2 PHILIPPINES

Ione S. Alejo

2.1 Country's Profile

The Republic of the Philippines is strategically located at the crossroads of East and West. It is nestled some 800 kilometers off the southeast coast of the Asian mainland. From its location, one can reach within two to four hours' flight the following current and emerging economic dragons: Japan, South Korea, Taiwan, Hong Kong (China), Thailand, Malaysia, Singapore and Indonesia.

The archipelago of 7,107 islands with a land area of 299,404 sq. km. is divided into three major island groups: Luzon in the north, Visayas in the middle and Mindanao in the south. Administratively, the country is classified into 15 regions which represent group of provinces. Within the provinces are cities, municipalities (towns) and barangays (the smallest local government units).

The Philippines represents a market of approximately 70 million people, a population which grows at an annual rate 2.3 percent. Population density is 234 people per square kilometer. It is basically a young population with half of the populace below 22 years of age. The labor force stands at 26 million.

The Republic of the Philippines is a constitutional democracy, with the President as head of state. The national government has three coequal branches which exercises a system of checks and balances: the executive, the legislative and the judicial. The local governments are similar to the executive branch in structure and function. Provinces are headed by governors; cities and municipalities, by mayors; and barangays, by barangay captains.

Philippine culture is a product of diverse ethnic and historical influences. Though majority of the population is of Malay origin, the roots of many of its traditions, practices and gustatory preferences can be attributed to the Spanish, American, Chinese and Islamic. These are reflective of the 300 years of Spanish dominion, the 50 years of American colonization and the stream of Asian and Islamic traders who have visited the country throughout the history. As a result of these diverse influences, the country has more than 87 languages and dialects spoken. However, Filipino is the national language, while English is widely and extensively used in business, government and education. Spanish is another popular language.

The capital of the Philippines is *Manila*.

The unit of exchange is the *Philippine peso (P)*.

2.2 Overview of Macroeconomic Activity and Fiscal Position

From the beginning of the history of the Philippines one can realize that it has undergone a lot of struggles. Under the many regime it has been, from the Spanish rule to the American colonization, the war era up to the post wartime, and even when it has finally regained its independence 100 years ago, this country always seems to be always searching for ways to rebuild its economy. The economy has a difficulty in finding its way up because of so many internal constraints which to name a few are democratic, financial and peace. Despite the existence of the so many constraints and the difficulty it has been suffering one administration to another, the leaders of the nation had exerted a lot of effort to establish a stable economy. For a time it has established a good standing within the region it belongs but unfortunately it seemed that it has not maintained the good economic standing.

From then on the government was faced with a very great challenge of rebuilding the economy. One economic reform initiative after the other has been introduced. It was from 1986 during the Aquino administration that alongside the reinstitution of democratic principles was the task or rebuilding the treasury and restructuring the huge debts obtained during the past administration. Aside from the restructuring, the Department of Finance likewise spearheaded the Philippine privatization program and the rationalization of the financial operations of the government. Such other programs as tax and tariff reforms, trade and investment liberalization and other administrative reforms were instituted. These have somewhat made the economy take off a bit but because of the series of natural disasters, military coup attempts and unfavorable international developments aggravated the economic downtrend thus causing the economic take-off falter. In 1990, the government realized a need to establish an economic stabilization program. The program has somewhat succeeded in curbing the inflation to a single-digit level, reducing the deficits and attaining a modest economic growth in 1991.

It is worthy to note that the past few years, especially in 1995, the Philippines is moving closer to its dream of attaining sustained economic growth. For many years the Philippines has difficulty in establishing a position in the eyes of the world when it comes to its economy. There was a time when the Philippines was widely regarded as the "sick man of Asia", a country with a crippled economy, whose people are believed to be left behind by their more affluent neighbors. With the joint effort of the government and private sector, this unsavory remark about the Philippines whether justified or not is now believed to be a thing of the past.

Under the present administration, the country finally realized the economic turnaround it had only dreamed before. With the great opportunities being made available to the Philippines, the country is now aspiring to be Asia's new tiger. The government is determined to "change the Philippines from an economy gathering dust to an economy gathering steam".[1]

In 1996, the economy grew by an impressive 6.8% real growth, from 5.5% in 1995. Growth was spurred by exports and investments, which comprised 41.9% and 24.1% of gross national product in 1996, respectively. This growth is also attributable to the transformation of the government from being a burden to the nation's resources to a dynamic player in national progress. With the firm implementation of prudent fiscal policies, the Department of Finance has succeeded in effecting a stable fiscal position in the past years.

Much of the transformation of the economy has been due to the stable political climate of the country. This in turn has made possible the successful implementation of a broad range of reforms. The strategies considered for the economic reforms are the following:

a) establishing fiscal responsibility
b) implementation of a privatization program
c) independence of the Central Bank
d) monetary restraint
e) deregulation of key factors of the economy such as telecommunications, banking, airline and inter-island shipping
f) liberalization of trade and capital flows.

One factor that made possible the continuing expansion of the Philippine economy is the increase in exports and investments backed by a more open and competitive domestic environment and financial stability. The financial sector has also done its share in maintaining the economic situation. Helped by the improved business climate and sound fiscal and monetary policies, this sector has been well managed, thus creating an image that gains back the renewed confidence of investors and traders from within the country and without. Financial stability has been made easier to maintain through the constitutionally guaranteed independence of the Central Bank. Another favorable development was the decrease of the unemployment rate from 8.4% to 7.4%. The government believed that to sustain strong economic growth in the long term, the government has committed to opening the country to global economic competition. As a proof of its investment liberalization, as of 1996, 10 new foreign banks, among them Bank of Tokyo-Mitsubishi and Fuji Bank, have been authorized to start operations in the Philippines either as a branch, locally incorporated subsidiary or a joint venture. This indeed will benefit the country in terms of access and linkage to international investors and markets and the exchange of banking and financing technology.

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[1] Speech delivered by Philippine Secretary of Finance.

2.1.1 Macroeconomic Activity

International Environment

A.1 Trade Balance

The expansion of the Philippine economy is made significant because of the factors that led to its upward trend. Driving the consistent real economic growth of the Philippines has been rising exports. Exports posted a 29.4 percent in 1995 up from 18.5 percent in 1994. The surge in export figures have been led by a boom in the sale of electronics goods. The electronics and automotive sectors more than took up the slack left by the flagging garment sector. Electronics comprised 43% of the country's exports in 1995. The overall growth in exports continued in 1996 which resulted to an increase of total exports of goods and services by 23.9%. As for the 1st quarter of 1996, aggregate exports amounted to $4,685 million and this 25% higher for the same period last year and 10% from the program level. Maybe we can attribute this export performance as a result to the wave of relocations of these industries to the Philippines. The trend is expected to continue for some time as the labor cost in the Philippines seems lower than other countries and some other factors which led new businesses to move in the Philippines.

Despite this considerable increase in exports, importation has also its share of increase. For the year 1994 and 1995, the bulk of imports come from Japan, followed by United States, Republic of Korea and Taiwan. Imports for the 1st quarter of 1996 reached $7,331 million which is way above the target level by $930 million. Large part of the increase is traceable to the raw materials and capital goods which are actually the materials and accessories for the manufacture of electronics in line with the growth of electronics exports. Capital goods imports also increased compared to the programmed level by $310 million specifically telecommunications equipment and electrical machineries in line with the ongoing expansion in the telecommunication industry. Other importations that contributed to the sharp increase compared to the programmed are on mineral fuels and lubricants. Consumer goods also contributed to the increase because of the importation of 472 thousand metric tons of rice amounting to $160 million. Though the Philippines is mainly an agricultural country, the calamities that frequented the country for the past year have destroyed the expected crops, thus no choice but to import.

A.2 Current Account Balance

Table 2.1 Trade Balance

(in million US$)

Year	Exports	***Imports***	Trade Balance
1990	**8,186**	**12,206**	**-4,020**
1991	**8,840**	**12,051**	**-3,211**
1992	**9,824**	**14,519**	**-4,695**
1993	**11,375**	**17,597**	**-6,222**
1994	**13,483**	**21,333**	**-7,850**
1995	**17,447**	**26,391**	**-8,944**
1996	**4,685***	**7,331***	**-2,646***

1st qtr*

Table 2.2 Current Account Balance

(in million US$)

Year	Merchandise Trade, Net	Non-Merchandise Trade, Net	Transfers, Net	Current Account, Net
1990	-4020	739	714	-2567
1991	-3211	1515	827	- 869
1992	-4695	3020	817	- 858
1993	-6222	2507	699	-3016
1994	-7850	3964	936	-2950
1995	-8944	6084	880	-1980
1996	-2646*	1962*	185*	-499*

1st qtr *

The current account balance closed 1995 with a deficit of $1,980 million or 2.6 percent of GNP. The merchandise trade gap brought about by the large increase of imports over the exports, though the net inflows from services and net transfers recorded a considerable increase mainly accounts for the current account deficit of $1,980 million for 1996. Actual deficit for the first quarter of 1996 can be attributed mainly to the merchandise trade gap. Inflows from services for the 1st quarter was due to increased earnings particularly from peso conversion of foreign deposits; personal income; and miscellaneous services. Outflows also recorded an increase but still the net inflow showed a higher than programmed amount for the 1st quarter. Meanwhile, net transfers account, though reflecting an increase for the 1st quarter of 1996, it actually declined by 19.2% from the projected level. This decline can be explained by the reduced inflows from private and central government sources.

A.3 Exchange Rate and Exchange System

The following table shows the exchange rate relative to the US dollar. Peso is in a "managed-float" system where the Central Bank would intervene to keep it trading near a certain target. They keep it near a constant exchange rate to the US dollar. Stable gross reserve of the Central Bank can result in the appreciation of the peso. With the continued strength of private capital inflows, the gross reserve went up to $7 billion as Central Bank bought foreign exchange to stem the appreciation of the peso.

With the latest issue on the depreciation of some Asian currency, the Philippine peso was no longer in a "managed float". Beginning July, 1997, the government gave up trying to maintain an unrealistic rate and let the peso fall increasingly unhindered. It has now decreased in value for about 28 percent relative to the dollar.

A.4 Foreign Direct Investment

As mentioned in the earlier part of this paper, the real economic growth of the Philippines can be attributed to the rising exports and investments. Over the six year period, foreign direct investment have increased consistently. The increased can be said to be the result of the improved investor sentiment or the restoration of foreign investor's confidence in the Philippines. Liberalization of capital account transactions since 1992 has also contributed to the increase of gross foreign investment flows both the direct and portfolio investments. With the liberalized economy, the country is opened to external competition and freed of major policy-induced distortions, thus leaving Philippines a business environment that compares favorably with other reforming countries. The two main factors (restoration of investors' confidence and liberalization) which led the increase in investments have a great impact on the economy through increased technology transfer and reduce reliance on debt financing. In the Medium Term Development Plan of 1993-1998, it was pointed out that mobilization of foreign resources will be critical for the country's development over the medium term and this means that it should aim to secure direct foreign investment in excess of one billion annually. The Philippines for the past 3 years successfully attained such required amount as shown in the following graph. A substantial portion of the flows is linked with Build-Operate-Transfer (BOT) which was another manifestation of the privatization initiative of the Philippine government. The BOT was initially intended to solve the power crisis that plagued the country in the early 1990s. The BOT program for the power sector was such a success and in fact it includes such other projects as transport, irrigation and industrial area development. As of the close of 1996, there are a total of 82 BOT projects of which 25 have been completed. Total investment on these projects amounted to $4.17 billion.

A.5 Foreign Exchange Liabilities

The country's total foreign exchange liabilities stood at US$37,778 million at end – December 1995. Net availments contributed to the rise in debt stock which were principally disbursed to finance various projects such as power and energy development, financial, structural and economic reforms. The increase was also traceable to the renewed strengthening of major industrial countries' currencies against the US dollar, particularly the Japanese yen of which one third of the country's outstanding liabilities was denominated.

The bulk of the outstanding foreign exchange liabilities were medium and long term in nature which is equivalent to 86%. The short term liabilities' share in the increase of the total outstanding debt is on the account of the substantial increase in reported liabilities of commercial banks. Classified by creditor, liabilities owed to bilateral creditors accounted for 38.1 percent, 21.2 percent to multilateral sources, and 16.8 percent were obligations to banks and other financial institutions.

A.6 Aid

Aid comprises 1.6% of the Gross National Product 1994. The following tables shows some figures on ODA disbursed to the Philippines for the year 1992-1994.

The loan and grant aids for 1993 were mostly for the infrastructure projects which included engineering and science education projects, emergency telecommunications system , water supply in resettlement areas of Mt. Pinatubo victims and constructions of primary and

Table 2.3 Peso-Dollar Exchange Rate

Peso-Dollar Rate (P/USD)

	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995
Period Average	20.39	20.57	21.09	21.74	24.31	27.48	25.51	27.12	26.42	25.71	26.20
% Change	9.6	0.9	2.5	3.1	11.8	13.0	-7.2	6.3	-2.6	-2.7	1.9
End-of-Period	20.53	20.80	21.34	22.44	28.00	26.65	25.10	27.7	24.42	26.21	26.29
% Change	7.9	1.3	2.6	2.6	24.8	-4.8	-5.8	10.4	-11.8	7.4	.31

Figure 2.1 Foreign Direct Investment

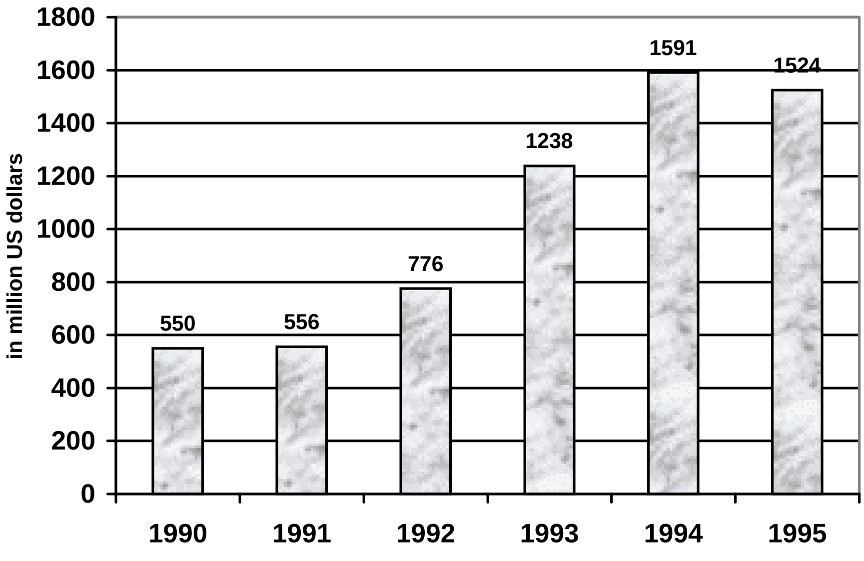


Table 2.4 Foreign Exchange Liabilities

(in million of US$)

Item	1990	1991	1992	1993	1994	1995
By Type of Debt	**28,549**	**29,956**	**30,934**	**34,282**	**37,079**	**37,778**
Med. & Long Term	24,173	25,129	25,678	29,247	31,882	32,499
Short Term	4,376	4,827	5,256	5,035	5,197	5,279
• Trade	4,099	4,589	4,397	3,495	3,401	2,674
• Non-Trade	277	238	319	1,540	1,796	2,605
By Institutional Creditor	**28,549**	**29,956**	**30,934**	**34,282**	**37,079**	**37,778**
Commercial Banks	10,982	10,451	9,083	5,682	5,521	6,345
Other Financial Institution	509	556	324	303	-	-
Suppliers	2,312	2,802	2,963	3,185	3,549	2,587
Multilateral of which	6,005	6,499	7,168	7,949	8,224	8,028
• I B R D	3,067	3,130	3,473	3,936	3,985	4,095
• IMF	997	1,165	1,183	1,312	1,139	814
• A D B	1,686	1,889	2,113	2,300	2,558	2,643
Bilateral	8,547	9,572	11,328	13,369	15,033	14,393
Others	194	76	68	3,794	4,752	6,425

Table 2.5 Amount of Development Assistance Countries and International Organizations' ODA Disbursements to the Philippines

(in million $)

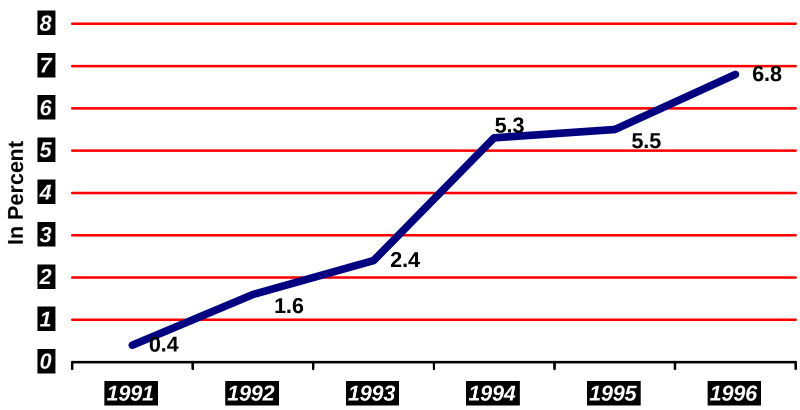
Year	DAC Countries	International Organization	Total
1992	1,538.60	176.9	1,715.50
1993	1,335.20	154.8	1,490.00
1994	942.6	110.6	1053.2

Table 2.6 Japan's ODA Disbursements to the Philippines

(in million $)

Year	Grants			Loan Aid		
	Grant Aid	Technical Cooperation	***Total***	Gross	Net	Total
1991	110.19	63.43	173.62	333.42	285.30	458.92
1992	112.34	73.32	185.66	1,200.13	845.01	1,030.67
1993	158.23	87.19	245.42	798.99	512.97	758.39
1994	138.41	110.41	248.82	586.85	342.78	591.60
1995	121.08	114.43	235.51	604.48	180.62	416.13
Total	**1,471.96**	**936.04**	**2,407.99**	**6,910.55**	**4,987.46**	**7,395.46**

Figure 2.2 GNP Growth Rate



secondary school buildings.

B. Domestic Environment

B.1 Economic Growth Rate (GNP)

Since 1991, real GNP has grown consistently and at an accelerating pace. The growth rate has accelerated from .4% in 1991 to an impressive 6.8% in 1996. In 1995, the primary task of the government was to sustain the economic gains of the past year. In that year, the economy is projected to grow at 6 to 6.5% but despite the good performance of some sectors like the public sector and the national government, growth expectations were dimmed throughout the year external factors commencing with the Mexican devaluation and confidence crisis followed by the Barings fiasco. Some investment advisors just thought that Philippines and other emerging economies might follow suit. As capital moved back from emerging economies, to safer business environment, Philippine financial managers promptly intervened in the foreign exchange market to dampen the speculative attack on the peso by moderate tightening of monetary policy. This prompt policy response renewed confidence in the economy which caused the increase in inflows, stabilized the exchange rate, bolstered the reserves and cut interest rates.

Weather disturbances also made its share in slowing the up surging economic growth. There was a scarcity of rice supply in the market resulting from prolonged drought and alleged hoarding by unscrupulous traders. Although the government resorted to rice importation to ease the situation on ashort term basis, the hike in the price of the commodity has pushed inflation to a higher-than-expected level. Other constraints to growth were the strong typhoons that hit various parts of the country causing damage to lives, crops and properties. The lahar problem in Central Luzon still hinders development efforts as billions of funds were allocated to alleviate the plight of those affected. The catastrophe in this region still affects its domestic production adversely.

Despite the crises in 1995 which would have devastated a less stable economy, a 5.5% growth was still achieved and this is attributable to the increase in merchandise exports and investment as mentioned earlier in this paper. The growth momentum continued in 1996 and it achieved a remarkable growth rate of 6.8%. Again, this growth is spurred by exports and investments, which comprised 41.9% and 24.1% of the GNP in 1996 respectively.

B.2 Inflation Rate

One of the three factors that are considered to be the significant contributors to the economic growth in 1995 is the management of inflation within single-digit level despite the rice crisis that plagued the country during the second half of the said year. The sound economic reforms which the government considered definitely has led inflation to decline. Inflation as measured by the changes in the consumer price index has declined from 1991 levels. There was a temporary increase in September 1995 of 11.3 percent which was due to the rice supply shortage but 1995 still managed to have a decline in inflation rate of 8.1 percent from the 9 percent in 1994. Though 1996 started with a double-digit inflation, it has slowly diminished to below 5% mark beginning September of 1996, thus bringing about an average annual inflation rate of 8.4%. The following graph shows the trend of inflation rate since 1990.

B.3 Consumption

The following table shows the amount of consumption of both the personal and the general government. Personal consumption expenditure (PCE) rose by 12% in 1995 posting a very slight increase from that of 1994 increase. For the 1st quarter of 1996, PCE rose by 4.2 percent. Expenditure on food which accounted for more than half of the total PCE went up by 4.1 percent. Fuel, light and water, and transportation and communication also showed notable increases. For 1995, government consumption expenditures increase by 16 percent, a good indication when compared to 1994 where the consumption increased by 23%.

B.4 Investment

It is said that the Philippine Board of Investments (BOI) has done a great job in 1995. With the numerous marketing intiatives which it aggressively pursued, it has helped the economy stay in the track of economic growth. The BOI has exceeded its target of P300 billion worth of approved investments to reach a level of P335 billion by the end of 1995.

It is a 12% above the target of approved investments. The public utilities sector absorbed most of the investment with P156.86 billion, followed by the manufacturing sector that raked in P150.64 billion and energy related projects which drew P13.16 billion in investments. This P335 billion worth of approved investments represents 479 projects that ultimately resulted to an estimated 80,866 more job opportunities for Filipinos.

As to equity, a total of P48.11 in foreign equity has been infused into the projects approved for 1995. More than 50% of these foreign equity investments or P26.4 billion were made by 100 percent foreign-owned corporation.

Figure 2.3 Annual Inflation Rate

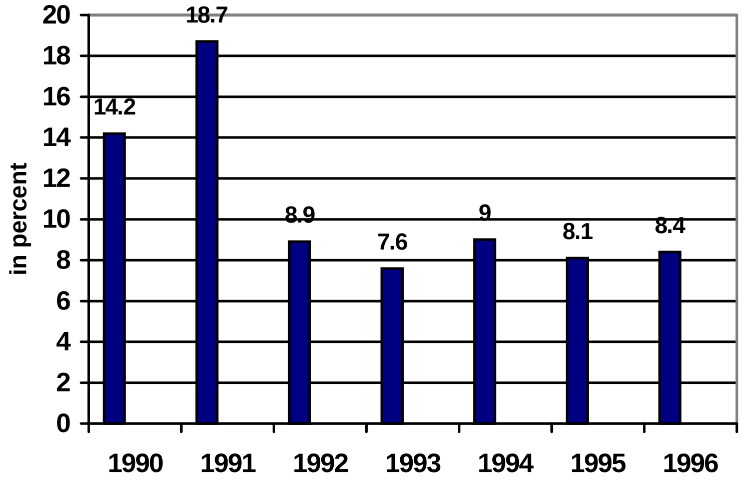
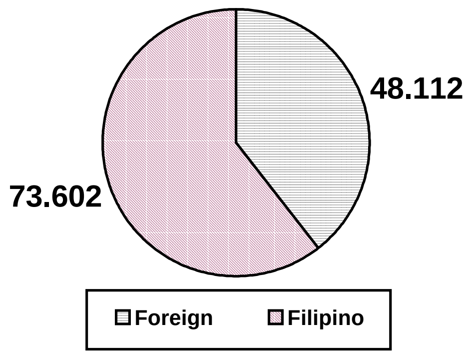


Table 2.7 Consumption

(in million pesos, at current prices)

	1990	1991	1992	1993	1994	1995
Personal Consumption Expenditures	767,061	916,384	1,019,209	1,122,528	1,258,750	1,411,904
General Government Consumption Expenditure	108,843	123,885	130,524	149,057	182,776	217,045
TOTAL	875,904	1,040,269	1,149,733	1,271,585	1,441,526	1,628,949

Figure 2.4 Equity Investment in Billion Pesos



The local equity investments drew in P73.6 billion worth of investments. The local businessmen outpaced their foreign counterpart in terms of investments infused. This confident attitude of Filipino businessmen on the economy to grow further encouraged foreign investors to consider doing business in the Philippines.

B.5 Capital Stock

The following graph shows the increasing trend of capitalization since 1991. This trend can be attributed to the institution of reforms in the capital market. A comprehensive set of reforms is being introduced to broaden the type of financial investments available in the market, strengthen and rationalize supervision, enhance laws for confidence, remove unnecessary regulations and other incentives that is neutral to various type of financial institutions. Among the said measures is the deepening of the government securities market. A new technology was employed to smooth the flow of government securities transactions. To further strengthen the capital market, the Securities and Exchange Commission (SEC) initiated amendments to some existing investment, financing and securities agreements. The amendments involved the liberalization of the foreign memberships in the board of investment companies and financing companies, removal of double taxation of mutual funds, recognition of the stock exchange as a self-regulatory organization, operational of the full disclosure policy, and the exercise of due diligence among market intermediaries, among others. With these in place, there is no doubt that investment will grow more and the capitalization can maintain its upward trend.

B.6 Money Supply

There seems to be a substantial increase in money supply in 1995 as compared to 1994. The money supply (M1) in 1995 is 24.28% of the total domestic liquidity.

B.7 Employment

The unemployment rate slowly decreased since 1991 up to 1993. In 1993 where the unemployment was lowest in the 5-year period (1991-1995), was also the period with the lowest inflation rate of 7.6%. With regards to 1995, the great inflow of investment which simply translates to new job opportunities, prevented the unemployment rate from sharply going up because of some economic disturbances that plagued the country during the year.

Figure 2.5 **Stock Market Capitalization in the Philippines**

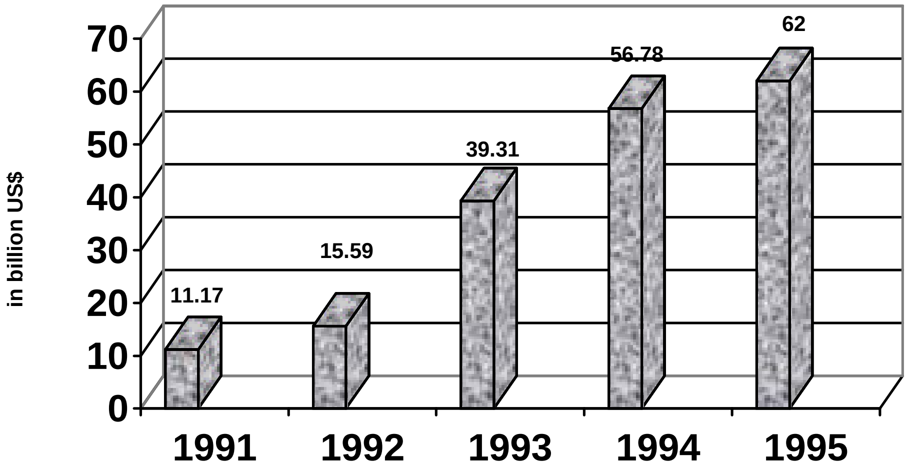


Table 2.8 **Money**

(in billion of pesos)

	1990	1991	1992	1993	1994	1995
Money Supply	**89.01**	**101.37**	**112.09**	**133.88**	**151.95**	**184.93**
% of change	**13.3**	**13.9**	**10.6**	**19.4**	**13.5**	**21.7**
Domestic Liquidity	**300.5**	**347.1**	**385.4**	**480.3**	**607.6**	**761.4**
Inflation Rate	**14.2%**	**18.7%**	**8.9%**	**7.6%**	**9.0%**	**8.1%**

Figure 2.6 Unemployment Rate

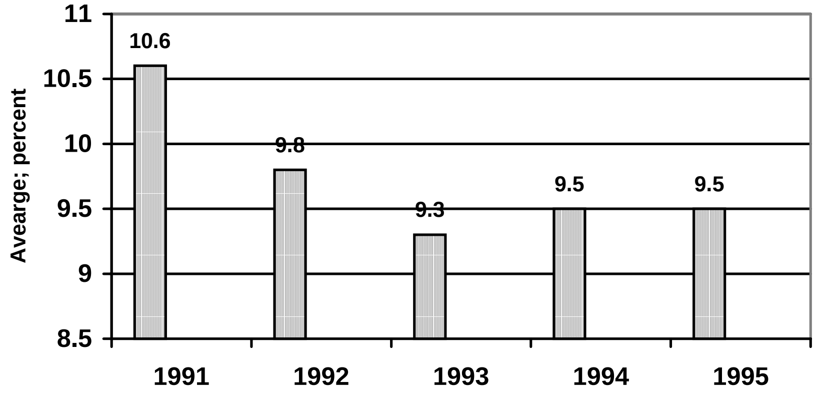
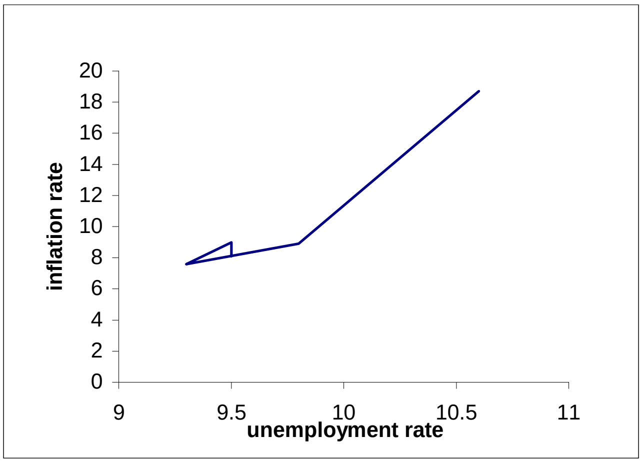


Figure 2.7 Inflation and Unemployment Rate 1991-1995



2.2.2 Fiscal Position

A. Government Expenditure

When compared to 1994 total government expenditure, the 1995 figure shows a 9.4% increase. But the amount of P350.1 billion total expenditure for the year is below the target figure by 4.5%. This can be traced to determination of the government to spend with prudence and restraint. The 1995 percentage of expenditure to GNP represents a decline of .6% compared with 1994 figure. The decline can be attributed to the savings realized from the 7.9% decrease in interest payments from 1994. The repayment of government debt in 1994 and 1995 and the existence of lower interest rates reduced the interest cost payments of the national government. Likewise there is an evident decline in the equity and lending which is due to the 50% cut in equity and subsidy extended to government owned and controlled corporations.

Though the government is so determined to rein its spending, it did not result in cutbacks in basic infrastructure and basic services as can be seen in the capital expenditures figure which substantially increased by 57% in 1995. National infrastructure projects increased by 20.6% from 1994 to 1995. The allocation for social services rose by 14.5% which is P106.8 billion in 1995. This figure reflected a higher spending for education, health and welfare.

Personnel services figure has also its share of increase. Compared with 1994, it incrased by almost 18%. This is the result of the wage hike of government employees under the salary standardization plan. Civil servants received 17% salary increase in 1995 which actually the third year of implementation of the salary standardization plan. This program intends the government salary to be comparative with those in the private sector.

As to the National Government (NG) cash budget, for the fist time in many years it has posted a surplus for two consecutive years (refer to Table 2.10). This really contributed to the stability of the public sector.

B. Aggregate Tax Revenue

The government revenues comprised 18.3% of GNP in 1995. Revenue collections posted a 7.2% increase over the 1994 figure. This is attributed to an increase in tax revenues of 14.4%, arising from strong performance of the country's collecting agencies. The Bureau of Customs (BOC) has raised its collection by 18.9% over 1994 amount and the Bureau of Internal Revenue (BIR) contributed a 12.1% increase from last year's collection.

From the previous table (Table 2.10) it can be noticed that non-tax revenues decreased by

Table 2.9 National Government Expenditures

(in million pesos)

	1990	1991	1992	1993	1994	1995
Current Operating Expenditure_	**n.a**	**n.a**	**219,505**	**234,561**	**277,274**	**289,053**
Interest Payments	**71,113**	**74,922**	**79,539**	**76,489**	**79,008**	**72,658**
Domestic	**53,727**	**56,347**	**63,112**	**56,183**	**59,771**	**51,569**
Foreign	**17,386**	**18,575**	**16,427**	**20,306**	**19,237**	**21,089**
Personal Services	**n.a**	**n.a**	**74,337**	**78,696**	**92,678**	**109,074**
Capital Expenditures	**n.a**	**n.a**	**46,125**	**37,830**	**33,606**	**52,673**
Net Lending & Equity	**2,769**	**5,965**	**-6,950**	**9,905**	**8,994**	**8,420**
TOTAL	**218,096**	**247,136**	**258,680**	**282,296**	**319,874**	**350,146**

Table 2.10 National Government Cash Budget

(in million of pesos)

	1990	1991	1992	1993	1994	1995
Tax Revenue	**151,698**	**182,275**	**208,706**	**230,171**	**271,305**	**310,517**
Non-Tax Revenue	**29,204**	**38,512**	**34,009**	**30,234**	**64,855**	**50,703**
Total Revenues	**180,902**	**220,787**	**242,715**	**260,405**	**336,160**	**361,220**
Expenditures	**218,096**	**247,136**	**258,680**	**282,296**	**319,874**	**350,146**
Overall Surplus/ Deficit (-)	**-37,194**	**-26,349**	**-15,965**	**-21,891**	**16,286**	**11,074**

21.8% in 1995. This decline is attributable to the decrease in income from Bureau of Treasury due to the governments policy to reduce government bank deposits and use funds to repay domestic debt. Another factor that contributed to the decline is the 23.7% decrease in privatization proceeds due to the bulk sale of one of the largest oil refinery in the country.

C. Borrowings

Gross borrowings for 1995 amounted to P75.5 billion of which P16.8 billion was raised from foreign sources and 58.7 billion from domestic sources.

Debt Management

As a result of the national government surplus and effective management of cash, the National Government's (NG) debt outstanding declined as a percentage of GNP from 61.3% in 1994 to 56.6% in 1995. The NG's external declined from 22.9% to 19.8 % while domestic debt declined from 38.5% to 36.8%. The ratio of NG's debt service to GNP rose from 6.8% to 7.2% as the National Government accelerated principal payments to its creditors. But this increase resulted in the decline in the percentage of interest payments to GNP from 4.6% to 3.7%. The NG continued to limit its availment of domestic loan to allow the private sector continued priority to use domestic funds allotted for loans. In 1995, the NG also paid back P12.9 billion in external borrowing compared to P11.6 billion repayment in 1994.

The country's overall outstanding external debt dropped from 57.3% of GNP in 1994 to 53% in 1995. This ratio is a great improvement for it placed the country closer to other neighboring countries in the region having sound economy. External debt service likewise declined from 17.4% of exports in 1994 to 14.9% in 1995. This decline can be attributed to the past efforts to restructure the country's debt at the same time enhancing the increase of export-and investment-led growth. Debt swapping was also a strategy employed wherein the government was able to conclude with the Swiss and German governments deep discounts of 50% and 70% respectively. Early in 1995, the Department of Finance cancelled the 5th round of rescheduling with the Paris Club, thus accelerating the graduation of the country from rescheduling country status. With this status together with other favorable rating from leading international credit rating agencies, the country was able to restore confidence of investors.

2.3 Tax Structure : Institutions and The Reality

The two major operating revenue contributing agencies under the Department of Finance are the Bureau of Internal Revenue (BIR) and the Bureau of Customs (BOC). The BIR is

Table 2.11

(in million pesos)

	1990	1991	1992	1993	1994	1995
Gross Domestic Borrowings	30,097	64,722	148,145	-16,990	4,623	58,653
Gross Foreign Borrowings	24,406	23,086	34,143	28,223	12,283	16,833
TOTAL	**54,503**	**87,808**	**182,288**	**11,233**	**16,906**	**75,486**

Figure 2.8 External Debt Ratio

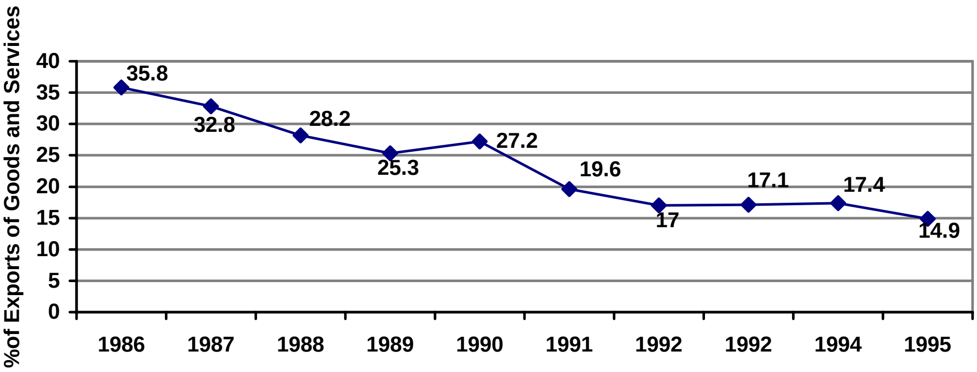
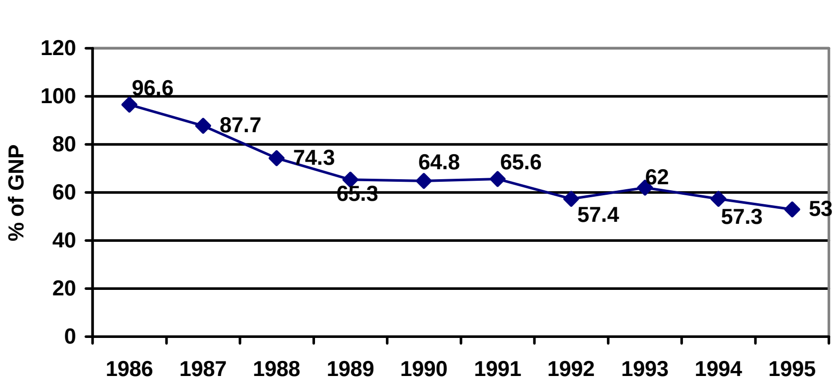


Figure 2.9 External Debt Service



responsible for 68% of the tax revenue in 1995 and BOC contributed 31% of the total tax revenue for the same year. The BOC takes charge of the tariffs and other coustom duties. The BIR is responsible for all national taxes.

The BIR has undertaken reforms and implemented some initiatives to increase voluntary compliance which actually comprises the bulk of the agency's collection. Meanwhile the BOC reported a record high collection for 1995 due also to some reforms this agency has undertaken. The BOC launched the On Line Release System which eliminated 40 steps in processing cargo transmittal, the Green Lane which is a fast lane for selected accounts, and the Valuation Center and Library which provides the various assessment units and offices of the BOC dutiable values in electronic form. Thus, the improved collections of the two main revenue collecting agencies of the government can be attributed to the improved tax administration through the computerization of both agencies. The BIR has computerized the registration of taxpayers, collections and bank reconciliation, processing of returns, audit of returns and monitoring of tax cases. The BOC launched a "Computerized selectivity System" at the Port of Manila to further speed up the processing of custom clearance and likewise to improve the delivery of its service to importers. A cashless transaction was inagurated in 1996 at the BOC through the electronic linkage of the port to the Land Bank of the Philippines.

A. The National Internal Revenue Taxes

Under the National Internal Revenue Code of the Philippines, the following are deemed to be national internal revenue taxes.

a) Income Tax
b) Estate and Donor's Tax
c) Excise taxes
d) Taxes on business
e) Documentary stamp taxes
f) Mining taxes; and
g) Miscellaneous taxes fees, fees and charges namely: taxes on banks, finance companies and others, franchise taxes, taxes on amusements and charges on tobacco, forest products and other inspection fees.

The Philippines adopts the progressive income tax system and the global tax system. The more you earn, the higher the rates you would be subjected to. Income from all sources are taxed subject to some limitations depending on your citizenship or residency. For a citizen, whether resident or not, he will be taxed for all income received within and without the Philippines. Corporations are also taxed the same way.

Table 2.12

(in million Pesos)

	1994	1995	
		Program	Actual
Total Revenues	336.3	370.01	361.2
Tax Revenues	271.3	310.2	310.5
BIR	187.4	214.1	210.2
BOC	81.6	93.4	97.6
Other Offices	2.2	2.8	2.7

Table 2.13 Kinds of Taxes and their Respective Rates

Kind of Tax	Tax Rate	Tax Base
Income Tax: on *Individual*	0 – 35%	Gross Compensation less personal exemptions.
Corporation :		
Domestic	35%	Gross income from within and without less deductions.
Foreign	35%	Gross Income from within.
Estate Tax	0 – 35%	Value of the estate less some deductions.
Donor's Tax	0 – 20%	Value of the gift.
Value Added Tax	10%	Gross selling price or gross value in money of the goods involved in the transaction.
Other percentage Taxes	Various rates	Gross receipts
Excise Tax :		
specific	Various rates	Weight or volume capacity or other physical unit of measurement
Ad valorem	various	Selling Price or other specified value of the good
Tax on sale or transfer of Real property	5%	On the selling price or the zonal valuation of the property whichever is higher.
Documentary Stamp Tax	various	On what kind of document or instrument is executed.

Majority of the taxes are self-assessed. The tax payable is being calculated by the taxpayer himself. Since May 1, 1997, collection of taxes is done through the services of Accredited Agent Banks (AAB) except in places where there is no AAB, the payment is to be made in cash with the revenue collection agent assigned in that particular place. The payment of the tax due is to be done at the time the return is filed. We call this the "pay as you file system". Withholding tax system is also employed in the Philippines as one of the modes of collection taxes. The following table shows the tax rates and tax base of the major classification

The following schedule is used to determine the income tax liability of an individual with taxable compensation, business and other income.

Not over P2,500	0%
Over P2500 but not over P5,000	1%
Over P5,000 but not over P10,000	P25 + 3% of excess over P5,000
Over P10,000 but not over P20,000	P175 + 7% of Excess over P10,000
Over P20,000 but not over P40, 000	P875 + 11% of Excess over P20,000
Over P40,000 but not over P60,000	P3,075 + 15% of Excess over P40,000
Over 60,000 but not over P100,000	P6,075 + 19% of Excess over P60,000
Over P100,000 but not over P250,000	P13,675 + 24% of excess over P100,000
Over P250,000 but not over P500,000	P49,675 + 29% of Excess over P250,000
Over P500,000	P122,175 + 35% of Excess over P500,000

B. Deductions from the Gross Income:

B.1 Personal, Additional and Special Additional Exemptions

For income derived purely from compensation, the only deduction allowed will be the personal and additional exemption which is *P9,000 for single/widow/widower/legally separated with no qualified dependents; P12,000 for head of the family* (unmarried or legally separated man or woman with one or both parents, or with one or more brothers or sisters, or with one or more legitimate, recognized natural, or legally adopted children living with and dependent upon the taxpayer; and *P18,000 for each married individual.* An *additional exemption of P5,000* shall be allowed for each of the taxpayer's qualified dependent children (not more than 21 years old, unmarried and not gainfully employed. Regardless of age are incapable of self-support because of mental or physical defect) not exceeding four. The husband is the proper claimant of the additional exemption unless he explicitly waives his right in favot of his wife in the withholding exemption certificate, in which case the wife shall be entitled to the additional exemption. A *special additional personal exemption of P4,000* is allowed to a taxpayer whose aggregate gross compensation income does not exceed P20,000.

For income derived from business, the appropriate exemption is deducted from the net income form business to arrive at the taxable income of the individual. It is worth to note that in the Philippines, foreign source gross income (less exemption) derived by a non-resident citizen is subjected to another set of rates. This is called the one; two; three percent.

If the amount subject to tax is:

Not over U.S. $6,000	**1%**
Over U.S. $6,000 but not over U.S. $20,000	US$60 + **2%** of excess over U.S.$6,000
Over U.S.$20,000	US$ 340 + **3%** of Excess over U. S. $20,000

Certain passive income such as interest, royalties, prizes except those amounting to less than P3,000, and other winnings except the Philippine Charity sweepstakes winnings are subjected to a final rate of 20%.

The following is the schedule to which the net estate of a decedent is subjected to. Estate tax is to be paid first before any distribution to the heirs can be made.

If the Net Estate is:

Over	***But not Over***	***The Tax Shall Be***	***Plus***	***Of Excess Over***
-	200,000	Exempt	---	-
P 200,000	500,000	5%	---	P 200,000
500,000	2,000,000	P 15,000	8%	500,000
2,000,000	5,000,000	135,000	12%	2,000,000
5,000,000	10,000,000	495,000	21%	5,000,000
10,000,000	And Over	1,545,000	35%	10,000,000

The deductions allowed from the Gross Estate are expenses (funeral expenses and judicial expenses of the testamentary or intestate proceedings);losses; indebtedness or claim against the estate such as loans, mortgages, etc.; and taxes.

Donor's Tax is computed based on the following schedule and is to be paid by any person, resident or non-resident, who transfers a property by gift.

If the Net Gift is:

Over	But not Over	The Tax Shall Be	Plus	Of Excess Over
---	P 50,000	Exempt	---	---
P 50,000	100,000	1.5%	---	P 50,000
100,000	200,000	P 750	3%	100,000
200,000	500,000	3,750	5%	200,000
500,000	1,000,000	18,750	8%	500,000
1,000,000	3,000,000	58,750	10%	1,000,000
3,000,000	5000,000	285,750	15%	3,000,000
5,000,000	---	558,750	20%	5,000,000

In general, the tax for each calendar year shall be computed on the basis of the net gifts made during the calendar year. If the donee or beneficiary is a *stranger* (a person not a brother or a sister, spouse, ancestor, and lineal decendant; or a relative not within the fourth degree of relationship; and any candidate, or political party for campaign purposes) the tax payable shall be ten per cent of the net gifts.

C. Collection Goal for the Internal Revenue

The goal for the BIR for a certain year is based on a certain percentage of the GNP. This is the reason why in 1995, the BIR missed the target of P 214.105 billion by 1.23% because of the inability of real GNP to reach the growth target of 6%. So in 1995, the BIR contributed 68.22% to the National Government revenue and in 1996, the share of BIR is 70.88%.

There is a significant increase both in terms of goal and of last year's figure. As the economy improved so with the collection performance of BIR. The bureau has exceeded its target of P258.825 billion by P1.949 billion or by 0.75% .In 1996, collection reached P 260.78 billion which is P49.31 billion or 23.32 % increase over 1995 figure. Contributing to the Bureau's improved collection performance is the positive growth posted by all major sectors of the country.

The BIR also realized an 11.45% tax effort ratio to GNP for CY 1996, which is an improvement over the 10.73% last year.

Taxes on Net Income and Profit registered the highest contribution at 52.29 % to the total tax revenues, followed by Excise taxes with 18.56% and closely followed by Value Added Tax with a share of 15.69%.

Figure 2.10 BIR Share in National Government Tax Revenues CY 1996

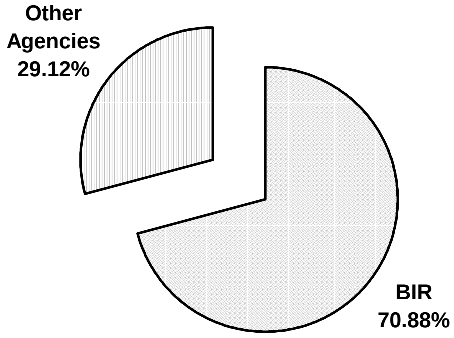
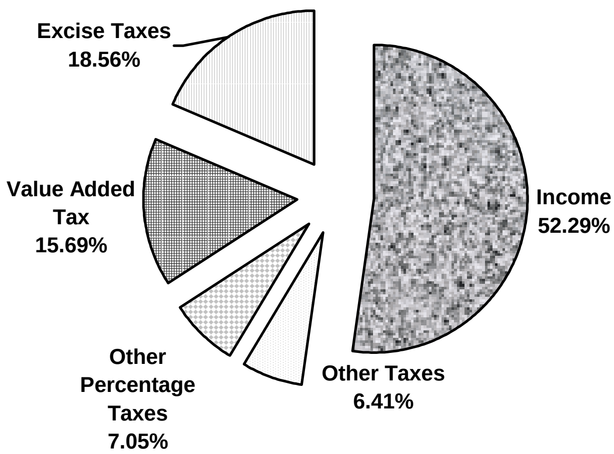


Figure 2.11 Percent Distribution of BIR Collection by Major Type of Tax, CY 1996



2.4 Country-Specific Fiscal Issues

Though the Philippines is enjoying an up trend in the economy, it does not mean that the task is over. The economic growth that the Philippines is experiencing is a result of the reforms and initiatives that has been instituted or implemented by the people in the government. As we live in a changing world, challenges do always exist. The Philippines has a lot of challenges ahead of her which the government has to face. The following are some issues which are most urgent at the moment.

a) Maintaining a sound fiscal position and raising private savings. - In order to attain this the following are some measures that will surely contribute to its attainment.

- The need to consolidate and strengthen the tax base by the passage of the other parts of the Comprehensive Tax Reform Package (CTRP). The CTRP is intended to be a self-sustaining revenue system that will provide increasing resources as the economy grows .
- Streamlining the Public Sector – this is intended to complement the tax reform package. The streamlining aims to build an efficient and professional bureaucracy that will be more responsive to the needs of the people.
- Instituting measures which should strengthen the government's fiscal position like improving the management of government's contingent liability exposure in BOT projects, developing a sustainable housing finance and coming up with a contractual savings reform.

b) Strengthening the country's ability to compete in the global marketplace.

c) Intensifying the social reform agenda efforts. The government has already adopted some programs that focuses of the provision of minimum basic needs, harnessing productive potential of the people and promoting social integration. Ensuring that the fruits of growth are distributed equally is considered the most challenging of all.

These are all the reforms being focused onto by the government but I think one specific issue that will eventually affect all the measures and reforms being instituted is the political stability. With the upcoming presidential election in May 1998, there are some apprehensions as to the political uncertainty. Concern is being expressed regarding the continuity of government policies but the present administration is hopeful that as a nation we can move on. As President Ramos stated in one of his speeches " We must not compromise the goals, the directions and the program that underpin our national economic turnaround. The issue of completing our national modernization is beyond partisan politics." [2]

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[2] Speech of H.E. President Fidel Ramos at the 5th Annual National Convention of the Federation of

2.5 Conclusion

People of the Republic of the Philippines are always optimistic that the growth the country has established will be sustained. Despite the apprehensions on some major changes and the presence of stumbling blocks along the way, it is hoped that it will always turn out for the better. The country has started treading in the economic field and with the reforms and initiative being instituted, it can move on at pace with its neighboring countries.

Filipino-American Media Associations of the US and Canada (FFAMAS) October 29, 1997, Manila.

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