fuller public discussion of the issues, or, if ever they occurred, would be accompanied by public censure or dismissal of the officials involved. An unmuzzled press, an independent academe and an effective political opposition could keep the public informed of the true economic choices open to them and the political actions required to have these implemented. Finally, a free and honest electoral process, combined with an informed and organized electorate, would provide a workable system of accountability between bureaucrats, on the one hand, and the people on the other, eliminating much of the present leeway for using public resources for private benefit.

The political and legal reforms required to achieve such a working democracy are only too well-known and have already been detailed by others. We might simply mention the need for greater electoral safeguards, the need to reduce the president's decree-making powers, the repeal of decrees which are construed as threats to free speech, free press, and the growth of an effective opposition (e.g., Preventive Detention Action [PDA]), the lifting of various restraints on union activity, etc. For researchers and educators, however, there is a great need for wider public access to information and data which are relevant, timely, and of good quality. For reasons already discussed, such a need has not been urgently felt before, and this has had some undesirable economic consequences.

The success of democracy rests, to a large extent, on information availability. The quality of the people's participation in decision-making and their perception of their interests is greatly affected by the amount and quality of information they possess. Asymmetries in the distribution of information and of information-processing capacities will be reflected in inequalities in the ability to bargain, lobby, and respond to events. Such asymmetries are especially pronounced under authoritarianism where, in theory, the people's participation is not even required. However, even in a liberal democracy, those social groups for whom information costs are high (e.g., due to inability to obtain an education) could still be effectively disenfranchised. In a sense, the academe, the media, and parliament have the task of transmitting information to the public in generally accessible form which can be the basis of electoral decisions. However, a prerequisite for this is that the government's various agencies fully disclose the required information. Appendix 2 contains a critique and some suggestions regarding presently available official statistics and their mode of disclosure.

Nevertheless one should not be so naive as to think that, by simply postulating the existence of such processes or institutions, e.g., elections, a free press, etc., the desired economic consequences would automatically follow. For example, in order for accountability to be effective, all officials, including the highest must be made to feel that their positions are genuinely at risk from such elections. Otherwise, if elections affect only minor positions, if there is no guarantee that through elections the authoritarian power may be drastically curtailed, if there is a possibility that illegitimate intervention may nullify the results of elections, then there would hardly be a reason for officials to change their behavior or shift their allegiance to the electorate. Under such circumstances, elections would only serve a cosmetic purpose. An official could merely seek to manipulate the people's choices through fear, withholding of information, and the cultivation of a general feeling that opposition would be futile and uncertain. The electorate, if it did not perceive any imminent superior alternative, would likely as not strive to avert risks and sell its votes, in the meantime compromising its objective interests. Under such conditions, the people's interest will have been compromised even if the elections had been free and honest, simply because the people will not have been aware of the objective possibilities.

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On the other hand, the experience of the National Citizens' Movement for Free Elections (NAMFREL) in the recent elections for the national assembly illustrates what might be achieved through education and organization of the people. The majority of voters were eventually convinced that a real choice was possible and that their votes stood a reasonable chance of being counted. Hence they participated and returned a larger-than-anticipated vote for the opposition, although whether their hopes were justified still remains to be seen.

It may seem ironical that, in order for democratic processes and institutions to be effective and meaningful against a ruling group, the majority must in a sense already be in "power." By this we mean that the people in the majority must already possess all relevant information regarding available alternatives for them to make their choices effectively and consciously as well as the bargaining power to establish such democratic procedures and institutions as may promote their interests. In this sense, free elections and other institutions associated with liberal democracy are not the ends but simply the means towards a working democracy. The development of democratic politics involves a long process that must begin by building up the people's bargaining power in society through organization and self-education. In this sense, the activities of NAMFREL, the boycott movement, the trade unions and other cause-oriented groups are to be commended and encouraged as well as the greater outspokenness of media and the schools. For insofar as these lead to the growing self-awareness and bargaining power among people, they serve as foundations for a more meaningful democratic system in the future.

4.2 *Government priorities must be reordered; expenditures should be reduced substantially instead of raising new taxes or failing to adjust compensation.*

The government's huge and persistent budget deficits were a main cause of the present economic crisis. If the country's dependence on foreign borrowing is to be eventually terminated, such deficits must be drastically reduced. In the context of the International Monetary Fund's (IMF) stabilization programme, the government is constrained to reduce its budget deficits as a proportion of GNP (for other details, see 4.6 below). However, the government's response to the constraints on its deficits has been to raise new taxes and to scrimp on the adjustment of compensation to its employees. Among the moves to raise new revenues, the most important ones have been the 10 percent ad valorem tax on all imports, the 30 percent "stabilization tax" on differential export earnings, the 10 percent tax on all foreign exchange transactions, and the increase in the specific taxes on petroleum products. While there have been some cuts on government expenditures, they still remain at historically high levels and have not always been directed towards the most urgent social priorities. The government is, in effect, asking the public to reduce their consumption while it maintains a high level of expenditure.

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Increases in specific taxes, such as the ad valorem taxes on imports, penalize the poor more than the rich, where both consume the same goods since both have to pay the same tax and higher price per unit, despite the greater value of money to the former. The larger number of the poor who are not exempt from indirect taxes implies that it is mostly from them that such revenues are being collected. By contrast, if revenues are derived mainly from income and wealth taxes, it would be mostly the more affluent who would pay. If the government adjusts to the present crisis mainly by increasing indirect taxes, as it seems to be doing, it will in effect be shifting the burden to the less-privileged members of society.

We propose, on the other hand, that as a broad rule, the government reduce the share of its expenditures in GNP from the present 18 percent to premartial law levels of 10 percent or so. This must be accompanied by a reordering of its priorities so that a greater share of the total budget will be channelled to those ministries and agencies whose contributions to social services and income redistribution are more apparent, such as those in charge of health, education, labor and welfare, and technical extension. While this may not be immediately achievable due to employment implications, there are certain areas where considerable headway could be made. The objectives may be accomplished, among other ways, by (a) reducing equity contributions to government corporations, and in general minimizing government participation in the economy, (b) cutting down on all non-infrastructure construction, (c) eliminating allocations to "special funds" (e.g., KKK), and (d) eliminating or reducing allocations to ministries and agencies with dubious contributions to social productivity (e.g., allocations to some offices in human settlements or defense ministries). After all this fat has been trimmed away, it may even be possible to adjust government salaries to a level which at least compensates for inflation. The reduction in government expenditures would not necessarily imply a reduction in total employment in the long run. Although there might be initial displacement, the resources released would eventually be absorbed by the private sector, which can be expected to employ them more efficiently.

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Aside from the oft-repeated pleas for more efficient tax administration, revenues for socially urgent programs may be raised in less painful ways for the majority by, among others, (a) disposing of the assets of failed corporations taken over by the government and by this token also eliminating the drain represented by government subsidies and honoraria of government officials who sit on several boards; (b) sale or lease of excess office space in government buildings (which may be accomplished when sizes of staff are reduced in low-priority ministries); and (c) elimination of multiple sources of income of high government officials (e.g., fees from government corporate boards).

In any event, the general thrust of this proposal is clear. We agree that budget deficits need to be reduced. However, we are against any attempt to do so which shifts the greater burden of adjustment to the people without first eliminating large-scale waste and inefficiency in the government.

4.3 *Halt the trend of increasing economic concentration; dismantle the monopolies and reduce the government's role in the eco-*

nomy. Eliminate the discrimination against agriculture and support reforms promoting efficiency in industry.

The presence of numerous monopolies in the economy represents an enormous drag on productive capacity.

The presence of numerous monopolies in the economy represents an enormous drag on productive capacity. In the absence of economic competition, many of these entities are allowed to earn higher than average profits or to fritter away this potential surplus in the form of waste and inefficiency. Where they dominate production, they are able to charge higher prices to clients or get away with inefficient service (e.g., the utilities); where they are exclusive purchasers (i.e., monopsonies) as in the sugar and coconut industries, they may penalize direct producers by paying them a lower price than under a competitive system. The government has mandated the existence of many private monopolies, and is itself a monopolist in some sectors of the economy (e.g., through the NFA). Especially disturbing has been the concentration taking place in the banking industry and its close relationship to concentration of ownership elsewhere in the economy; the combination of finance and industrial interests has concentrated the most important decisions on the allocation of society's resources into a few private hands, both local and foreign. Parallel to this has been the growth of the government's own economic role. Apart from its implications on economic efficiency, such a trend has had a severe negative impact on income distribution. Over a longer period the costs of such a system could come in the form of discouraging innovation and entrepreneurship, and increasing amounts of resources being diverted towards obtaining and protecting such mandated privileges.

This report's general position is that, except where there are valid economic reasons for maintaining them (and these must be publicly demonstrable), monopolies are economically harmful, and the trend towards greater economic concentration should be discouraged. Existing monopolistic and other privileges, especially those which exist only by virtue of presidential decrees or letters of instructions, should as a rule be abolished and reestablished, if at all, only after lengthy public discussion and study. These include the more important monopolies in agriculture, such as sugar, coconut, and the NFA's various trading prerogatives. Government financial institutions should cease acting as mere conduits for Central Bank credit and other government funds and should generate their own sources of funds (e.g., by attracting deposits). This change will force them to become more efficient in their lending, since they would be held liable by their sources of funds for any bad credit decisions; competition in the whole financial market would thereby also be stimulated. Along the same vein, the privileges given to various political banks by the Central Bank and the government should be stopped. Of course, if rules on size and concentration are to be applied to local monopolies, they must be applied to foreign monopolies as well. The point being made is direct: the market should be allowed to work and select economic survivors without preemption by the state.

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Agriculture deserves special mention because the more important monopolies are to be found in that sector and also because, due to the crisis, there is a belated appreciation for agriculture's potential contribution to the economy. Even in the past, many policies intervening with prices have tended to be biased against agriculture, as manifested, e.g., in the overvalued currency, the tariff structure, various export taxes and quotas, and price controls. Government-mandated monopolies in agriculture are the newest and more obvious form of intervention in a sector that has known all too many. While such intervention has often been justified by unexceptionable social objectives, e.g., providing cheap food, stabilizing export incomes, promoting greater processing, etc., its effect has been mainly to discourage agricultural production by lowering the prices received by direct producers. Estimates suggest that, because of such distortions, the agricultural sector has actually been providing large net subsidies to the rest of the economy (David 1983) over the past decade. Apart from the implications on efficiency, the inequity of that situation is obvious if one considers that the agricultural sector embraces the largest number of the poor. In many instances, e.g., sugar and coconut, as discussed in this report, the original objectives of the intervention (e.g., greater bargaining power abroad) do not seem to have been achieved in any case. Moreover, in general, it would be more efficient and equitable to seek to achieve those objectives through a system of taxes and subsidies on production, consumption, income and assets, rather than by granting exclusive trading rights to a single entity.

We support efforts to undo such disincentives to agriculture. At the same time, we view with some puzzlement the discrepancy between the government's newfound concern for agriculture and its new tax measures on foreign exchange and on export earnings. Because agriculture still accounts for the bulk of net exports (the large gross share of nontraditionals being offset by their high import requirements), such measures are bound to affect the earnings of direct producers in agriculture and reduce whatever incentives to production the devaluation might have. It is not likely that the monopolies would allow such taxes to eat into their trading profits, hence they would pass them on to the producers.

We find it strange that both the government and the private sector should be enthusiastic about agriculture yet remain silent regarding what must be done about the structure of ownership in that sector. If incentives are to be given to agriculture, it must be asked who is most likely to benefit from them. Unless the monopolies in agriculture are dismantled and a farther-reaching land reform than the present one is implemented, it is likely that very little of the benefits from any new incentives would really reach the smaller farmers.

If incentives are to be given to agriculture, it must be asked who is most likely to benefit from them.

The discrimination against agriculture is sometimes justified as being support of industrialization efforts. Industrialization is often held necessary to change the country's position in the international division of labor as a simple exporter of raw materials and importer of finished products. There is nothing wrong with this objective; however, from the viewpoint of efficiency, the policy-instruments used and the projects actually implemented leave much to be desired. Such policies and projects have had results which may not have been anticipated (certainly not desired) when they were first enunciated.

The overvalued currency (partly due to heavy foreign borrowing), which has penalized agricultural exports had, by the same token, encouraged the import-dependence of industries, contrary to the oft-stated imperative of developing self-reliance. The tariff structure, although now in the process of revision through a World Bank loan, still tends effectively to protect consumer goods rather than intermediate or capital goods. As a result, the protected consumer goods industries become much larger than what they should be, and has allowed a few large foreign and local firms to take commanding monopolistic positions, e.g., the food and beverage industies. To this extent, the trend towards concentration is not only due to specifically mandated privileges but is also built into the system of industrial incentives itself. Such large protected firms tend to be import-dependent and capital-intensive as well. On the other hand, the very objective of promoting intermediate and capital goods industries is frustrated, insofar as small but efficient machine and tool shops are not given sufficient protection against imports.

In addition to the distortions built into the system of incentives, the government has taken a direct and heavy-handed approach in determining large industrial projects to be implemented by granting certain entities monopolistic privileges and preempting private sector initiatives. The most obvious example of this approach is the copper smelter, whose inefficiency may be gauged by the fact that suppliers of ore have to be coerced into selling to it. Another ill-fated industrial venture has been the car-manufacturing program, where the government guaranteed privileged status to several firms competing for too small a market. Such privileges allowed these firms to soak up a large amount of credit and foreign exchange for many years, only for their inefficiency to be shown up later through their bankruptcies (e.g., DMG, Delta). The growing inefficiency of industry is well-documented; total factor productivity has been declining. The fact that resources are being sucked out of agriculture to support inefficient industrial activities only means that the country as a whole has been wasting its opportunities.

The fact that resources are being sucked out of agriculture to support inefficient industrial activities only means that the country as a whole has been wasting its opportunities.

As an alternative, a more efficient industrial sector should be promoted by adopting a competitively determined exchange rate, by adopting a uniform tariff for all imports, whose purpose is mainly revenue and not discrimination, and by allowing the private sector to have a free hand in determining the country's comparative advantage. If, after public discussion, it should be found necessary for national welfare to promote certain infant industries, then this should be done through outright subsidies to production, subject to legislative approval. This is superior to tariff protection in that, if the industry's promotion benefits the general public, then the general taxpayer must pay, rather than the consumer of the product alone. Secondly, being specific and subject to legislative approval, a subsidy is more visible and less likely to develop into a permanent monopolistic privilege. Again, of course, this presupposes a certain level of public awareness and participation in decision-making.

4.4 *Call a halt to further commercial foreign borrowing by the government. Negotiate a moratorium on principal and interest on existing commercial external debt.*

With the present level of the debt service hovering at $1.5 billion annually for interests alone, a rescheduling of the country's external debt has become unavoidable. The level of exports and other current foreign exchange inflows is obviously inadequate to cover imports at normal levels and at the same time service debts. The only question to be answered is under what terms such a rescheduling may be obtained.

Given the choice whether to allocate scarce foreign exchange to imports which are required to sustain production and employment, or to the servicing of past debts, a government mindful of the people's welfare would choose the former. The focus of negotiations by such a government with its creditors, therefore, should be on reducing the burden which the repayment of past debts represents for the economy. There are, of course, any number of possible ways of doing so, each not without its own shortcomings.

Given the choice whether to allocate scarce foreign exchange to imports which are required to sustain production and employment, or to the servicing of past debts, a government mindful of the people's welfare would choose the former.

On one extreme, some would advocate an outright repudiation of the entire debt. This might seem attractive in principle or, perhaps, as a bargaining position; it would immediately and permanently remove the pressure on the balance of payments coming from present and future debt-servicing and, ideally, allow the use of foreign exchange for imports. It might gain added attraction as an alternative for a new government which has repudiated past policies and feels no obligation to honor commitments of previous governments. Its critical premise, perhaps, is that most of the borrowed funds have been used on unproductive projects anyway and it would be "unfair" in a sense to expect the country to pay back debts from such projects.

Unfortunately, while attractive in principle, such an alternative would be difficult to implement. Creditor banks, which would certainly balk at the suggestion, could have recourse to retaliatory measures, such as the suspension of normal trade credits and the refusal to service foreign transactions. These could cripple trade, for the country then would have to resort to barter and to a drastic change in the direction of trade. Legitimate earnings from exports or import payments, insofar as they passed through private banks, could be "hijacked" as payment for outstanding debts. This would negate the anticipated beneficial effects of repudiation, since to that extent, foreign exchange inflows would still be preempted by debt service, rather than go to needed imports. Finally, some worthwhile projects which could otherwise have obtained foreign financing (e.g., in the private sector) would be unduly penalized, since a debt-repudiation would undoubtedly entail a stop to all future loans as a consequence.

On another extreme, the present government's approach has been to seek additional financing to service both past debts and to cover imports. For 1984 the additional financing being sought from both official and private sources is at least \$3.6 billion. On this basis it appears the government's basic response to shortfalls in the external accounts has not radically altered from the past; primary emphasis is still placed on financing, with internal readjustments being taken only if and to the extent required to secure new financing (e.g., as stipulated by IMF conditionality). Such an approach would be unobjectionable, assuming internal policies were already socially optimal and not themselves in need of basic overhaul; but that is, at the least, a debatable point.

The hopeful scenario underlying the government's approach is that the economy's condition is basically "sound," and that the project for which such funds were spent will eventually "pay off" and liquidate the debts. It is expected that within a relatively short period, the economy's performance will improve sufficiently to allow the repayment of past debts, as well as the new ones to be incurred during the years of recovery. Hence, the size of the debt is not really a matter of urgent concern, and the emphasis should be how to get even more.

The view of this report is markedly different from the two mentioned above. The following considerations have motivated our proposal: First, if the aim is to hasten economic recovery, then there is no point in saddling the economy with a large debt service, for this would only further slow down recovery, insofar as such debt-service payments preempt necessary imports. Second, there is possibly still a positive role which foreign financing, properly channelled, can play in the economy. The problem is not with borrowing per se, but in the methods of borrowing, the use to which such borrowings are put, and the possibility that the availability of foreign financing may encourage the use of domestic resources for unproductive purposes. In any case, any serious proposal must seek as much as possible to keep the country's financing options open. Third, there is the assessment that the country's level of debt and the consequent debt-service levels should be based not on optimistic forecasts, but should allow for the likelihood of future international disturbances (e.g., another U.S. recession). Hence, while the role of foreign borrowing is not being repudiated, definite self-imposed limits should be set on such borrowings, based on a cautious assessment of the likelihood of continuous growth in an increasingly turbulent world environment.

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Given these considerations, the following proposals are made. As a first priority, the government should negotiate with its commercial creditors for a suspension or a moratorium on principal and interest-payments on loans directly taken out or guaranteed by the government, the moratorium to last for a definite period of economic recovery. This proposed moratorium differs from the present one in that it would also suspend interest payments, which are actually more important at present than principal repayments.

As a first priority, the government should negotiate with its commercial creditors for a suspension or a moratorium on principal and interest-payments on loans directly taken out or guaranteed by the government. . .

However, this should not be interpreted as a repudiation of debt, but rather as a commitment to pay it upon the completion of economic recovery. In the meantime, accruing interest would, in effect, be reextended as new loans. If the country could join in the Third World clamor for interest-rate relief, and if such efforts succeed, its prospects could improve further. The immediate consequence of such a moratorium would be to allow the economy to use more of its foreign exchange earnings for necessary imports, rather than for servicing debts, during the period of recovery.

Apart from such accruing interest payments reextended as loans, however, the government should refrain from assuming any further commercial foreign debts, either directly or in the form of guarantees. Neither should it have to, if the previous recommendation regarding a reprioritization and scaling down of government expenditures is adhered to. As budget deficits are scaled down, so will the corresponding need to borrow abroad. On the other hand, there should be nothing to prevent efficient firms in the private sector from servicing their own debts, whether through their own foreign-exchange earnings (for exporters) or domestic peso profits (for import-substituting firms). The servicing of non-government-related debt could then be coursed efficiently through a competitive foreign exchange market. The participation of government and of many privileged but inefficient firms in such a foreign exchange market would be minimized, insofar as the moratorium on debt-service is in force. Hence, even if the exchange-rate were to be flexible, as we think it should be, the pressure on the rate would be less, and the currency would not depreciate unduly to penalize the more efficient sectors of the economy.

The restrictions on commercial borrowing by the government would not apply to the private sector, which may contract new commercial loans provided these are obtained without any government guarantees. Whether the government might still avail of loans from official and multilateral sources, whose interest rates are fixed and tend to be below commercial rates, should be decided only after sufficient public debate on the uses of such funds and the conditions attaching to them.

The restrictions on commercial borrowing by the government would not apply to the private sector, which may contract new commercial loans provided these are obtained without any government guarantees.

The most important assumption of this proposal, however, is that a recovery will indeed eventually occur, which would permit a redemption of debts, i.e., the original amount plus accruing interest. In turn, we consider that the likelihood of a recovery would really hinge on the adoption of such broad reforms as 4.1 to 4.3, but especially that pertaining to the system of government.

4.5 *Implement stabilization measures that cause the least burden to the poor.*

The so-called stabilization program is really based on a package of recommendations by the International Monetary Fund (IMF), intended to enable a borrowing country to pay off its debts eventually. These are usually in the form of broad macroeconomic prescriptions such as reducing the balance of payments deficits through exchange rate and price flexibility, narrowing government deficits down to a certain proportion of GNP, and slowing down the growth of money supply. The government of a debtor-country may then adopt such policy-instruments as it deems necessary in order to attain such targets. For example, the present government last October devalued the peso from ₱11 to ₱14 per dollar, and in June this year again placed it on a managed float at ₱18 to a dollar. Reserve requirements on deposits and deposit-substitutes were increased 5 percentage points last year. Again, in June this year presumably to narrow the budget deficit and "mop up excess liquidity," the government enacted new tax measures on imports, exports, and foreign exchange transactions. The increase in the specific taxes on oil products may also be regarded as an instance of revenue-raising.

There might be some disagreement over the specific mechanism by which the IMF stabilization policies might work to reduce a payments deficit. What is not probably in doubt, however, is that (a) if the aim is solely to reduce the payments deficits and allow the country to repay its debts, regardless of the social costs of adjustments, these measures are probably as good as any, and would suffice; (b) these social costs of adjustment are by no means negligible; (c) the IMF and the creditor-banks are not development institutions and are not particularly interested in such social costs.

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Much of the discussion of the IMF stabilization program has revolved around the aspect of conditionality, i.e., the fact that availment of IMF loans, which are crucial for obtaining commercial loans, hinges upon the acceptance and implementation of such policies as mentioned above. In fact, however, unless a country can afford to repudiate its debts or the Third World pressure for debt-relief gains ground, some difficult economic measures broadly similar to those mentioned would still have to be implemented, whether they were part of IMF conditionality or not.

The technical questions are less problematic than the social ones. There is no question for us that a flexible and unified exchange rate, smaller budget deficits, and slower monetary growth would reflect themselves in the balance of payments and eventually allow the repayment of debt. The more important question, however, is how the burden of adjustment is to be distributed internally among the different groups in society.

The more important question, however, is how the burden of adjustment is to be distributed internally among the different groups in society.

To take a concrete example, consider what some take to be the vexing question regarding the type of exchange-rate regime to follow. The manner in which the debate has been presented in the popular press and the lecture circuits is that it is a simple matter of deciding the advantages of fixed versus flexible exchange rates, or vice versa. The decision is then held to color one's opinion regarding the desirability of the IMF's stabilization program calling for exchange-rate flexibility.

The widespread reaction to devaluation and exchange-rate flexibility has understandably been hostile, since under present economic conditions, exchange-rate changes are for many, nothing but the most palpable signals for a by-now-familiar process of inflation, lagging real incomes, rising costs, perhaps bankruptcy, and unemployment. Yet, what must be pointed out is that, in almost all cases, devaluations and a weak currency are nothing but symptoms of a more serious economic malaise, i.e., the structural problems mentioned earlier, which cause outflows of foreign exchange persistently to exceed inflows. The exchange-rate is nothing but one price among many others; it is the tail of the dog, and reflects the movement of the dog, i.e., the economy. It must surely be a matter of the least importance to a dog dying of cancer, whether its tail should be allowed to droop (as it should) or should be kept up artificially by applying starch on it. Contrariwise a stable currency is so, whether under fixed or flexible rates, and for reasons largely unrelated to the exchange-rate regime. Unfortunately, some commentators choose to base their critique, mistakenly in our opinion, on such technical non-issues as fixed versus flexible exchange rates and autarky (sometimes known as "delinking") versus free trade.

If the historical levels and patterns of government expenditure continue, and if the trend towards greater economic concentration persists, there is ground for believing that the burden of adjustments required to implement the "stabilization program" will fall primarily on the earners of fixed income and others of the laboring class. The government's massive reliance on new specific taxes (i.e., on imports, exports, foreign exchange) is a matter for serious concern if it indicates the basic strategy to be followed throughout the whole adjustment period. There are any number of possible scenarios. What is common is that people, especially in the lower income brackets, must sooner or later, support incipient current account deficits through their reduced consumption. This can come about either through various forms of taxation (to narrow the budget deficit while maintaining the level of expenditures), or declines in real income as a result of either inflation caused by exchange rate changes, or falling economic activity. This is one sort of equilibrium that might be achieved if the internal distribution of economic power is not changed.

If the historical levels and patterns of government expenditure continue, and if the trend towards greater economic concentration persists, there is ground for believing that the burden of adjustments required to implement the "stabilization program" will fall primarily on the earners of fixed income and others of the laboring class.

On the other hand, assuming that some adjustment is going to take place in any event, a different state of affairs might be achieved, if the government's priorities were to be reoriented towards doing more with less, e.g., eliminating or reducing expenditures in areas with low social productivity, such as the military or the human settlements bureaucracy, or the dissipation of funds through the bailout of losing but privileged corporations. Then budget deficits could be narrowed without having to raise new taxes (especially specific taxes which are regressive); monetary growth could be curbed without starving the nonprivileged private sector, and the pressure on the balance of payments could be eased, reducing the need for currency depreciation. Underlying such decisions, of course, is in effect a change in the constituency which the government represents, from a small coterie which benefited from such expenditures and policies in the past, towards the laboring classes and hitherto suppressed entrepreneurs. This is one example of how a change in distribution can affect equilibrium outcomes. Of course, such changes will not solve all problems of development for the country, but it could make the transition much easier for the majority of our people.

4.6 *Adopt a unified and flexible exchange rate conditional upon the fulfillment of reforms.*

Previous to June this year, the exchange-rate system in existence was, in effect, a multi-tiered system. All foreign exchange earnings by exporters were gathered into a pool, from which availments by importers could be had, based on their position in a list of priorities which included interest payments, petroleum imports, inputs to nontraditional exports, and some others. Importers not on the list were expected to obtain their foreign exchange requirements from the blackmarket, at rates much higher than the official ₱14 to $1. This was a multiple exchange rate system in the sense that different agents were given different treatment. This system in effect imposed a tax on exporters to the extent that they actually coursed their earnings through the Central Bank, and subsidized consumers or importers of certain types of foreign goods, together with entities servicing their debts.

Previous to June this year, the exchange-rate system in existence was, in effect, a multi-tiered system.

In June this year the government announced that the peso would once more be put on the float and dollar-trading permitted, with banks being allowed to retain 20 percent of the foreign exchange coursed through them. At the same time, the ad valorem tax on all imports was raised to 10 percent, while a 30 percent tax was imposed on the difference between the value of exports at the current exchange rate and its value at the old rate of ₱14 to $1, the tax rate gradually falling to zero by the end of 1985. The "float" of the peso, as of this writing, seemed to be managed, since there was little trading ongoing at the "guiding rate" of ₱18 to $1. The blackmarket still retained its importance as the source of foreign exchange, although the differential between the "guiding rate" and the blackmarket rate had narrowed.

In a sense the June measures represented a step towards exchange-rate unification, though not as large a step as might seem from calling it a "floating rate." The most perceptible effect of the measures was first, that the difference in the exchange rate applied to priority versus non-priority imports was now less, thus triggering price increases for many of these imports; secondly, that, because of the new taxes, the government was now taking in a huge amount of revenues. The need to raise revenues is presumably related to the need to pay off large Central Bank borrowings which rose steeply previous to the National Assembly elections. In turn, the need to pay off such borrowings by government may be linked to the need to meet targets on liquidity growth imposed by the IMF.

The system of taxes applied to trade by the June measures penalizes both exporters and importers, and benefits the government. The de facto devaluation is 22 percent, but the increase in the peso payments importers have to make is really much more because of the ad valorem and foreign exchange taxes. On the other hand, the increase in per unit revenue to exporters is also much less than 22 percent because of the "stabilization tax" and the foreign exchange tax. The difference, of course, accrues to the government. Consumers will have to suffer insofar as they have to pay higher prices than necessary for goods with imported content, and producers would also lose from the fact that their incomes from exports are lower than what they could have been, thus discouraging a further expansion of production. More immediately, export payments could be postponed to subsequent periods, when the export tax rates are lower. While redressing only partly the distortion of the previous system between priority and nonpriority imports, the present system introduces by far a more serious distortion by making the peso prices of imports higher, and the peso prices of exports lower than what they could have been. In a word, the government sells high to importers and buys low from exporters. For the moment the government is acknowledging that these taxes are temporary measures to deal with the crisis. However, there is danger the huge amounts of revenue forthcoming may tempt the government to make such impositions permanent.

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In the long run, a system of multiple exchange rates, such as what is even now effectively in place, would have significant effects on investment and production decisions. Exporting industries would be discouraged at precisely a period when they could make a contribution to recovery. Import-competing industries could expand to beyond what might be considered efficient scale. Poorer consumers would be especially penalized by higher prices. There is thus a greater danger that such a system would result in patterns of trade, industrial development and income distribution which were never the principal objectives of the exchange-rate policies in the first place. Hence, we recommend that both the ad valorem and stabilization taxes be removed and the exchange rate allowed to float without additional encumbrances.

5 CONCLUDING REMARKS

The emphasis the report places on the role of internal obstacles does not imply a view that all underdevelopment may thus be explained without referring to external conditions, or to the character of relations between developed and developing countries. The question the analysis has sought to answer was in reality a modest one: why is the Philippines today not like Korea, or Taiwan, or Malaysia, or even Thailand? These countries have not undergone a crisis of the magnitude the Philippines has been undergoing; this is still the only country in Asia to have asked for a debt-rescheduling. It is this "uniqueness" of the Philippines in the context of developing Asia which this report has sought to explain. To that extent, it was necessary to abstract from the broader problems faced by developing countries as a group and to concentrate on what distinguished them from one another.

To some extent, however, regardless of the internal rearrangements they may undertake, developing countries have options which are still severely circumscribed by the existing international division of labor and distribution of power and economic resources among nations. Hence even if the country had not encountered problems of "agenda" and "regime," it still would have had to bear its measure of development pains, as even the above-mentioned nations now do.

Most problems which developing countries face as a group can also be solved only when they act in concert. Among them are the efforts to reduce the burden of debt, either through interest-rate reductions or a debt write-off; the efforts to obtain freer access to the markets of the developed countries through the lifting of tariff and nontariff barriers on developing-country exports; efforts to change the international division of labor and patterns of trade through mutual cooperation among developing countries in trade and industrialization, legislation on transnational and technology transfer, etc. The debate between "North" and "South" is really one over a redistribution of resources—or more accurately, access to resources—throughout the world. To the extent this succeeds for the developing countries, their prospects may improve. On the other hand, it would surely be wrong to suggest that improvements in the lives of the people must wait upon a resolution of global problems. But perhaps this might serve to explain why such a number of Third World elites sound magnificently revolutionary at international forums yet are such reactionaries at home: placing the blame on global problems absolves them of guilt at home. Indeed, as has been said before, "There can be no new international order unless there is a new national order."

Appendix 1

PRESIDENTIAL DECREES AND LETTERS OF INSTRUCTIONS CLASSIFIED BY ECONOMIC ACTIVITY[a]

	P.D.	LOI	Total PDs	Total LOIs
AGRICULTURE, FISHERY & FORESTRY	275,295,457,461,462,472,864,901, 1066,1162		10	—
Agricultural Crops Production				
General	4,48,135,194,216,413,435,440,547, 552,681,699,729,792,936,946,1038, 1040,1041,1124,1127,1142,1159,1203, 1380,1474,1517,1531,1585	58,113,145,372,391, 490,617,660,693-698, 704,705,736,747,790	29	20
Coconut	225,232,414,514,527,582,623,755, 1173,1468,1768,1863,1891	115,232,926	13	3
Coffee	1095		1	—
Cotton	350,1432	803	2	1
Fertilizer	135,669,992,1144		4	—
Grains	4,262,437,726,1046,1145,1181,1212, 1381,1485,1583,1620	78,79,97,105,115,123, 124,127,139,140,157,185 413,437,474,622,904,979, 1004	12	19
Seeds	1197		1	—
Soybean	1130		1	—
Sugar	114,388,579,659,686,775,924,1192, 1209,1890,1905		11	—
Fishery				
General	704,977,1058,1105,1110,1165,1475, 1819	401,402,550,769,791,919, 954,1146	8	8
Fishpond	569,706		2	—
Offshore	43,292,534,570,600		5	—
Forestry				
General	705,853,888,1120,1121,1559	409,550,721	6	3
Logging	54,330,331,428,595,607,865,953,1852	172,304,403	9	3
Production of Livestock, Poultry and Other Animals				
General	672,861,914	16,56,57	3	3
Cattle	45,619		2	—
Feeds		321,322,323	—	3
Hog	7		1	—
MINING AND QUARRYING				
General	99-A,104,237,295,398,463,512,513, 958,1093,1100,1101,1305,1385,1558, 1696,1721,1765,1887	119,184,757,778	19	4
Metallic Ore Mining				
General	1001,1070,1536	540	3	1
Aluminum	1767		1	—
Gold	581,1150	171	2	1
Non-metallic Quarrying and Mining				
Oil	8,102,334,392,405,429,436,456,469, 572,602,647,781,927,949,1128,1153, 1167,1174,1516,1889	148,361,392,400,416,420, 485,741,781,975,983,995, 1003,1078	21	14

Appendix 1—(Continuation)

	P.D.	LOI	Total PDs	Total LOIs
MANUFACTURING				
General	66,279,1717		3	—
Basic Metal Industries	272,476,554,770,1402,1611,1767	27,412,719,787,910,989	7	6
Chemicals and Petroleum, Coal, Rubber and Plastic Products				
General	87,318,333,416,438,529,1132,1194	111,125	8	2
Asphalt		189	—	1
Chemicals	1803,1858,1872		3	
Coal	972,1091,1103,1159,1722	339,715,752,1091	5	4
Petroleum	782,987,1104,1354,1857,1865	360,1073	6	2
Fabricated Metal Products, Machinery and Equipment				
General	1258,1572	516,517,524	2	3
Engine	656		1	—
Firearms		9	—	1
Food, Beverages and Tobacco				
General		88,166,183	—	3
Beverage	820,1089		2	—
Food	280,1139,1140,1141,1143,1144,1147, 1205,1790	406,664,1013	9	3
Tobacco	62,88,288,446,627,628,655,753,754, 897,920,1142,1481,1483	166	14	1
Non-metallic Mineral Products, Except Products of Petroleum and Coal				
Cement	94,912,1094	62	3	1
Paper and Mineral Products, Printing and Publishing		836	—	1
Textile, Wearing Apparel and Leather Industries				
General	652,750,1440,1813	558,998	4	2
Fiber	967,1208		2	—
Textile		64	—	1
Wood and Wood Products, Including Furniture and Fixtures	267	110	1	1
Other Manufacturing Industries				
Cottage	817,1788	83,122,230,786,1069	2	5
ELECTRICITY, GAS AND WATER				
General	390,1068,1121,1206,1360,1442,1443, 1459,1484,1571,1573,1700,1749	517,793,1089	13	3
Electricity	40,269,380,395,502,648,758,852, 938,948,1164,1201,1360,1370,1645	15,38,328,355,431,432,714, 735	15	8
Gas	178,349,390,487,510,663,727, 874,1058,1122,1135,1154		12	—
Water	198,424,425,765,979,1067,1345,1479	523,619,700,744,809	8	5

Appendix 1—(Continuation)

	P.D.	LOI	Total PDs	Total LOIs
CONSTRUCTION				
General	17,35,113,393,401,520,636,693, 986,1113,1136,1167	19,736	12	2
Public Works	3,47,141,475,759,1062,1387,1562	624	8	1
COMMERCE				
General	160,252,721,950,1040,1071,1183, 1469	195,384,499,503	8	4
Exports	403,545,670,685,930,941,1074, 1075,1386,1449,1785,1786	96,167,484	12	3
Imports	882,1108,1853	37	3	1
TRANSPORTATION, STORAGE AND COMMUNICATION				
Communication				
General	947,990,1362,1370	546,640,794,798,894	4	5
Radio	1504,1572		2	—
Telegraph	489		1	—
Telephone	217,329		2	—
Storage and Warehouses	634,670		2	—
Transportation Services				
General	130,165,214,215,320,522,634,636, 666,667,700,843,896,900,962, 1059,1004,1188,1284	43,93,181,296,306,389, 400,428,916,930	19	10
Air	57,696,844,894,895,963,1114,1115, 1253,1590,1901	68,194,343,378,380,381 414,417,684,943	11	10
Land	492,494,741,808,860,902,964, 1057, 1108,1377,1465,1680	407,409,639,332,763	12	5
Water	165,305,458,467,474,744,764,806, 833,845,857,866,878,890,917	157,181,294,332,433,538, 657,670,734,1085	15	10
FINANCING, INSURANCE, REAL ESTATE AND BUSINESS SERVICES				
Banking Institution	5,32,64,71,72,80,113,117,119,121, 122,150,168,195,236,264,378,379, 450,515,542,679,694,717,779,783, 811,865-B,1007,1107,1134,1195, 1197,1403,1452,1453,1461,1478, 1538,1539,1771,1792,1799,1801, 1855,1871,1904	7,67,90,144,182,430,477, 478,497,706,718	53	11
Business Services	1810		1	—
Financial Intermediaries	10,41,129,154,167,270,385,668,695 711,752,1006,1014,1034,1035,1454, 1458,1648	411,475,1021,1766	18	4
Insurance				
General	123,352,530,612,645,653,1094, 1141,1270,1451,1455,1460,1467	596	13	1
GSIS	396,1102,1411	162,190,310,483,739,827	3	6
Real Estate	538,762,1084		3	—

family incomes is arrayed by size of family income for each quarter, so that the families falling in one income bracket in one quarter are not the same as those in another quarter. Hence, it is meaningless to add up the incomes for each of the brackets for the four quarters. For the analysis of distribution, there is an urgent need for the quarterly incomes of each family to be brought together and income brackets constructed on the basis of the annual incomes of each family in the sample.

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4.0 Changes in concepts and definitions have become so frequent that time-series analysis, and international comparisons for some basic data have become extremely difficult. Comparability over time and across countries is a major purpose of data collection, and better planning and supervision of surveys and data collection by senior statisticians should at least be carried out. If changes must be made, there should be efforts to collect data on the older concepts if only to permit overlapping and linking of series in the years when changes occur. It could also help if consultations with potential users outside the government (e.g., academe and the private sector) could be held in annual workshops as in some countries to improve concepts and data presentation. These meetings can also help to reduce misunderstandings between users and producers of statistics.

4.1 As an example, consider that the employment figures published by NCSO for 1982 show the Philippine unemployment rate to be five percent. Quite apart from the question of underemployment, it would seem implausible that in the middle of the recession, the Philippines posted a figure close to what may be considered full employment in the U.S. or the U.K., respectively. The explanation is to be found in the definition of "employment"; anyone who worked one hour in the preceding three months is considered employed (Tidalgo and Esguerra, 1982). In 1976 the reference period was changed from "the past week" to "the past quarter." Moreover, employment was expanded to include such activities as home gardening and raising poultry, as long as there was a harvest. These changes effectively increased the numerator of the employment rates. The base of the employment rate, which is the labor force, was also changed. Where before the labor force included the population 10 years old or over, who were either employed or looking for work, the cutoff age was changed to 15 years, thus reducing the size of the denominator. All these changes tend to reduce the unemployment rate figure. What is additionally vexing is that, since data based on the older definition are no longer collected, researchers no longer have a basis for comparing employment performance before and after 1976.

4.2 The computation of the inflation rate has also been affected by redefinitions of the consumer price index (CPI). First, the composition of the market basket that goes into the making of the index has been trimmed down from an original 644 items to 393 items. Second, the relative weights of these items were also changed in 1982 (with the base year also being changed to 1978). For example, the weight given to food has increased, while that of housing has decreased. A number of the items in the CPI with large weights are under price control, and it has only been the official prices which are recorded, although many such items are sold at higher prices than the official. Such changes tend to convey an impression of stabler prices than what consumers actually experience.

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4.3 A similar shift has occurred in statistical series on wages. Before 1981, the most helpful series in assessing the trend in wages was the Central Bank series, which was based on a survey of wages actually received by workers in various establishments. However, in 1981 this series was terminated and the only series available has been one on legislated wages. If only because noncompliance with wage legislation is rampant, the latter series would overestimate the average level of wages being received.

4.4 Because of its relevance to the assessment of the debt crisis, the definition of the "debt-service ratio" has been thrown into relief recently. The "debt-service ratio" is the ratio of the country's payments on principal and interest of its external debt to its foreign exchange receipts. The smaller this ratio, in theory, the lighter the debt burden is relative to the country's ability to pay: the numerator represents "burden," the denominator the country's "paying capacity."

In the Philippines there is a statutory limit or ceiling of 20 percent to this debt-service ratio, and it has been made much of that this limit has never been exceeded. Such prudence seems hard to reconcile with the actual occurrence of the debt crisis. Again, a problem of definition is involved. To be meaningful, the numerator of the debt-service ratio should include interest and amortization on all external debt. However, the Philippine definition excludes what authorities call "revolving credit," which is short-term debt that is not a "fixed term." The denominator, on the other hand, should represent only foreign exchange receipts on current account, i.e., exports and other nontrade receipts. It is this denominator that has been subjected to redefinitions which increased its size. The original interpretation was that the denominator should be the average of foreign exchange receipts for the three previous years. In 1974 this was changed to just the previous year's receipts. In 1976 another substantive change was made: the definition of foreign exchange receipts was expanded to include private and public foreign loans. By the 1980s the denominator according to the new definition was about double that according to the original; this effectively halved the resulting debt-service ratio. Thus, the debt-service ratio has been defined in such a way that the numerator is unduly small, and the denominator unduly large; further, the ability to pay had, in effect, become dependent on the ability to borrow, rather than vice versa.

Thus, the debt-service ratio has been defined in such a way that the numerator is unduly small, and the denominator unduly large . . .

4.5 The definition of international reserves (IR) was also changed in 1977. Prior to that period, IR consisted of gold, foreign exchange assets of the Central Bank, and net foreign exchange holdings of the commercial banks. As of January 1, 1977, however, net foreign exchange holdings of commercial banks, which had become negative and larger over time, were excluded. Using the original definition would have shown that beginning 1977, the reserves would have covered much less than three months' imports, which is the rule of thumb.

5.0 The putting together of this report has itself uncovered several data gaps which would be essential in forming a complete picture of past economic policies and their effects.

5.1 Government corporations have grown rapidly over the last decade, yet there has been no consolidated official reporting on their number, financial status, sources of funds, reasons for establishment, etc.

5.2 The Central Bank reports some of its advances to banks under the bills payable account. This manner of reporting fails to identify special CB credits granted to selected banks and also prevents a thorough analysis of banks' intermediation function.

5.3 The sharp increase in the Central Bank's foreign liabilities needs to be explained through a breakdown of those liabilities according to purpose. Since international reserves include gross CB assets, the incurring of such liabilities would tend to raise international reserves artificially.

5.4 There has been no report detailing the external debt, especially as to the recipients of government debt guarantees and contingent liabilities.

There has been no report detailing the external debt, especially as to recipients of government debt guarantees and contingent liabilities.

5.5 Large borrowers from government banks (i.e., those receiving ₱100 million or more) need to be reported.

5.6 The national government's capital outlays include an "other capital outlays" account, which increased from 9.6 percent in 1976 to 32.6 percent in 1982. An account which takes up such a sizeable proportion of the total needs to be further specified.

6.0 A major riddle concerns the national accounts data of NEDA for the 1970s. Here, growth rates of per capita real product of 3.5 percent per annum are shown, which is not high compared with East and Southeast Asia, but high compared to South Asian standards. Since real agricultural product per capita of agricultural population also grew roughly at 3.5 percent, the increase in per capita real product in nonagriculture must also have been 3.5 percent (or more). On the other hand, daily or monthly wages, annualized for the 1970s, have been falling in real terms, as many researchers have pointed out. One may then ask the question: where did all the increase of 3.5 percent in per capita product in the nonagricultural sector go if real annual wages were falling? To the urban proprietors, salary earners and employers? If that were the case, the income distribution data should show a considerable increase in inequality. However, the increase has been only 10 percent in either the total disparity measure or Gini index. Two possibilities may be considered. One is that the income distribution data understate the rise in inequality.

The other possibility is that the real growth of GNP in the 1970s may have been overstated. Two pieces of evidence indirectly suggest this. One is that in the estimation of proprietors' income in the small firms in industry and services, the estimated growth of small proprietors' incomes may be overestimated (Oshima, 1983).

The other piece of evidence, simply stated, is as follows: One of the most stable relationships in modern economic growth is the decline in the percentage employed in agriculture as real income (GNP) per capita grows. In Malaysia, Taiwan, India, South Korea, Indonesia and Thailand during the 1970s, the share of agriculture in total employment declined 2.3 percent, on the average, for every one percent increase in per capita real income; the last two countries registered the smallest declines, 1.2 percent. In the Philippines, during the 1960s, it was 2.2 percent. In the 1970s, however, the decline was only 0.6 percent. Unless the data from the labor force surveys on agricultural employment are way off, such a small decline must be attributable to the overstatement of GNP growth rates. One must remember that the relation between agricultural share in employment and income growth per capita works through Engel's Law, a tendency that has been found to be virtually universal and which, in turn, is based on the declining income elasticities in the demand for food.

The GNP and GDP figures are of crucial importance in the analysis of the 1970s, and attempts to reexamine them should be made for possible upward biases. The main body of this report has worked on the assumption that national accounts figures were correct but yet found the economy's performance unsatisfactory for a country in that class. If the national accounts figures have indeed been overstated, that would mean even the previous unfavorable rating would have to be revised several notches downward.

If the national accounts figures have indeed been overstated, that would mean even the previous unfavorable rating would have to be revised several notches downward.

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