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April 9, 1982

To: Members of the Executive Board

From: The Secretary

Subject: Philippines - Recent Economic Developments

This paper provides background information to the staff report on the 1982 Article IV consultation discussions with the Philippines, which was circulated as SM/82/55 on March 24, 1982 and has been tentatively scheduled for discussion on Friday, April 30, 1982.

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INTERNATIONAL MONETARY FUND

PHILIPPINES

Recent Economic Developments

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Approved by the Asian, Exchange and Trade Relations, and Fiscal Affairs Departments

April 7, 1982

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Philippines

Basic Data

Population (1981)	49.5 million
Population growth per annum (1981)	2.5 per cent
Real GNP growth per annum (1971-81)	5.9 per cent
GNP per capita (1981)	US$783

	1978	1979	1980	1981 1/
Selected aggregates as per cent of GNP				
Gross domestic investment	28.9	29.9	30.5	30.1
Gross domestic savings	22.9	25.0	24.9	24.6
Agricultural production	26.4	25.4	23.3	22.5
Manufacturing production	25.4	25.1	25.8	26.4
National Government revenue	13.5	13.5	13.1	11.7
National Government expenditure	14.7	13.7	14.4	15.6
Overall budget surplus/deficit (-)	-1.2	-0.1	-1.3	-3.9
Total liquidity 2/ 3/	29.1	26.3	25.7	25.7
Quasi-money 2/ 3/	19.6	17.6	17.1	18.0
Narrow money 2/	9.5	8.6	8.5	7.6
Exports of goods and services	17.7	19.0	20.5	19.3
Imports of goods and services	23.2	24.3	26.0	24.8
Current account deficit	4.9	5.3	5.8	6.2
Total disbursed external debt 2/ 4/	25.6	24.0	24.1	26.0
External debt service 5/	3.3	3.8	3.6	4.3
Annual percentage changes in selected economic indicators				
Gross national product (1972 prices)	6.5	5.9	5.4	2.5
Gross national product (current prices)	15.6	23.2	21.1	15.8
Consumer price index	7.6	18.8	17.8	11.8
National Government revenue	20.0	22.9	17.6	2.9
National Government expenditure	14.9	13.7	27.9	24.9
Total liquidity	18.0	10.7	18.2	15.8
Quasi-money	20.3	10.4	17.5	22.0
Narrow money	13.4	11.2	19.6	3.5
Merchandise exports, f.o.b.	8.7	34.3	25.8	2.1
Merchandise imports, f.o.b.	20.9	29.8	25.8	8.7
	(In millions of U.S. dollars)			
International reserves 2/				
Gross official reserves	1,883	2,423	3,155	2,697
(In months of imports)	(4.8)	(4.7)	(4.9)	(3.9)
Net international reserves of the banking system	153	-426	-778	-1,265

1/ Actual or latest estimate.
2/ End-of-year.
3/ Includes deposit substitutes.
4/ Excludes loans of maturities of one year or less but includes IMF.
5/ On debts with maturities of over one year and including IMF.

I. Introduction

The Philippine economy was subjected to important internal and external disturbances in 1980-81. The economy, which is highly dependent on imported oil, suffered a sharp deterioration in the terms of trade during the second round of oil price increases. This deterioration was aggravated by a substantial decline in the prices of the major commodity exports due largely to recessionary trends in the world economy. Compounding the effects of the depressed terms of trade, a financial crisis in early 1981 disrupted private sector activity and generated severe liquidity problems for a number of enterprises dependent upon these institutions for credit.

Reflecting these adverse developments, the current account deficit of the balance of payments rose substantially in 1980 and 1981, both in terms of absolute levels and as a percentage of GNP, while the rate of growth in real GNP decelerated. The rate of inflation increased sharply during 1979 and the first half of 1980, before declining significantly in the second half of 1980 and in 1981.

Policies during 1980-81 were directed at coping with the difficulties confronting the economy, while continuing to provide for an ambitious development program and for structural adjustments to improve export competitiveness and the efficiency of resource allocation. Fiscal policy, which was mildly expansionary during 1980, became more stimulative in 1981 as capital expenditures were adjusted to respond to the sluggishness of the economy and to the financial disruption. Government revenues in 1981, however, did not keep pace and, as a consequence, the overall budget deficit, in absolute terms and as a percentage of GNP, widened considerably. Monetary policy in 1981 was primarily designed to restore confidence in the financial system while preserving the downward trend in inflation. The rate of growth in total liquidity decelerated in 1981, even though large-scale emergency assistance was extended by the Central Bank to nonbank financial institutions affected by the confidence crisis. Structural measures adopted during the period to improve export competitiveness and the efficiency of resource allocation included: implementation of substantial tariff reform, elimination of all remaining interest rate ceilings on deposits, development of multipurpose banks, and measures to promote energy conservation and development.

II. Output, Employment, and Prices

1. Economic growth in recent years

Real economic growth during 1977-79 was remarkably stable, averaging 6 per cent increase per annum in real GNP (Appendix Table I and Chart 1). During the period, private consumption expenditure increased at a faster pace than government consumption; total consumption grew by over 5 per cent on average in real terms. Following an investment boom in 1975 led by an increase in private and government construction of more than 50 per cent in real terms, the rate of growth in fixed investment moderated to an average growth of about 7 per cent in the following four years. During this period, the growth in construction activity was primarily led by government expenditures. Export performance during 1977-79 was subject to substantial variation, with volume rising quite sharply in 1977 but declining in 1978; the average rate of growth in exports of goods and services during the period was about 9 per cent in real terms. Gross domestic savings during 1977-79 was equivalent to about 25 per cent of GNP on average, compared to an average for gross investment expenditures of about 29 per cent of GNP (Appendix Table II). During the period, the incremental capital output ratio rose moderately from a level of 3.9 in 1977 to about 4.1 in 1979.

Although the rate of growth decelerated in 1980, real GNP expanded by 5.4 per cent. This growth reflected a steady increase in real consumption, a relatively strong export performance, and substantial private sector investment, particularly in construction. Gross domestic savings during 1980 continued to be about 25 per cent of GNP and financed about 80 per cent of total investment.

According to preliminary official estimates released in January 1982, real GNP grew by 4.9 per cent in 1981. Most sectors registered moderate growth, with the exception of mining and quarrying, which was somewhat depressed. The extremely limited availability of primary data on domestic production and expenditure at the time the estimate was prepared, however, implied that the 4.9 per cent real growth was highly tentative.1/ The preliminary official estimate was difficult to reconcile with more reliable official data on exports, imports, and the fiscal accounts as well as survey data of the labor market.2/ The tentative staff estimate is in the range of 2 to 3 per cent, with 2.5 per cent being the midpoint estimate.

1/ There are a variety of problems affecting the national accounts data that indicate that estimates of real growth in 1981 may be subject to wide margins of error. The latest data from industrial surveys are several years behind and the reliability of the data collected by such surveys suffers from poor response rates. In the agricultural sector, production figures for several major crops were unavailable for 1981 at the time of the mission.

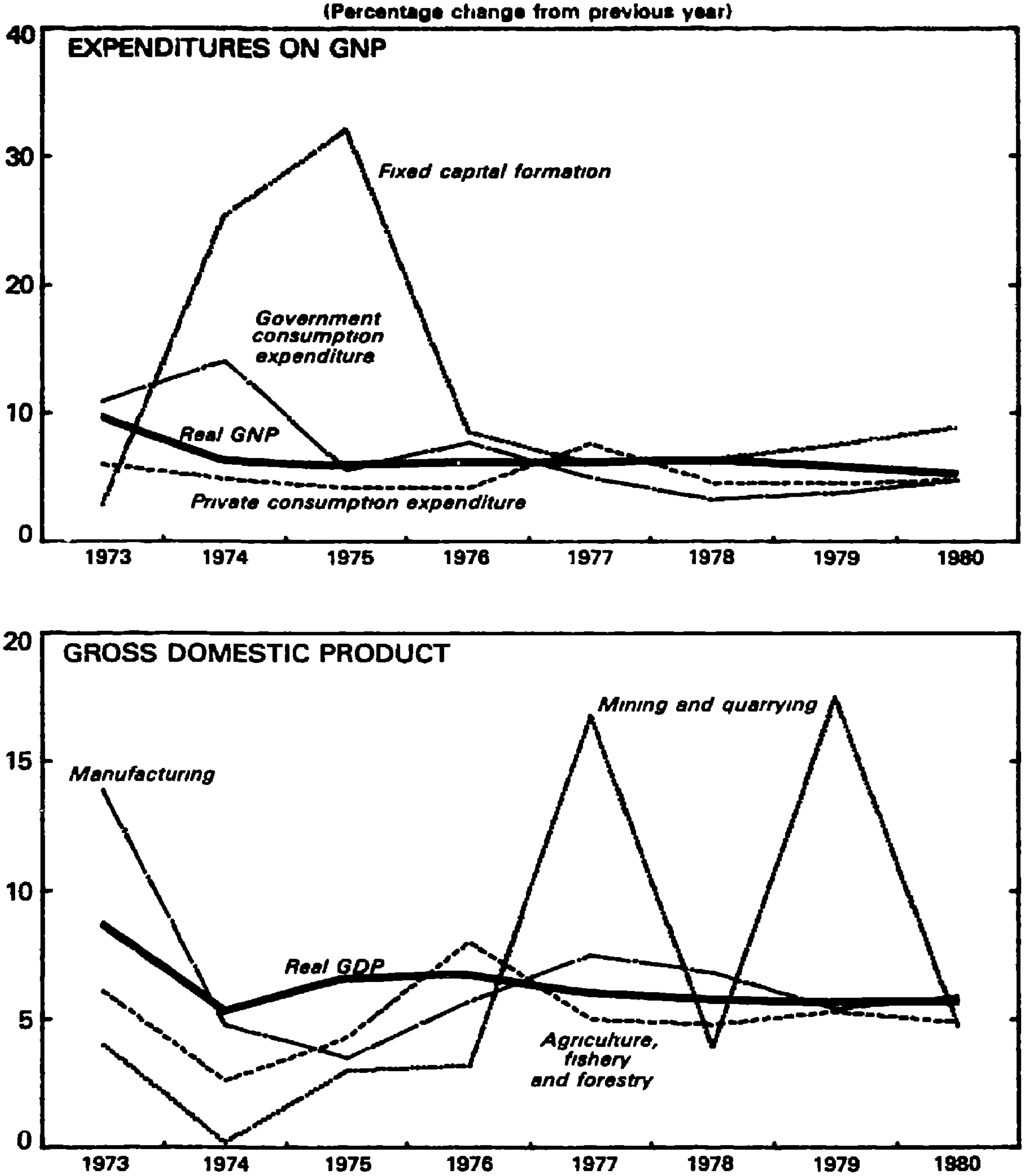
2/ The staff has estimated an equation for real imports as a standard log-linear function of real GNP and the relative price of imports. In the regression equation, which exhibited good statistical properties (e.g., $\bar{R}^2 = 0.88$, Durbin Watson statistic = 1.79), the income elasticity of imports was estimated to be about unity and the relative price elasticity to be about -0.4. Both estimated elasticities were highly significant, having relatively narrow confidence intervals. Given the official estimates of a 3 per cent decline in the volume of merchandise imports and an increase in the relative import prices of over 4 per cent, the estimated income and price elasticities suggest that real output may have actually declined in 1981.

CHART 1

PHILIPPINES

GROSS NATIONAL PRODUCT AT CONSTANT PRICES, 1973-80

(Percentage change from previous year)



Source Data supplied by the Philippine authorities.

The discussion of economic developments in 1981 in Sections II.2 and II.3 below is conducted in terms of the preliminary official estimates of national income accounts made in January 1982. However, new official data that are currently becoming available will be studied by the staff and discussed in a supplement to SM/82/55 that will be issued shortly.

2. Aggregate demand in 1980 and 1981

In spite of the second oil shock, real GNP continued to expand at a rate in excess of 5 per cent in 1980. Fixed capital formation grew by almost 9 per cent in real terms, largely on the strength of private sector investment activity; investment in machinery and equipment expanded by 8 per cent and private construction increased by 13 per cent. The growth of gross domestic investment, however, decelerated somewhat during 1980 due to a slowdown in the growth of inventories in real terms. Private consumption remained on its stable growth path, buoyed by a substantial increase in wages and the deceleration in inflation during the second half of the year. Exports of goods and services increased by almost 16 per cent in real terms.

The rate of growth of aggregate demand decelerated in 1981, mainly reflecting a slowdown in investment and weak export demand. Real gross domestic capital formation, which had increased by 6 per cent in 1980, expanded by only about 2 per cent in 1981. There was a further deceleration in the growth of real inventories, and there was a sharp deceleration in the growth of private investment in machinery and equipment and in construction as a result of overexpansion in previous years, a deterioration of export prospects, and a decline in profits. Business confidence was also

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2/ (cont'd from p. 2)
The weak tax revenue performance for 1981 was also difficult to explain with the official growth estimate. Domestic based tax revenues are estimated to have increased by about 9.5 per cent in 1981 which indicates a sharp drop in the elasticity of domestic based tax revenues with respect to nominal income. While some of the decline in the tax elasticity was probably due to problems in tax administration, it is also likely that real growth during 1981 might have been lower than the official growth estimate.

A survey of major manufacturing enterprises conducted by the National Economic and Development Authority for the first semester of 1981 showed a decline in employment in the following manufacturing sectors: micro-circuits, electric wires and wiring devices, electrical machinery, textile, milled and refined sugar, paper and paper products, basic industrial chemicals, nonmetallic mineral products, and basic mineral transport equipment.

impaired by liquidity problems for a number of enterprises following a major disturbance in the financial markets in January 1981. Public expenditures, notably in infrastructure, followed a countercyclical path to offset weak private sector investment in the second semester of 1981. Exports of goods and services declined by 3.4 per cent in real terms in 1981, due mainly to increased protectionism, the recessionary conditions in the industrial countries, and some administrative decisions restricting commodity exports. The volume of imports of goods and services declined by 6 per cent in 1981, according to official data. Real private consumption expenditures, by contrast, grew at about the same rate as in 1980, as inflation continued to decelerate throughout the year.1/

Gross domestic savings as a ratio of GNP was about 25 per cent in 1980-81, or about the same as in 1979. Gross domestic savings financed about 80 per cent of total investment in 1980-81. Net domestic savings accounted for about 60 per cent of total domestic savings during the period, with just under two thirds of net savings being generated by the private sector.

3. Aggregate supply in 1980 and 1981

In 1980, real GDP increased by about 5.8 per cent, about the same rate as in the previous three years (Appendix Table III and Chart 1). Output in the agriculture, fishing, and forestry sector increased by about 5 per cent in 1980, which is also in line with previous growth performance. Manufacturing output expanded by almost 6 per cent, with the highest growth rates reported in the machinery and furniture and fixture sectors. Mining and quarrying production, which grew by almost 18 per cent in 1979 in response to higher prices in world markets, increased by a further 5 per cent in 1980. In 1981, most sectors registered somewhat lower growth rates.

a. Agricultural production and policies

The Philippine agricultural sector, which accounted for about 23 per cent of GDP in 1980, compared with about 28 per cent a decade ago, continued its steady growth in 1980 (Appendix Table IV). Output in the agricultural sector is largely based on coconut products, rice, corn, and sugar.

An important priority of agricultural policies in recent years has been the production of staple foodgrains. To promote the output of grains and other crops, the Government has implemented specific programs in recent years to provide technical assistance, improved seeds,

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1/ According to official GNP data, total private consumption expenditures rose by 4.7 per cent; this development is somewhat difficult to reconcile with official balance of payments data that indicate a 3.5 per cent decline in non-oil consumer imports.

fertilizer, and credit at preferential interest rates. In addition, considerable progress has also been made in the construction of infrastructure (e.g., irrigation, rural electrification, and secondary roads). In 1978, the Agricultural Investments Priority Plan was introduced to provide fiscal incentives to priority agricultural activities such as the production of livestock, poultry, foodgrains, hybrid seeds, and citrus foods. The National Grain Authority and other agencies provide support prices to farmers for commodities such as rice, corn, and sugar. In 1981 the Ministry of Agriculture also intensified its Kabaska program, a special project intended to promote multiple cropping technology in the Iloilo province. A similar project is being developed for Mindanao, where most of the country's nonirrigated areas are farmed.

As a result of such policies, the Philippines has been a net exporter of rice since 1978. In 1980, the production of rice expanded by almost 6 per cent, with about two thirds of the increase due to higher yields per acre under cultivation (Appendix Table V). Self-sufficiency in corn was attained in 1979, although corn had to be imported in 1980, due to a decline in production. A new corn production program was launched in late 1981 with a goal of making the country a corn exporter within three years.

Preliminary data for 1981 indicate that corn, sugar, and pineapple production registered gains. Rice production declined, however, due to a reduction in rice acreage under cultivation and lower yields per acre. The decline in rice yields was mainly attributed to insufficient rainfall in the regions of Mindanao and Visayas, and crop damage caused by a severe typhoon during the latter part of the year.

The growth performance of the coconut industry has had an important influence on the overall level of economic activity. In 1980, 26 per cent of cropland was devoted to coconut production, which in turn represented 25 per cent of agricultural output value; about one third of the population depended on the coconut industry for at least part of its income. After a generally favorable period in the 1970s, the coconut industry faced two difficult years in 1980 and 1981. Whereas the value of coconut exports increased at an average annual rate of 19 per cent between 1970 and 1979, it decreased by 20 per cent in 1980 and rose by only 2 per cent in 1981. Further, while average export prices of coconut products registered a steady increase during the periods 1970-74 and 1976-79, interrupted by a serious decline in 1975, the unit value index of the Philippines' exports of coconut products fell by 29 per cent in 1980 and by 12 per cent in 1981. These developments are the result of several factors: excess supplies of copra and coconut oil and soybeans and other vegetable oils; high interest rates and carrying charges on forward purchases; and the recession in the industrialized countries.

The determination of domestic prices of coconut products, in particular the role of a levy on copra, was a controversial issue in 1981. The levy, which was ₱ 76 per 100 kilograms, had been criticized as a burden on the farmers. It was temporarily suspended in September but was reinstated later in that month at ₱ 50 per 100 kilograms, with a view to sustaining the major projects of the Philippine Coconut Authority, namely, the coconut replanting programs and other projects that benefit farmers. In January 1982, the flat coconut levy was changed to a floating levy which would range from 11 per cent to 23 per cent. Moreover, if international coconut prices fell below 20 cents per pound, the levy would not be collected.

Forestry production has been declining in recent years, because the Government has placed limits on exports of logs to conserve forests. Forestry production recovered in 1981, however, mainly due to the relatively higher average prices in world markets and a provision that allowed log exporters to apply the unused portion of their 1980 log export quotas in 1981.

A dairy production program was introduced in 1981 to increase milk production, cattle fattening, and the upgrading of local livestock. During the year, the Philippine Dairy Corporation (PDC) was organized under the Ministry of Agriculture. This corporation was set up to accelerate dairy production, increase employment and income among small farmers, and promote proper nutrition.

b. Mining and quarrying

Copper is the most important mineral produced in the Philippines. In 1980, there was an increase in copper output as additional mines were opened. However, as copper prices fell by almost 20 per cent in 1981, there was a sharp decline in the total value of copper output. Gold is mined separately and is also found in copper ores; following a decline in 1979, gold output increased both in 1980 and 1981. However, the value of gold production fell in 1981 on account of lower prices. Nickel, chromite and other metals recorded volume and value declines in 1981.

c. Manufacturing production and policies

The Philippine manufacturing sector contributed about 26 per cent to GDP in 1980. Food processing is the country's largest industry. Other important industries include chemical products, petroleum products, textiles, footwear, basic metals, nonmetallic mineral products, and a wide variety of machinery manufacturing.

In 1980-81, the rate of growth of manufacturing output remained somewhat depressed in comparison to recent years (Appendix Table V). In 1980, most of the sectors showed relatively low growth rates, with wood and paper products, including printing, registering negative growth rates. The petroleum and coal subsectors registered negative growth rates in both 1980 and 1981, reflecting the sharp increases in oil prices. The textile industry, which has registered very impressive growth rates in recent years, experienced sluggish growth in 1980-81.

The principal elements of the Government's industrial strategy are the eleven major industrial projects, promotion of small- and medium-scale industries, and regional dispersal of industry. A reform of overall industrial promotion policies is being implemented to encourage more efficiency and competition in the industrial sector and, ultimately, more rapid export growth and employment expansion. The first phase of the industrial policy reform consisted of trade liberalization (tariff reform and removal of quantitative import controls) and strengthening of export incentives. The tariff reform is taking effect over a four-year period from 1981 to 1985; the first stage of the reform, which concentrated on reducing tariff rates in excess of 50 per cent, was implemented on schedule in January 1981 and in January 1982. Quantitative import controls are also being removed in stages over the same period. Export incentives have also been strengthened to place exporters on a free trade basis (Annex I).

A second phase of industrial policy reform is now under preparation, and it will center around the reform of fiscal incentives for investment. The existing incentives system, which is biased toward capital-intensive production, will be replaced. The new system will compensate for market imperfections, and be more directly related to the Government's employment, export, and regional dispersal objectives.

The eleven major industrial projects are intended to deepen the industrial structure of the economy.1/ Construction of the copper smelter project started in 1980 and is expected to be completed in 1983, with an estimated cost of $373 million; the project is being financed by Japanese export credits, equity contributions by a private foreign contractor and by the International Finance Corporation, and cash loans. Plant construction for the phosphate fertilizer project started in 1981 and will be completed in 1984. The main plant will cost approximately $300 million, and is being supported by soft loans from Belgium and Spain and commercial loans. Progress has also been made in the construction of the cement expansion project and the diesel engine manufacturing plant.

The consolidated cost for the eleven major industrial projects is estimated at $4 billion, with the heaviest expenditures during 1982-85. The Government's financing strategy is to seek foreign equity investment and long-term suppliers' credits in order to minimize demand on domestic resources. The financing requirements will be met from foreign debt financing of $2.8 billion, foreign equity financing of $427 million, domestic equity of $495 million, and government funds of $300 million.

1/ These are: copper smelter project, phosphate fertilizer project, integrated steel mill project, heavy engineering industries project, cement expansion project, diesel engine manufacturing project, aluminum smelter project, integrated pulp and paper project, petrochemical complex program, alcogas project, and the coconut industry rationalization project.

4. Price developments

The rate of increase in consumer prices, which had averaged about 7 per cent annually during 1976-78, accelerated sharply during 1979 (Table 1). Consumer prices rose by 19 per cent in 1979, on average, as a result of higher energy costs, the abolition of price controls, and a substantial increase in minimum wages and allowances. The wholesale price index also recorded a 19 per cent increase in 1979.

The acceleration of inflation in 1979 continued into the first quarter of 1980, aggravated by further large increases in oil prices and subsequent hikes in utility rates as the Government continued its policy of fully passing on increases in oil import costs to consumers; the consumer price index for fuel, light, and water increased by 35 per cent in 1980. In February, the Government announced a three month freeze on prices of nine basic food items. A system of price controls, which allowed for periodic adjustments, was subsequently adopted and the list of controlled items was expanded to include three school supply items.1/ The Government also re-established the Price Stabilization Council. The Price Stabilization Council is the office for price regulation and its major functions are to recommend to the President the setting of price ceilings and to enlist the assistance of ministries and agencies in the enforcement of these ceilings.

From a peak of 25 per cent in the 12 months ending March 1980, the rate of inflation declined steadily through 1980; by December, the rate of inflation on a year-earlier basis had declined to 14 per cent.

Inflation continued to decelerate somewhat in 1981; for the year as a whole, the consumer price index rose by about 12 per cent on average and by 13 per cent on a December to December basis. This inflation rate includes the effects of upward adjustments in the prices of utilities and other price-controlled items; on average, the prices of controlled items increased at about the same rate as the prices of uncontrolled items in 1981. Food prices, which represent the largest item in the CPI, increased by 13 per cent in 1981. Fuel, light, and water prices increased by 15 per cent.

The rates and charges of public utilities--transportation, communication, power, and water services--have been adjusted upward in recent years, mainly to take account of higher costs. In 1981, the rates charged by the National Power Corporation were raised by an average of 13 per cent, and the rates charged by the Metropolitan Waterworks and Sewerage Authority were raised by 23 per cent. Bus rates were increased by an average of 12 per cent. Domestic air fares were increased by an average of 6 per cent, while international air fares were raised by 15 per cent. Telephone service charges were also increased, particularly those for international service which were increased by an average of 185 per cent.

1/ The 13 categories of food items and school supplies are: rice, corn, sugar, poultry, eggs, pork cuts, edible coconut oil, canned fish, canned milk, school pads, notebooks, pencils, and ballpens.

Table 1. Philippines: Consumer and Wholesale Price Indices, 1970-81

(Changes in per cent)

	(Weight)	1970-75 Average	1976 2/	1977 2/	1978 2/	1979 2/	1980 2/	1981 2/	1981 3/ March	June	Sept.	Dec.
Consumer price index 1/	(1.0000)	15.8	6.2	7.9	7.6	18.8	17.8	11.8	11.2	11.1	11.6	12.7
Food	(0.4904)	17.7	6.1	7.5	8.3	19.0	16.2	12.6	10.8	12.4	12.5	14.4
C othing	(0.0612)	22.0	2.0	5.9	10.3	17.6	28.3	9.7	14.3	8.6	8.2	4.4
Housing and repair	(0.1883)	11.3	4.7	7.2	7.2	14.3	9.8	10.9	11.2	10.4	10.9	10.9
Fuel, light, and water	(0.0395)	18.3	6.0	3.9	2.3	20.5	34.6	15.4	19.1	12.1	10.6	16.0
Transportation and other services	(0.1489)	12.1	10.6	14.3	8.1	23.1	23.1	12.4	10.2	11.1	13.3	15.0
Miscellaneous	(0.07[illegible])	19.0	5.3	4.3	4.1	18.9	17.8	7.7	9.2	6.4	6.8	6.4
Wholesale price index		21.2	9.2	7.4	6.8	19.0	18.3	12.7 4/	9.1	14.1	14.8	...

Sources: Data supplied by the Philippine authorities and *International Financial Statistics*.

1/ Covers Metropolitan Manila.
2/ Based on yearly averages.
3/ Changes over the corresponding month of previous year.
4/ Estimate based on data for first three quarters.

5. Employment and wages

Employment growth appears to have declined in 1980-81 as indicated by increased layoffs and the retrenchments and closures of businesses that have resulted from the increased cost of production and the effect of worldwide recession. The available survey data of the labor market, according to the Ministry of Labor and Employment, indicate the unemployment rate in Metro Manila was 14.6 per cent in 1980--a sharp increase from the 6.5 per cent unemployment in 1979. Although unemployment data for 1981 was incomplete, there is evidence that unemployment in Metro Manila rose further in 1981. Data on workers laid off due to shutdowns and retrenchments in 1981 disaggregated into industries indicate that textile and wearing apparel sector accounted for about 32 per cent of total layoffs, followed by the fabricated metal sector, wood and furniture, basic metals, and paper and printing. The manufacturing sector, as a whole, accounted for 82 per cent of total layoffs.

A moderation in wage increases accompanied the increase in unemployment in 1980. The index of average monthly earnings of wage earners in the Philippines increased by 21 per cent in 1980, compared to 25 per cent in 1979, implying a 2 per cent increase in real wages. Wages increased more rapidly in the manufacturing sector than in the agricultural sector. In line with its policy of maintaining the purchasing power of wages, the Government increased minimum wage rates and cost of living allowances in 1980-81. In August 1980, the minimum daily wage was raised by ₱ 1 and additional increases in the cost of living allowances for workers were granted. In January 1981, the mandatory living allowances were integrated into the basic pay of all covered workers, thereby increasing the statutory daily minimum wage by ₱ 6. Minimum wages were increased in March 1981 when the mandatory emergency living allowance of all workers earning less than ₱ 1,500 per month was increased by ₱ 2.00, ₱ 1.50, and ₱ 1.00 per day for nonagricultural, agricultural plantation workers, and agricultural nonplantation workers, respectively. As of March 1981, the effective minimum daily wage was ₱ 31.82 for the nonagricultural sector and ₱ 26.18 for the agricultural sector. However, to protect the competitiveness of labor-intensive enterprises in depressed areas and export firms from the increased cost of production, the law provides for exemptions due to temporary financial distress and dislocations. The authorities received 1,630 petitions from employers for minimum wage exemptions during 1979-81, of which only 430 were accepted. These exemptions affected about 11,000 workers in total.

Measures were implemented during 1981 to improve employment opportunities domestically and overseas. These included the implementation of the Kilusang sa Kabuhayan at Kaunlaran (KKK) Program (the National Livelihood Movement). The aim of the KKK program is to promote economic and social development by transforming the country's 42,000 barangays (districts) into self-reliant productive units through the establishment of various livelihood projects and enterprises to be owned and managed by the community residents themselves. The program places primary emphasis on private enterprise and is expected to generate 750,000 jobs per year.

Measures were also taken to promote overseas employment, including the creation of a welfare fund for overseas workers and improvements in recruitment. As of end-September 1981, the program had placed a total of 204,709 workers overseas, compared with a total of 161,611 workers as of end-September 1980.

6. Energy

The major source of energy supply in the Philippines is petroleum, which provided 83 per cent of total energy consumption in 1981 (Table 2). The other sources of energy are hydroelectricity (8.1 per cent), geothermal (6.1 per cent) and coal (1.6 per cent). Domestic petroleum production is limited, accounting for only about 3 per cent of petroleum requirements in 1981.

Table 2. Philippines: Energy Supply, 1979-81

(In millions of barrels or equivalent)

	1979	1980	1981 1/
Total supply of energy	89.32	88.51	87.53
Oil imports	74.89	73.72	71.20
Domestic sources of energy	14.43	14.79	16.33
Oil	7.72	3.77	1.88
Non-oil			
Of which: Coal	0.80	0.97	1.36
Hydro	4.80	6.19	7.10
Geothermal	1.10	3.84	5.34
Other	0.01	0.02	0.65
Memorandum item:			
Total domestic energy output	14.43	14.79	16.33
(As per cent of total energy)	(16.2)	(16.7)	(18.7)
Index of energy intensity 2/	1.07	1.00	...

Source: Data supplied by Philippine authorities.

1/ Estimate.
2/ Defined as ratio of total energy consumption in millions of barrels of oil equivalent to GNP in billions of pesos at 1972 prices.

The Government is pursuing an active energy policy to reduce the country's dependence on imported petroleum through expanded exploration and development of domestic energy resources as well as through energy conservation. The primary goal of the Five-Year Energy Program for 1981-86 is the substitution of imported petroleum with non-oil alternative energy sources and indigenous oil. The share of oil-based energy is projected to be reduced to below 50 per cent by 1986 as a result of oil substitution programs that emphasize increased reliance on coal and further development of the country's regenerative fuel capabilities in hydroelectric, geothermal, and diffused solar energy. This program embodies a reduction of the share of oil used in power generation, heating, and industrial operations. The share of oil used in power generation is expected to fall from about 70 per cent in 1980 to about 30 per cent in 1986, as the share of coal, hydro, geothermal, and nuclear power generation each expand by approximately 10 percentage points. Large-scale industrial energy users, such as the mining, steel, and fertilizer industries, are being encouraged to convert from oil to coal for their energy needs.

To meet these targets, coal requirements will increase from 0.3 million metric tons in 1981 to about 7 million metric tons in 1986. It is projected that the increased coal requirement in 1986 will be satisfied by about 4 million metric tons from local sources and about 3 million metric tons of imports. Geothermal development will focus on the drilling activities on Tiwi, Makiling-Banahaw, Tongonau, and Paslimpinan steamfield areas which are in advanced stages of development. By 1986, it is projected that eight fields will be developed with a total of 615 wells. The hydroelectric resource potential will be developed with the installation of 1,315 megawatts of additional capacity, raising the total capacity to 2,258 megawatts--about two and a half times the existing capacity in 1980.

Nonconventional energy sources, such as cocodiesel and alcogas, are projected to grow over the next five years as technology transfer, mass production, and lower costs will make them more competitive compared to traditional fuels. By 1986, contributions from these sources will be equivalent to about 3 million barrels of oil, or over 2 per cent of total primary energy consumption. Under the alcogas program, alcohol production for 1981 is estimated at 9 million liters, displacing about 0.58 per cent or 57,000 barrels of oil equivalent of gasoline demand. Given the programmed construction of additional distilleries, there will be nine alcohol distilleries in 1986 producing 180 million liters, or over 1 million barrels of oil equivalent, displacing the total gasoline requirement by 14 per cent.

Energy conservation has been identified as a primary objective. A key element of energy conservation is the official policy of adjusting domestic retail prices of oil products to reflect changes in import prices of oil. Retail prices of regular gasoline increased by 70 per cent during 1980 and by a further 6 per cent in 1981. The price of gasoline is set higher than diesel in order to promote the public transport sector. A number of other conservation measures have been introduced in recent years to curtail energy usage in the public and private sectors. These measures entailed: (a) the national dessemination of information on energy conservation through the media, schools, seminars, etc.; (b) the auditing and monitoring of energy consumption by industrial, commercial, public sector and transport enterprises; (c) legislation regulating the standards of energy efficiency for electrical power machines, the operating hours of business and entertainment establishments, and the use of neon lights, air conditioning, etc.; and (d) fiscal measures to discourage the residential consumption of electricity in excess of a certain limit.

7. Development planning

The basic objectives of the Five-Year Development Plan (1978-82) are: to sustain increases in agricultural output and maintain self-sufficiency in rice; to promote industrial growth and create employment opportunities; to reduce dependence on imported oil; and to remove income disparities and develop lagging areas, especially rural areas. Special emphasis has been placed on labor-intensive and export-oriented industrialization. The implementation of the Plan has been adversely affected by the economic slowdown in the industrial countries and the rapid increase in the prices of oil products. Real GNP growth has been less than the Plan targets and the rate of inflation has exceeded the 7 per cent guideline. Nonetheless, progress was made in the expansion of infrastructure support such as in transportation, electrification, and irrigation; in reduced dependence on imported oil; and in agrarian reform through land transfer and extension of leasehold contracts.

The Development Plan for 1983-87 was submitted to the Batasang Pambansa, the country's legislature, for approval in December 1981. The new Plan also aims at balanced development of the various sectors of the economy and an equitable distribution of the gains from development. The key elements of the macroeconomic strategy to be pursued are the following: efficient exploitation of agricultural potentials for food, agro-energy, and export crops; industrial development along the lines of comparative advantage; expansion of necessary infrastructure to support the agricultural and industrial growth; import-substituting investments and effective demand management in the energy sector. (The major quantitative macroeconomic targets of the Plan are presented in Annex II.) In industry, the Plan aims at the promotion of labor-intensive industries, although capital-intensive industries based on domestic raw materials will also be emphasized. Since the average capital/labor ratio in small- and medium-scale industries is only about half of that in large-scale enterprises, the Government will expand its program of industrial extension which includes technical assistance for project feasibility studies, marketing assistance and preferential credit. To reduce the country's dependence on oil imports, the development of hydroelectric and geothermal energy will be promoted. The Government will continue to give high priority to petroleum exploration and development.

III. Public Finance

The general government sector in the Philippines consists of the National Government and a large number of local government units, covering 88 provinces, 62 cities, 1,557 municipalities, and some 42,000 villages. The Social Security System (SSS) and the Government Service Insurance System (GSIS), which have their own budgets, are also part of the general government sector. There are 37 nonfinancial public enterprises, consisting of public utilities and enterprises engaged in industrial and commercial activities. 1/2/

1. National government budget

National government budgetary operations are effected through the General Fund, which covers the current and capital budgets. The budget shows revenue on an accrual basis and expenditure on an obligational basis, but the budget documents also give estimates of major aggregates on a cash basis. On the basis of expenditure obligations, cash disbursement ceilings (CDCs) are established, which specify the maximum amount of cash which an agency can withdraw from the Treasury during the year for payments of current obligations and prior years' accounts, broken down into quarters. The cash budget estimates of expenditure include a "reserve" (a percentage of budgeted expenditure) which can be withheld if revenue developments fall short of expectations. This "reserve" mechanism provides a flexible instrument for controlling government expenditure and for achieving overall stabilization objectives.

A summary statement of the cash budgetary operations of the National Government for the period 1977-81 is presented in Table 3, which also provides the official budgetary estimates for 1982 on a cash basis. The actual data are obtained from the Cash Operations Statement (COS) of the Treasury, which is issued monthly with a lag in the availability of data of about two months. While data from the COS have the virtue of being relatively current, in some areas the available data do not permit a disaggregated analysis of government finances. In particular, no functional analysis of expenditure can be made from the data as recorded in the COS, and only a limited analysis of expenditure by economic category. Revenue can be classified by major tax categories, but a breakdown within these categories is usually not possible, e.g., of import duties and excise duties by commodity groups.

Treasury cash balances, except for minor amounts of cash in vaults, are held as deposits with the Central Bank and with deposit money banks. In addition, in recent years, the Treasury has built up considerable balances with the Development Bank of the Philippines (DBP) and the Land

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1/ A review of the structure of the public sector is provided in SM/80/183, page 14.
2/ For a list of these enterprises, see Government Finance Statistics Yearbook, Vol. V, 1981, page 497.

Table 3. Philippines: National Government Cash Budget, 1977-82

(In billions of Philippine pesos)

	1977	1978	1979	1980	1981 Latest est.	1982 Estimates
Revenue	20.0	24.0	29.5	34.7	35.7	40.7
Tax revenue	17.0	20.5	25.9	30.5	31.7	36.0
Nontax revenue 1/	3.0	3.5	3.6	4.2	4.0	4.7
Expenditure	22.7	26.2	29.8	38.1	47.6	51.2
Current expenditure	17.7	19.2	20.6	24.5	26.5	30.4
Capital expenditure 2/	5.0	7.0	9.2	13.6	21.1	20.8
Overall surplus/deficit (-)	-2.7	-2.2	-0.3	-3.4	-11.9	-10.5
Financing	2.7	2.2	0.3	3.4	11.9	10.5
Foreign borrowing (net)	0.2	1.9	3.2	2.0	5.9	5.3
Gross borrowing	(0.8)	(2.3)	(3.7)	(2.9)	(7.0)	(6.3)
Amortization	(-0.6)	(-0.4)	(-0.5)	(-0.9)	(-1.1)	(-1.0)
Domestic borrowing (net)	2.5	0.3	-2.9	1.4	6.0	5.2
Banking system	(1.2)	(--)	(-0.2)	(1.2)	(5.5)	(4.5)
DBP and LBP 3/	(0.7)	(-1.0)	(-1.0)	(-1.4)	(-2.0)	(...)
Other 4/	(0.6)	(1.3)	(-1.7)	(1.6)	(2.5)	(...)
Memorandum item:						
Overall surplus/deficit (-) as a percentage of GNP	-1.7	-1.2	-0.1	-1.3	-3.9	-3.0

Source: Data provided by the Ministry of Finance and the Central Bank of the Philippines.

1/ Includes minor amounts of grants.
2/ Includes government equity contribution and net lending.
3/ The DBP and the LBP are not part of the consolidated banking system, as presented in the monetary survey.
4/ Includes trust funds.

Bank of the Philippines (LBP) which are not deposit money banks and, therefore, are not part of the banking system as defined in the monetary survey. Treasury cash balances include the balances of various trust funds such as the Depository Fund (Corporations) and the Oil Price Equalization Fund. Changes in the latter balances, which represent government liabilities, are treated as budgetary financing from the domestic nonbank sector and included in the item "Other" in Table 3.

a. Budgetary developments, 1977-80

During the period 1977-80, budgetary policy was mildly expansionary, with the overall deficit averaging slightly more than 7 per cent of expenditure, or 1.1 per cent of GNP (Table 3). Approximately 85 per cent of the cumulative deficit of ₱ 8.6 billion was financed from external sources. Net borrowing from the domestic banking system amounted to ₱ 2.2 billion, or less than 7 per cent of the expansion in total liquidity over the four-year period, while net indebtedness to the domestic nonbank sector declined by ₱ 0.9 billion, reflecting a sharp build-up in government deposits with the DBP and the LBP. These placements were made partially in lieu of equity contributions, and were used to support investment and production of small and medium industries and export-oriented industries, as well as to promote the agrarian reform program in line with the Government's development strategy. 1/

Revenue grew at a compound annual rate of 17.7 per cent, averaging 13.3 per cent of GNP during 1977-80 (Table 4). Tax revenue increased at a faster rate than nontax revenue, and its share in total revenue rose from 85.0 per cent in 1977 to 87.9 per cent in 1980 (Appendix Table VI). Import duties continued to constitute the largest source of revenue (32.3 per cent), followed by taxes on income and profits (25.1 per cent), excise duties (16.1 per cent), and sales and business tax (10.7 per cent). During the period under review, the authorities introduced a number of measures aimed at enhancing the responsiveness of the tax system to domestic activity and reducing the dependence on taxes on international trade. However, among domestic-based taxes, only taxes on income and profits exhibited buoyancy greater than unity, and the share of revenue from domestic-based taxes in total tax revenue declined marginally from 1977 to 1980. While the available information on the impact of discretionary measures on tax revenue does not permit a precise calculation, staff estimates indicate that the built-in elasticity of

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1/ To the extent that government deposits with the DBP and the LBP are made for purposes of economic policy rather than for management of government liquidity or for earning a return, changes in such balances should, according to the GFS Draft Manual (page 130), be treated as government lending (above the line) rather than as negative financing (below the line). The authorities regard these deposits as available for budgetary disbursement, although in practice there is a limit on their availability. About 90 per cent of all deposits at the LBP and about 50 per cent of all deposits at the DBP were from the National Government at the end of 1981.

Table 4. Philippines: National Government Budgetary Revenue and Expenditure--Growth Rates and Ratios to GNP, 1977-82

	1977	1978	1979	1980	1977-80 Average 1/	1981 Latest Est.	1982 Estimate
				(Annual growth rates in per cent)			
Revenue	10.5	20.0	22.9	17.6	17.7	2.9	14.0
Tax revenue	11.1	20.6	26.3	17.8	18.8	3.9	13.6
Nontax revenue	7.1	16.7	2.9	16.7	10.7	-4.8	17.5
Expenditure	12.3	15.4	13.7	27.9	17.0	24.9	7.6
Current expenditure	12.0	8.5	7.3	18.9	11.6	8.2	14.7
Capital expenditure	13.3	40.0	31.4	47.8	31.8	55.1	-1.4
				(Ratios as a percentage of GNP)			
Revenue	13.0	13.5	13.5	13.1	13.3	11.7	11.5
Tax revenue	11.0	11.5	11.9	11.5	11.5	10.4	10.2
Nontax revenue	2.0	2.0	1.6	1.6	1.8	1.3	1.3
Expenditure	14.7	14.7	13.6	14.4	14.3	15.6	14.5
Current expenditure	11.5	10.8	9.4	9.3	10.2	8.7	8.6
Capital expenditure	3.2	3.9	4.2	5.1	4.1	6.9	5.9

Sources: Data provided by the Ministry of Finance; and staff estimate and projection of GNP for 1981 and 1982, respectively.

1/ Average growth rates are compound annual growth rates for 1977-80 and average ratios to GNP are arithmetic averages for 1977-80.

total tax revenue averaged around 0.85 for the period 1977-80, implying that efforts to restructure the tax system and improve its administration met with limited success.

Expenditure (including equity contribution and net lending) increased at a compound annual rate of 17.0 per cent, averaging 14.3 per cent of GNP. However, current expenditure rose at a much slower rate (11.6 per cent) than capital expenditure (31.8 per cent), and the ratio of current expenditure to total expenditure declined sharply from 78.0 per cent in 1977 to 64.3 per cent in 1980 (Appendix Table VII). The relatively slow growth in current expenditure reflected strict expenditure controls, especially on maintenance and subsidy outlays. Among capital expenditure, infrastructure showed the highest growth rate in line with the authorities' decision to step up sharply the infrastructure investment program; its share in total expenditure rose from 10.1 per cent in 1977 to 19.2 per cent in 1980.

b. Budgetary performance in 1981

The budgetary position deteriorated rapidly during 1981, reflecting both the operation of built-in stabilizers on the revenue side and a pronounced expansionary shift in expenditure. The latest estimates, based on outturns for the first 11 months of the year, show an overall deficit of ₱ 11.9 billion (3.9 per cent of GNP), compared with an original estimate of ₱ 4.2 billion (1.3 per cent of GNP).1/ Foreign financing at ₱ 5.9 billion, including ₱ 1.5 billion from the first structural adjustment loan, covered about half the deficit.2/ To meet the financing requirement, the Government relied heavily on the domestic banking system, which provided ₱ 5.5 billion in net credit, or about half of the expansion in total liquidity. The Government continued its policy of building up deposits with the DBP and LBP, with net claims on these institutions increasing by ₱ 2.0 billion and, to a large extent, offsetting the financing obtained from other nonbank sources.

Revenue developments in 1981 were adversely affected by the slowdown in activity in most domestic sectors and sharp declines in import and export growth. Tax revenue rose by only 4 per cent and nontax revenue declined marginally. While problems of tax administration contributed to the weak performance, discretionary measures did not, on balance, lead to a loss of revenue.3/ Receipts from taxes on income and profits increased by 9.5 per cent, compared with an estimated growth rate of 15.8 per cent in nominal GNP.1/ In January 1981, the Government granted a tax relief (increased personal exemption), which meant that revenue of about ₱ 300 million was foregone. However, the loss from this action was more than compensated for by a revenue gain of ₱ 400 million from a tax amnesty in September 1981, providing for payment of taxes on undeclared income

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1/ Estimates of GNP for 1981 are staff estimates.
2/ The onlending of the first structural adjustment loan from the IBRD is budgeted for 1982.
3/ Estimates of the impact of discretionary measures are official estimates.

and/or wealth during 1974-80. The relatively slow growth in taxes on income and profits can in part be attributed to a squeeze in profits, especially of major firms engaged in exports of primary products, and in part to deficiencies in tax collection. Excise duties, which are levied at specific rates, showed the highest rate of growth (12.5 per cent) of any major tax category, mainly due to increases in duties on cigarettes and liquor in September 1980 and again on cigarettes in April 1981, which contributed ₱ 400 million to revenue. Receipts from sales and business tax increased by only 2.8 per cent. This poor performance which occurred despite higher tax rates on forest products that provided ₱ 200 million in revenue, may be attributed to problems with the tax collection mechanism. The decline in import duties (4.5 per cent) occurred as a result of a sharp fall in the growth of imports and reductions in tariff rates in January and August 1981, with a loss in revenue estimated at ₱ 400 million. In addition, about ₱ 500 million in import duties owed by the Philippine National Oil Company was not collected.

Expenditure policies in 1981 were influenced by the disruption of financial markets in the early part of the year and the sluggishness of the economy. While strict economy measures were imposed on current expenditure, the Government stepped up sharply its equity contribution and lending to financially distressed enterprises, and, in an effort to compensate for depressed private investment, accelerated the implementation of the infrastructure program. Total expenditure increased by 24.9 per cent, about 10.5 per cent in real terms. With current expenditure increasing by only 8.2 per cent and capital expenditure by 55.1 per cent, the share of current expenditure in total expenditure declined sharply to 55.7 per cent. Among current expenditure, personal services increased by 7.5 per cent, reflecting a moratorium on recruitment and tight wage restraint. The increase in maintenance and other operating expenditure was limited to 5.3 per cent by postponement of maintenance expenditure, cutbacks in fertilizer subsidy payments, and reductions in aid to local governments. In the capital budget, infrastructural investment expenditure rose by 29.0 per cent, facilitated by the extension of the expiration date for CDC releases on infrastructure projects in 1980 to mid-1981. Other capital outlays increased sharply by 154.5 per cent, mainly on account of disbursements for housing and energy projects as well as for the KKK. Equity contribution to government corporations rose by ₱ 3.3 billion, or 73.6 per cent, of which ₱ 0.5 billion represented a budgetary contribution to the Industrial Rehabilitation Fund. Net lending for servicing of debt of public sector entities and for housing increased by 60.9 per cent.

c. The 1982 budget

The 1982 budget provides for an overall deficit of ₱ 10.5 billion, equivalent to 3.0 per cent of projected GNP, resulting from an estimated growth in revenue of 14.0 per cent and in expenditure of 7.6 per cent. 1/

1/ The budget estimates for 1982 in this report are official estimates as of January 1982, and contain substantial revisions to the cash budget estimates in the 1982 budget documents published in August 1981.

Current expenditure is estimated to increase by 14.7 per cent, while capital expenditure is estimated to be 1.4 per cent lower than in 1981. External financing is projected at ₱ 5.3 billion, consisting of project loans (₱ 3.0 billion), bond issues (₱ 1.7 billion), the second structural adjustment loan (₱ 1.6 billion), and amortization payments (₱ 1.0 billion). Net credit from the domestic banking system is estimated at ₱ 4.5 billion, equivalent to 5.7 per cent of total liquidity at the end of 1981. The authorities plan to make further deposits with the DBP and the LBP, but expect a smaller increase in such deposits than in 1981.

The revenue estimates are based on the following economic assumptions: real GNP growth of 5.1 per cent; an inflation rate of 10 per cent; and nominal import and export growth rates of 7 per cent and 10 per cent, respectively. No discretionary measures have yet been implemented that are expected to provide additional revenue in 1982. Among the major tax categories, revenue from sales and business tax is estimated to show the largest increase (16.6 per cent), followed by taxes on income and profits (14.9 per cent), excise duties (13.7 per cent), and import duties (11.2 per cent). Overall, the revenue estimates for 1982 imply an elasticity of total tax revenue with respect to GNP close to unity, compared with an elasticity of only 0.3 for 1981. While the delayed implementation of tax increases on liquors, scheduled for April 1982, is expected to provide ₱ 90 million in additional revenue, this gain will be offset by an estimated loss in import duties of ₱ 180 million from the reductions in tariff rates in January 1982.

The 1982 budget message contained a number of tax proposals including: the adoption of a "modified gross income taxation scheme;" the imposition of a value-added tax on the second sale of articles; standardization of franchise utility rates; and restrictions on the use of the tax credit method for the calculation of sales tax. Of these measures, which were estimated to generate additional revenue of ₱ 900 million, only the first one has been implemented so far, and it is not expected to have any significant impact on revenue in 1982. The other proposals have been either deferred or shelved, partly because the system of indirect taxation and the schemes of fiscal incentives are currently under review. Under the "modified gross income taxation scheme," employment income will be taxed on a "gross basis," after allowance for personal exemption, while business income/income of professionals will remain taxable on a "net basis," i.e., after legitimate deductions.1/ The new system seeks to simplify tax administration by reducing discretion in the determination and allowance of deductions on the part of the taxpayer/tax examiner, and through wider enforcement of the withholding tax on employment

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1/ Since the rates applicable to employment income were reduced (from a range of 0 per cent to 70 per cent to a range of 0 per cent to 35 per cent), relative to the rates applied to business income/income of professionals, the new system resulted in schedular taxation. The rates imposed on business income/income of professionals were scaled down from 37 brackets ranging from 3 per cent to 70 per cent to 5 brackets ranging from 5 per cent to 60 per cent.

income. The authorities expect that the new system will release manpower resources for concentration on other taxes, especially the corporate income tax, and, over time, will result in a significant improvement in tax administration and revenue collection. The 1982 budget message also announced increases in various administrative fees and charges, estimated to provide additional nontax revenue of P 300 million. However, none of these increases has yet been implemented.

The expenditure estimates will bring the ratio of total expenditure to GNP back to the 1980 level of 14.5 per cent and reverse the downward trend in the share of current expenditure in total expenditure in recent years. With current expenditure budgeted to increase by 14.7 per cent and capital expenditure to decline by 1.4 per cent, the share of current expenditure will increase from 55.7 per cent in 1981 to 59.4 per cent in 1982. However, as a ratio to GNP, current expenditure will decline marginally. The strict control on current expenditure, as evidenced by the steady decline in the ratio to GNP from 10.8 per cent in 1978 to 8.7 per cent in 1981, has resulted in inadequate maintenance of roads and irrigation systems and civil service compensation levels which generate problems in retaining sufficient numbers of capable professional and managerial staff.1/ About one fourth of the budgeted increase in current expenditure represents higher provisions for allotments to local governments and for interest payments. Personal services, maintenance and other operating expenditures are estimated to increase by 14 per cent and 12.5 per cent, respectively. Among capital expenditure, infrastructural investment is estimated to decline by 11.6 per cent, with emphasis being placed on the implementation of ongoing projects, particularly those scheduled for completion in 1982. Other capital outlays, however, are projected to increase by 33.6 per cent, mainly on account of disbursements for housing and local government construction projects. Equity contribution to corporations will be cut back by 10.7 per cent. The bulk of corporate equity investment will finance counterpart fund provisions for foreign-assisted projects implemented by corporations and the budgetary requirements of the 11 major industrial projects. Net lending, on the other hand, is budgeted to more than double, mainly because of the expected onlending from the first structural adjustment loan, and advances to government entities.

2. Local governments

A prominent feature of Philippine local government finance is a relative lack of fiscal autonomy for local government units. Their taxing powers are closely regulated by the National Government, and national government transfers are a key support of local government finance. Because of their greater taxing powers, larger tax base, and greater ease of administration, cities are more fiscally autonomous than provinces and municipalities. During the 1970s, several measures were

1/ In IBRD Report No. 2674-PH, November 12, 1979, it was recommended that the Government aim to stem the relative decline in current expenditure.

taken to expand the financial resources of local governments, mainly by increasing tax receipts from local sources and allotments from the National Government.1/ In addition, subject to certain limitations, local governments were authorized to borrow domestically for the financing of specific projects. Loans from foreign sources, however, have to be negotiated and secured by the National Government, which then may relend the funds to local governments. According to recent instructions for the investment of government funds, local governments are not permitted to lend to any private individual or company; any surplus funds are to be deposited with government financial institutions.

The aggregate size of local government budgets relative to the national government budget is modest; total revenue and expenditure of local governments, in recent years, have averaged about 14 per cent and 12 per cent of national government budgetary revenue and expenditure, respectively. The local governments have received about one third of their total revenue from the National Government, mainly the proceeds from revenue sharing; revenue from local sources consists of real property taxes, business taxes, administrative fees and charges, and property income. Current expenditure has accounted for nearly 90 per cent of total expenditure, mainly on general administration and public welfare.

During 1977-80, budgetary operations of the local governments resulted in a cumulative overall surplus of about ₱ 625 million, most of which was reflected in an increase in net claims on the banking system (Table 5). Revenue grew at a compound annual rate of 17 per cent, representing a fairly consistent 1.8 per cent of GNP. More than half of the increase in revenue was derived from higher receipts from local sources, with property taxes showing the largest increase, while allotments from the National Government accounted for 45 per cent of the increase. Expenditure rose at a compound annual rate of 14 per cent, with its share in GNP declining from 1.8 per cent in 1977 to 1.6 per cent in 1980.

Budgetary operations of the local governments are estimated to have resulted in an overall surplus of ₱ 404 million in 1981, with an increase of ₱ 304 million in net claims on the banking system. Revenue is estimated to have grown by some 13 per cent, and expenditure by about 15 per cent. About 70 per cent of the increase in revenue is estimated to have derived from local sources, and most of the remainder from allotments from the National Government. Budgetary projections for 1982 show a 150 per cent increase in the overall surplus to ₱ 1,015 million, resulting from a 24 per cent rise in revenue and a 13 per cent rise in expenditure. Reflecting a sharp increase in administrative fees and charges, nontax revenue is estimated to grow by 36 per cent, accounting for more than 60 per cent of the projected growth in revenue from local sources.

1/ For a summary review of these measures, see SM/80/183, page 19.

Table 5. Philippines: Local Government Budgetary Operations, 1977-82

(In millions of Philippine pesos)

	1977	1978	1979	1980 Prel. Act.	1981 Estimate	1982 Projection
Revenue and grants	2,989	3,278	3,880	4,729	5,359	6,628
Local source revenue	1,980	2,230	2,406	2,875	3,331	4,117
Property taxes	(586)	(674)	(799)	(915)	(1,098)	(1,281)
Business taxes	(504)	(615)	(738)	(822)	(962)	(1,102)
Nontax revenue	(890)	(941)	(869)	(1,138)	(1,271)	(1,734)
Internal revenue allotments from National Government	771	774	1,186	1,554	1,710	2,175
Special aids from National Government	238	274	288	300	318	336
Expenditure	2,914	3,237	3,781	4,321	4,955	5,613
Current expenditure	2,528	2,847	3,322	3,729	5,326	4,922
Capital expenditure	386	390	449	592	629	691
Overall surplus/deficit (-)	75	41	99	408	404	1,015
Financing	-75	-41	-99	-408	-404	-1,015
External	--	--	--	--	--	--
Domestic	-75	-41	-99	-408	-404	-1,015
Banking system	(-189)	(-63)	(-217)	(-104)	(-304)	(...)
Other	(114)	(22)	(118)	(-304)	(-100)	(...)

Source: Data provided by the Ministry of Finance, and the Central Bank of the Philippines.

3. Social security institutions

The two government social security funds, the GSIS and the SSS, play a significant role in public sector resource mobilization and as financial investors. The GSIS, established in 1936, is for government employees, while the SSS was created in 1954 to provide social security benefits for nongovernment employees. The combined investment portfolio of the GSIS and the SSS at the end of 1980 amounted to ₱ 14.5 billion, or about 20 per cent of total assets of nonbank financial intermediaries.

During the period 1977-80, the cumulative overall surplus of the GSIS and the SSS (after net lending to members) amounted to ₱ 5.3 billion (Table 6). Revenue rose at a compound annual rate of 18 per cent, slightly lower than the growth in GNP. Approximately two thirds of the increase in revenue derived from higher contributions, with most of the remainder coming from increased investment earnings. Benefit payments and net lending to members, mainly housing and educational loans at subsidized rates of interest, averaged 41 per cent and 29 per cent, respectively, of contributions.

The SSS has been investing primarily in public sector securities, especially in PNB/DBP notes and in goverment securities, whose portfolio share at end-1980 amounted to 50 per cent and 25 per cent, respectively.1/ Most of the remaining 25 per cent represented service loans to members. The portfolio of the GSIS shows a similar trend in recent years toward government securities with lower risk and an attractive rate of return.

Operations of the social security funds are estimated to have resulted in a surplus (after net lending to members) of ₱ 2.1 billion in 1981. Revenue grew by 23 per cent, reflecting a sharp increase in investment and other earnings, while expenditure rose by 25 per cent, largely due to higher net lending. Projections for 1982 show a marked slowdown in the growth of both revenue (13 per cent) and expenditure (12 per cent), with a surplus of ₱ 2.3 billion.

4. Government corporations

Investment by government corporations rose from a level less than 3 per cent of GNP in 1978 to an estimated 5 per cent of GNP in 1981 (Table 7). 2/ About 60 per cent of the capital accumulation took place

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1/ The available data from the monetary accounts do not permit a calculation of the net position of the social security funds with the banking system. In particular, deposits by the GSIS and the SSS are lumped together with deposits by other public sector entities, and holdings of PNB notes by social security institutions are not shown separately in the monetary accounts. In the accounts of the social security funds, holdings of PNB notes are grouped together with holdings of DBP securities.

2/ The 12 corporations in Table 7 account for more than 90 per cent of total capital investment by government corporations.

Table 6. Philippines: Operations of Social Security Institutions, 1977-82 1/

(In millions of Philippine pesos)

	1977	1978	1979	1980	1981 Latest est.	1982 Estimates
Revenues	2,405	2,832	3,486	3,946	4,868	5,506
Contributions	1,753	2,058	2,431	2,823	3,358	3,765
Employers	(982)	(1,171)	(1,395)	(1,613)	(1,892)	(2,149)
Employees	(771)	(887)	(1,036)	(1,210)	(1,466)	(1,616)
Investment and other earnings	652	774	1,055	1,123	1,520	1,741
Expenditures	1,323	1,950	1,859	2,244	2,812	3,167
Benefit payments	652	939	998	1,170	1,395	1,541
Other expenditures	172	212	270	328	347	381
Net lending 2/	499	779	591	757	1,070	1,245
Overall surplus/deficit (-)	1,082	882	1,627	1,702	2,056	2,339
Financing	-1,082	-882	-1,627	-1,702	-2,056	-2,339
External	--	--	--	--	--	--
Domestic	-1,082	-882	-1,627	-1,702	-2,056	-2,339
Banking system	(...)	(...)	(...)	(...)	(...)	(...)
Other 3/	(...)	(...)	(...)	(...)	(...)	(...)
Memorandum item:						
Government employer contributions to GSIS	582	687	757	895	1,092	1,281

Sources: Data provided by the Ministry of Finance.
1/ Consists of the SSS and the GSIS.
2/ Consists of net lending to members.
3/ Consists primarily of change in net claims on the National Government and other public sector entities.

Table 7. Philippines: Major Government Corporations--
Level and Financing of Capital Investment, 1978-81 1/

	1978	1979	1980	1981 2/
	(In millions of Philippine pesos)			
Capital investment	4,960	8,759	12,562	15,268
Financed by:				
Internal cash generation	369	495	883	1,453
Government equity contributions	1,616	2,629	4,165	5,867
Borrowings and use of cash balances	2,975	5,635	7,514	7,948
	(In per cent of GNP)			
Capital investment	2.8	4.0	4.7	5.0
Financed by:				
Internal cash generation	0.2	0.2	0.3	0.5
Government equity contributions	0.9	1.2	1.6	1.9
Borrowings and use of cash balances	1.7	2.6	2.8	2.6
	(In per cent of total)			
Capital investment	100	100	100	100
Financed by:				
Internal cash generation	7	6	7	9
Government equity contributions	33	30	33	38
Borrowings and use of cash balances	60	64	60	53

Sources: Data provided by the IBRD, except for data on government equity contributions provided by the Ministry of Finance.

1/ Includes the following 12 major government corporations: Philippine National Oil Company, National Power Corporation, National Electrification Administration, Metropolitan Waterworks and Sewerage System, Local Water Utilities Administration, Philippines Ports Authority, Philippine National Railway, Metro Manila Transit Corporation, National Irrigation Administration, National Housing Authority, National Development Company, and Export Processing Zone Authority.

2/ Estimates.

in the rapidly expanding energy sector, especially the National Power Corporation. While most government corporations have been generating operating surpluses, they have depended heavily on equity contributions from the National Government and on goverment-guaranteed borrowings (mostly foreign) for the financing of their investment projects. Internal cash generation for the 12 major corporations in Table 7 financed only about 8 per cent of the accumulated investment expenditures during 1978-81. During the same period, government equity contributions amounted to ₱ 14.3 billion, or about one third of the financing requirements. At the average interest rate prevailing in 1981 of 15.8 per cent, this would represent an implicit budgetary subsidy of ₱ 2.3 billion in 1982.1/

Tariff rates of most of the major corporations have been adjusted upward in recent years, mainly to take account of cost inflation. In 1981, for example, the rates charged by the National Power Corporation and by the Metropolitan Waterworks and Sewerage Authority were raised by an average of 13 per cent and 23 per cent, respectively. Further increases in water rates are expected by July 1982, while any upward adjustment in power rates will only reflect cost increases.

IV. Monetary Developments and Policies

1. Institutional developments

The Philippine authorities are in the midst of a major reform of the financial sector designed to enhance the efficiency of financial intermediaries and improve the maturity transformation undertaken by the financial system. This reform entails removing certain functional distinctions between commercial banks and specialized financial institutions (e.g., mortgage banks, development banks, and investment houses). Multipurpose financial institutions, or "universal" banks, would be able to take greater advantage of economies of scale in financial intermediation arising from portfolio diversification, information gathering and analysis, and lower transactions costs, while conserving scarce financial management skills and other resources such as computers and trained manpower. In addition, the reduction in legal impediments for financial innovation afforded by the new regulations is expected to improve the financial services offered lenders and borrowers and to foster increased competition among financial institutions. Due to greater deposit stability associated with larger size, multipurpose financial institutions would be able to engage in a higher proportion of medium- and long-term lending without weakening their liquidity position. The objective is for the domestic financial system to become a more significant source of medium- and long-term savings. This reform, which was initiated in mid-1980, is being undertaken in connection with technical assistance from the World Bank and the Fund.

1/ Some of the issues related to the financing of the corporate investment program and the pricing policies of government corporations, especially in the energy sector, are being discussed by the Philippine authorities and the World Bank in the context of SAL II negotiations.

Under the new regulations, universal banks have assumed functions previously limited to nonbank financial institutions such as investment houses, while thrift banks (savings and loan associations, mortgage banks, and private development banks) have been permitted to engage in many commercial bank functions, excluding acceptance of demand deposits and foreign exchange transactions. Rural banks have also been granted broader banking powers.

Universal banks were empowered to make equity investments, subject to certain restrictions, in nonfinancial enterprises. In addition, their required net worth/risk assets ratio was reduced and limitations on loan maturities were lifted to promote increased medium-term lending. While only one bank (the Philippine National Bank) was able to increase its capitalization in 1980 to the minimum of ₱ 500 million required to qualify as a universal bank, five other commercial banks became universal banks in 1981 by merging with their investment house subsidiaries or by merger and acquisition.

2. Monetary developments in 1981 1/

a. Mergers into the banking system

Financial developments in 1981 were dominated by the repercussions of the confidence crisis in the nonbank financial sector. This confidence crisis led to large withdrawals from nonbank financial institutions and subsequent inflow of deposits to the banking system. Furthermore, several nonbank financial institutions in weak condition were merged with stronger institutions in the banking system. These developments resulted in greater increases in domestic assets and liquidity in the monetary survey, which has traditionally been limited to deposit money banks.

The monetary survey for end-1981, both with and without the effects of mergers, is presented in Table 8. The column labeled "excluding mergers" provides the data on an institutional basis consistent with December 1980; however, these data have not been adjusted for the shift of funds into the banking system from nonbank financial institutions stemming from the confidence crisis.2/ As shown in the table, mergers give the appearance that total liquidity growth accelerated in 1981; whereas if the accounts are adjusted for mergers, total liquidity growth decelerated. In particular, total liquidity growth was 21.1 per cent

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1/ The presentation of the monetary accounts used in this and previous reports is under review on the basis of a study (Bureau of Statistics Central Bank Bulletin Project) made in mid-1980 by the Fund. The Philippine authorities are still evaluating the implications of the recommendations contained in that report. Classification changes were recommended for the treatment of foreign liabilities including medium- and long-term foreign liabilities of the Central Bank and those of foreign currency deposit units. (For a description of the foreign currency deposit system, see Annex III.)

2/ Data on funds transferred by individuals and corporations from one part to another of the financial system were not available.

Table 8. Philippines: Monetary Survey, 1980-81

	Dec. 1980	Dec. 1981 Including mergers	Dec. 1981 Excluding mergers
		(In millions of Philippine pesos)	
Net foreign assets	-10,536	-14,876	-14,876
Net domestic assets	78,339	96,967	93,415
Public sector	10,573	16,399	16,152
Private sector	84,696	99,406	94,996
Other items, net	-16,930	-18,838	-17,733
Total liquidity	67,803	82,091	78,[illegible]
		(Percentage change)	
Total liquidity	18.2	21.1	15.8

Source: Data provided by the Central Bank of the Philippines.

using the data including mergers, but only 15.8 per cent based on data excluding the effects of mergers (compared to an expansion of 18.2 per cent in 1980). To avoid analysis based on the pure accounting effects of the mergers, the discussion in this report is based on the monetary survey adjusted to exclude mergers. However, the effects of the shifts in funds from nonbank financial institutions into deposit money banks, and hence into the monetary survey, remain and are discussed below.

b. Liquidity expansion

Notwithstanding the flows into the banking system stemming from the financial crisis and from the effects of higher interest rates on deposits and deposit substitutes, the rate of growth (December-December) of total liquidity decelerated from 18.2 per cent in 1980 to 15.8 per cent in 1981 as nominal GNP growth slowed from 21.1 per cent in 1980 to 15.8 per cent in 1981 (Table 9). These developments contributed to changing the composition of total liquidity. Time and savings deposits, which accounted for 48.5 per cent of total liquidity in 1980, rose to 50.0 per cent in 1981, while the share of deposit substitutes increased from 18.2 per cent of total liquidity in 1980 to 20.3 per cent in 1981. The increase of 28.7 per cent in deposit substitutes in 1981 marked the first time since 1976 that deposit substitutes of the banking system expanded faster than

Table 9. Philippines: Monetary Survey, 1977-81

(In millions of Philippine pesos)

	1977 Dec.	1978 Dec.	1979 Dec.	1980 Dec.	1981 Dec. 1/
Net foreign assets	-1,093	-2,090	-7,164	-10,536	-14,876
Of which: FCDU deposits	(-8,589)	(-13,834)	(-18,505)	(-23,387)	(-25,000)
Net domestic assets	45,024	53,927	64,524	78,339	93,415
Total domestic credit	51,464	63,075	79,551	95,269	111,148
Net credit to public sector 2/	7,241	8,206	8,637	10,573	16,152
Of which: National Government, net	(3,302)	(3,272)	(3,098)	(4,336)	(9,613)
Credit to private sector	44,223	54,869	70,914	84,696	94,996
Of which: FCDU loans 3/	(3,064)	(5,588)	(8,150)	(10,652)	(12,067)
Other items, net	-6,440	-9,148	-15,027	-16,930	-17,733
Total liquidity	43,931	51,837	57,360	67,803	78,539
Of which: public sector deposits 4/	(1,859)	(2,265)	(2,671)	(3,224)	(3,600)
Narrow money	14,938	16,945	18,844	22,537	23,332
Time and savings deposits	17,593	23,398	26,565	32,894	39,284
Deposit substitutes	11,400	11,494	11,951	12,372	15,923
			(Annual percentage changes) 5/		
Net domestic assets	19.5	20.3	20.4	24.1	22.2
Net credit to public sector 2/	2.9	2.2	8.3	3.4	8.2
Credit to private sector	18.0	24.2	31.0	24.0	15.2
Total liquidity	23.4	18.0	10.7	18.2	15.8

Source: Data provided by the Central Bank of the Philippines.

1/ Effects of mergers of nonbank financial institutions into banking system were excluded.

2/ Defined as net credit of National Government plus gross credit extended to selected public sector entities.

3/ Net of consolidated foreign borrowing program.

4/ Excludes National Government deposits.

5/ In relation to liquidity stock at beginning of the period.

the inflation rate. The main factor behind this reversal in the trend for real deposit substitutes was the confidence crisis and accompanying shift of resources. On the other hand, narrow money rose by only 3.5 per cent in 1981, compared with 19.6 per cent in 1980, reflecting the impact of higher real interest rates on time and savings deposits and deposit substitutes. Within narrow money there was a marked movement away from demand deposits as currency in circulation rose by 15.1 per cent, or roughly in line with the growth of nominal GNP, and demand deposits declined by 6.0 per cent. These developments can be attributed to the relatively more limited use of demand deposits to settle transactions, especially in rural areas, which would thus make demand deposits more sensitive than currency holdings to interest rate movements on savings and time deposits and on deposit substitutes.

c. Interest rates and velocity

During 1981, the weighted average interest rate on money market instruments rose to an average level of 15.8 per cent from 13.3 per cent in 1980; nearly all of the increase occurred in the first half of the year (Appendix Table X and Chart 2). This increase primarily reflected higher interest rates in the interbank call market for commercial paper issued by nonfinancial entities, promissory notes, and Central Bank Certificates of Indebtedness (CBCIs); available data suggest that there was also a relative shift toward these instruments. Nevertheless, nominal interest rates in the Philippines remained below foreign interest rates for U.S. dollar deposits during most of 1981 as they had in 1980. The interest rate differential in favor of borrowing domestically would be even greater in 1981 than in 1980 if the effect of the more rapid depreciation of the Philippine peso against the U.S. dollar in 1981 were incorporated. With the upward movement in market interest rates and the lower inflation rate, real interest rates in 1981 moved to positive 3 to 4 per cent in 1981 from negative 3 to 4 per cent in 1980 (Chart 3). This marked a return to positive market interest rates that had prevailed during the period 1975-77.

In August 1980, the ceiling on interest rates for time deposits with an original maturity over two years was eliminated, while the ceilings on deposits of lesser maturities were raised to a uniform 14 per cent from a range of 10.5 to 14 per cent, and the interest rate ceiling on savings deposits was raised to 9 per cent. Moreover, in mid-1981, the ceiling on deposits with a maturity of two years or less was abolished. As a result, the modal interest rate on large savings deposits rose one percentage point above the previous ceiling to 10 per cent, although the range of interest rates offered extended to 14 per cent. Modal interest rates on large time deposits also remained close to the previous ceiling but the range of interest rates increased to 18 per cent at the upper end for 360-day deposits. The impact of lifting the ceilings on these deposit rates was weakened by efforts by the Bankers' Association to hold these rates at the prevailing 9 per cent level, perhaps because of reluctance on their part to compete for deposits in the face of the continuing interest rate ceiling on loans of one year or less.

Income velocity of total liquidity (based on the average liquidity level during the year) in 1981 declined by 3.2 per cent after an increase of 7.3 per cent in 1980 and 8.2 per cent in 1979 (Table 10 and Chart 4). The reduction in income velocity was confined to interest earning accounts; the income velocity of time and savings deposits and deposit substitutes declined by 6.4 per cent in 1981, compared with an increase of 8.8 per cent in 1979 and 7.2 per cent in 1980, while the income velocity for narrow money, continued its upward trend, rising by 4.1 per cent. The reversal in income velocity for interest earning accounts was associated with the upward movement in real interest rates that occurred in 1981, stemming from both the lower inflation rate and higher nominal interest rates, as well as higher deposit inflows due to the shift of funds from the nonbank financial sector.

Philippines: Table 10. Velocity Developments, 1978-81

	1978	1979	1980	1981 1/
	(Percentage change)			
Narrow money	-0.8	9.5	6.1	4.1
Currency in circulation	-2.9	5.9	8.4	3.4
Demand deposits	0.7	12.7	4.2	5.2
Interest earning accounts 2/	-3.6	7.2	8.8	-6.4
Liquidity	-2.8	8.2	7.8	-3.2

Sources: Philippine Financial Statistics; data provided by the Central Bank of the Philippines; and staff calculations.

1/ Based on staff estimates of nominal GNP.
2/ Time and savings deposits and deposit substitutes.

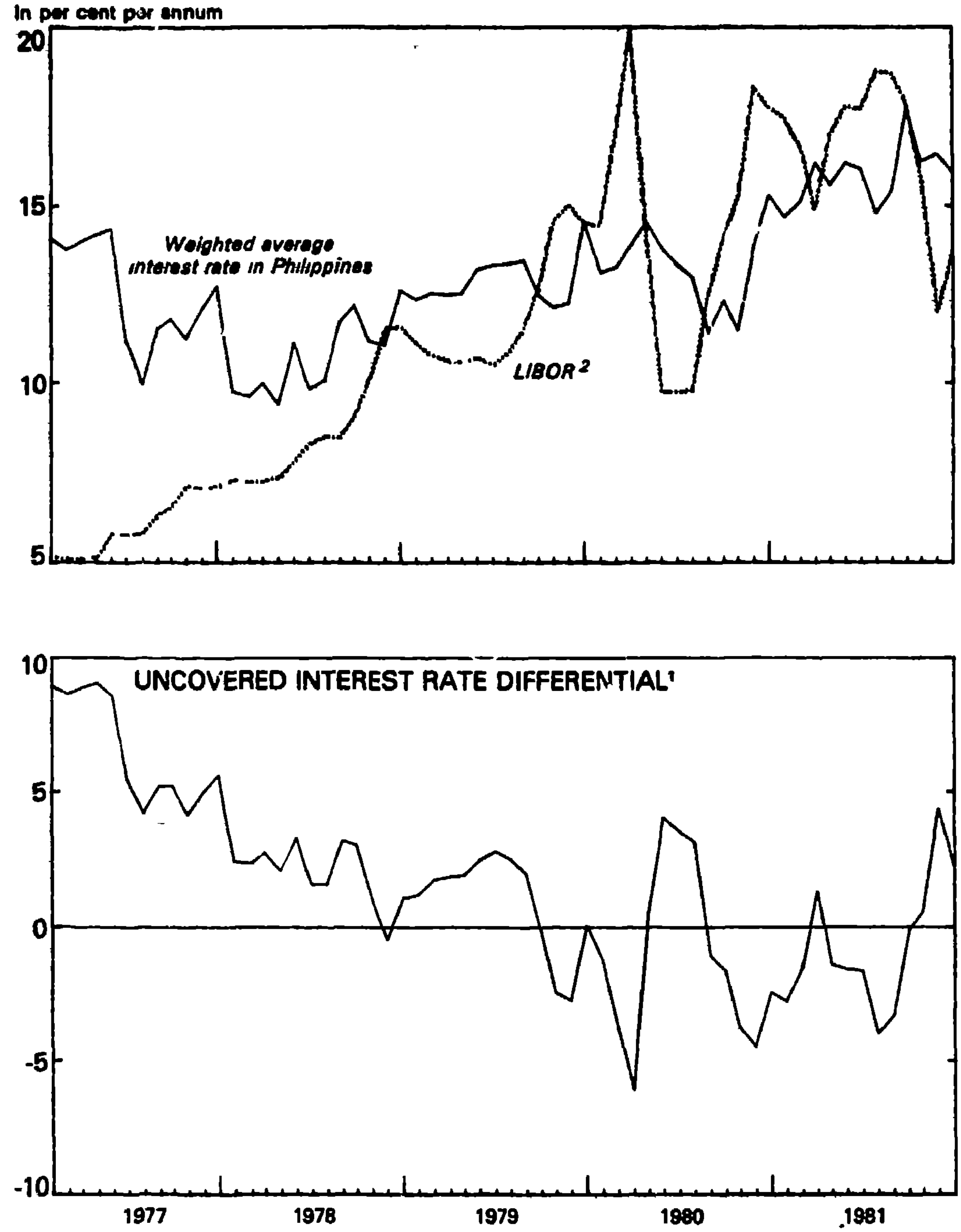
d. Sources of liquidity expansion

In 1981 as in 1980, about 60 per cent of the expansion in total liquidity was due to the growth of reserve money. The year-end increase in reserve money for 1981 at 9.2 per cent was below the 10.7 per cent expansion recorded in 1980. The major factors affecting reserve money developments were Central Bank advances to financial institutions mainly for the rescue operation, the net credit needs of the National Government

CHART 2

PHILIPPINES

DOMESTIC AND FOREIGN INTEREST RATES, 1977-81[1]

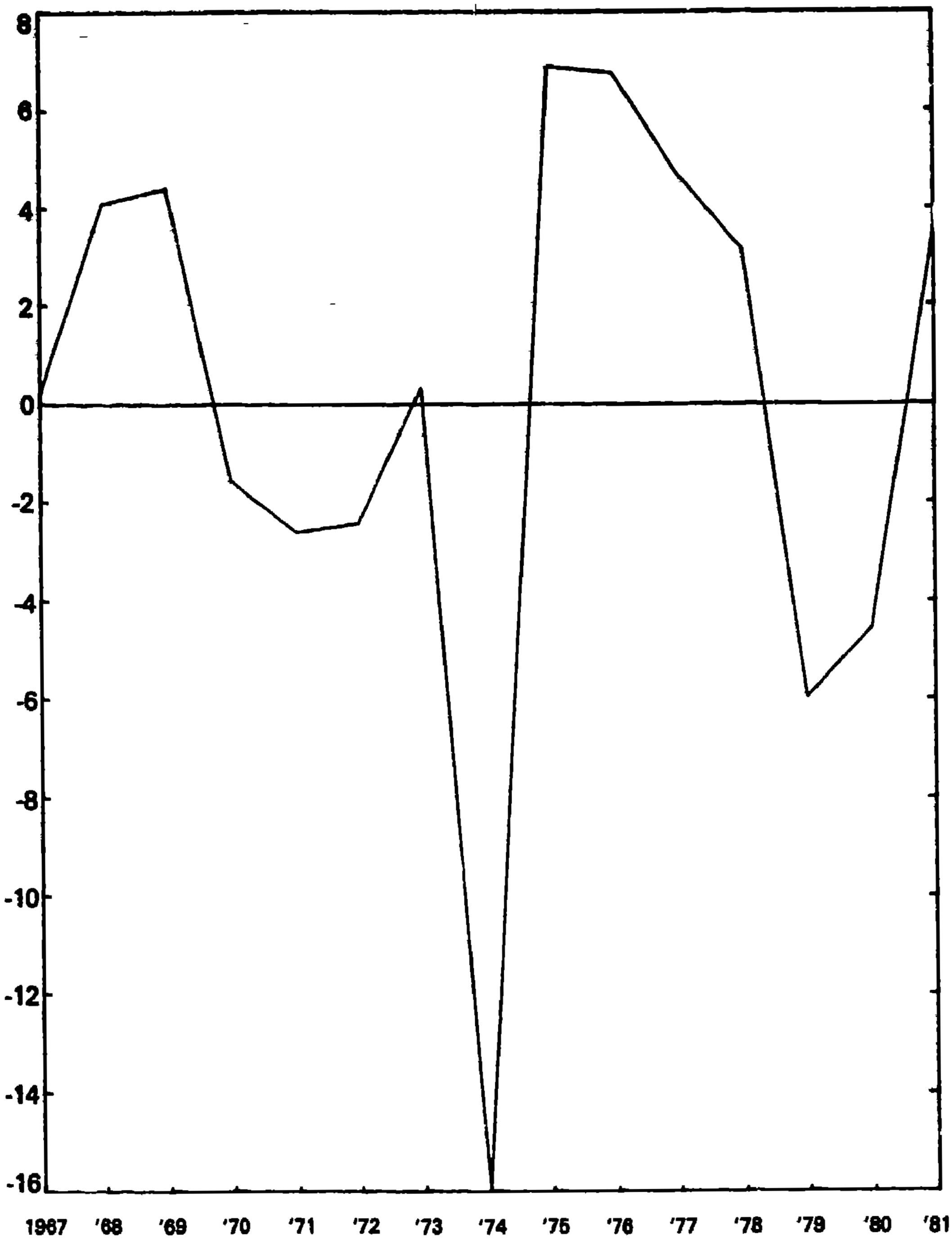


Sources: Data provided by the Central Bank of the Philippines and IMF, *International Financial Statistics.*
[1]In favor of borrowing externally
[2]Three-month deposit rate for U S dollars.

CHART 3

PHILIPPINES

REAL INTEREST RATE, 1967-81[1]

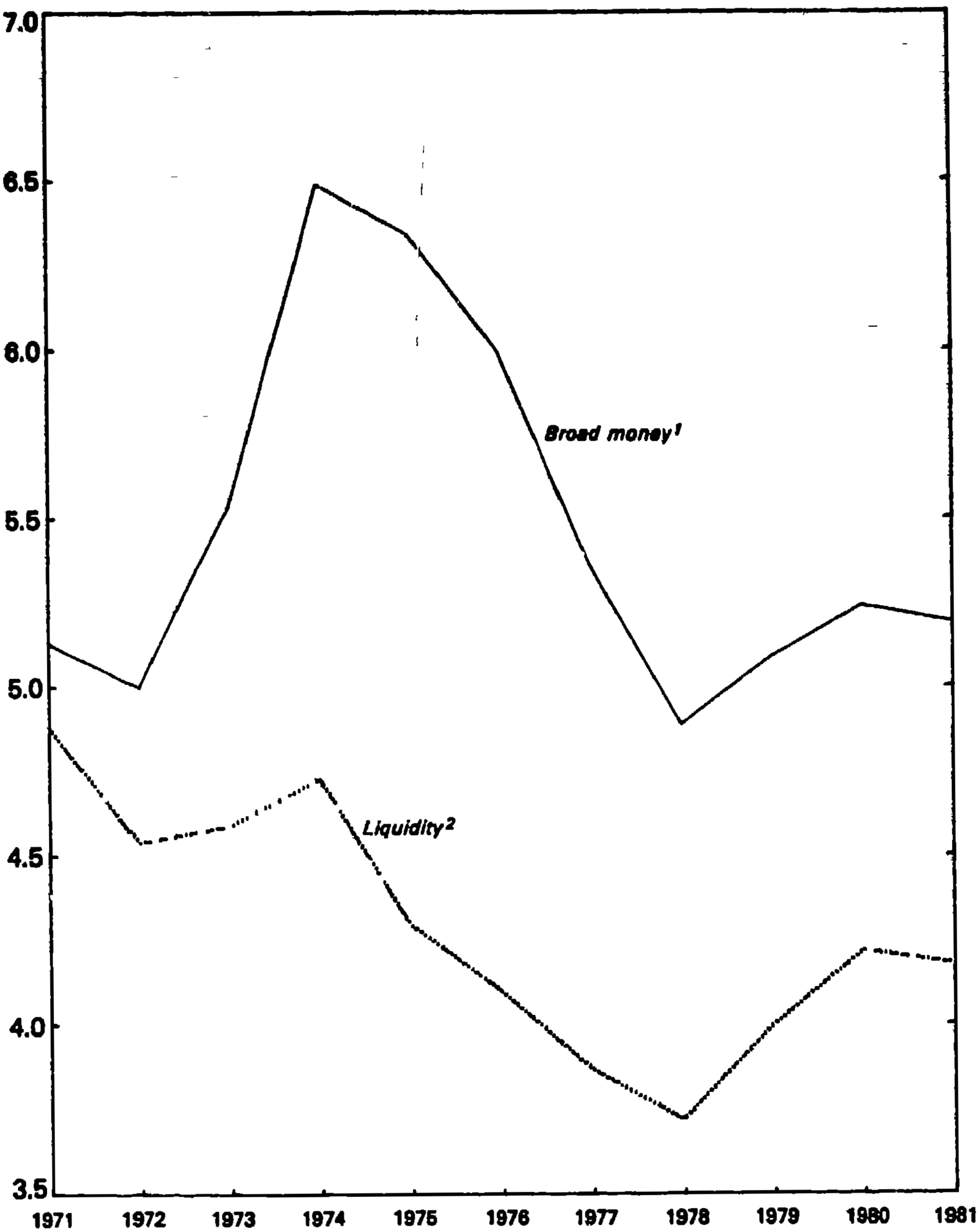


Sources: Data provided by the Central Bank of the Philippines and staff estimates.
[1]Weighted average interest rate less inflation rate, as measured by the consumer price index

CHART 4

PHILIPPINES

VELOCITY OF BROAD MONEY[1] AND LIQUIDITY,[2] 1971-81



Sources. Data provided by the Central Bank of the Philippines, and staff estimates.
[1]Includes money and quasi money
[2]Includes money, quasi money, and deposit substitutes.

funded by the Central Bank and the sharp deterioration in the net foreign asset position of the Central Bank. On the expansionary side, the credit needs of the National Government and the financial sector rescue operation were equally important in absolute terms. Net claims on the National Government by the Central Bank rose by ₱ 4,238 million, or nearly 92 per cent (compared with ₱ 605 million in 1980, or an increase of 15 per cent), as recourse to the Central Bank in 1981 accounted for over three quarters of the increase in the banking system's net claims on the National Government (Appendix Table XI). Central Bank claims on the financial sector (commercial banks and other financial institutions) rose by ₱ 4,316 million in 1981, or by 28.6 per cent (compared with ₱ 4,192 million in 1980, or an increase of 38.6 per cent). The expansionary impact of these two items--totalling ₱ 8,554 million--on reserve money was partially offset by the contractionary influence of a decline in net foreign assets of ₱ 5,719 million.

The growth in Central Bank claims on the financial sector primarily reflected emergency advances extended to alleviate the liquidity effects on certain financial institutions confronted with large withdrawals of deposits during the confidence crisis. Over three quarters of the expansion in claims on the financial sector arose due to emergency advances (Appendix Table XI). As a consequence of these emergency operations, the traditional allocative priorities underlying rediscounting and repurchase policies were less strictly adhered to in 1981. By end 1981, loans extended to commercial banks by the Central Bank, other than for emergency credits, were virtually unchanged from their December 1980 level. This contrasts sharply with the 67 per cent increase in rediscounts and repurchases that occurred in 1980. With the curtailment of rediscounts, other than for emergency or special credits, the proportion of outstanding rediscounts allocated to exports declined from 70 per cent in 1980 to 51 per cent in 1981, while the agricultural share was reduced from 17 per cent in 1980 to 13 per cent in 1981.

During 1981, the liquidity multiplier experienced different seasonality which complicated the conduct of monetary policy (Appendix Table XII). In the first quarter of 1981, the liquidity multiplier recorded an unusually large increase stemming primarily from the reserve deposits ratio which had its greatest first quarter decline in four years; the movement in the currency-deposits ratio followed past seasonal patterns. The sharp decline in the reserves deposits ratio was associated with the banking system's working-off an exceptionally high level of excess reserves--8.3 per cent--at end-1980 (Appendix Table XIII). By the middle of 1981, the liquidity multiplier had returned to historical levels. However, at end-1981, the liquidity multiplier did not experience a seasonal decline of the same magnitude as in the prior two years but declined by 10 per cent rather than by the average reduction of 15 per cent experienced during 1979-80. This milder seasonal pattern derived from the reserve deposits ratio and not from the currency deposits ratio. At end-1981, the reserve deposits ratio fell by 13 per cent rather than rising by 7 per cent as it had on average during 1979-80. The sharp departure from past seasonal patterns was caused by a reserve deficiency of commercial banks equivalent to 5 per cent of required reserves at end-1981. On January 1, 1982, the preannounced reduction in reserve requirements from 20 per cent to 19 per cent occurred--a 5 per cent lowering in the level of required reserves (Appendix Table XIV). Thus, it appears that the banking system may have anticipated the change in the reserve requirement ratio. In any case, the 6.0 per cent increase in the liquidity multiplier from December 1980 to December 1981 was a major factor in explaining the 15.8 per cent growth in liquidity over that period.

e. Monetary aggregates

The expansion of net domestic assets of the banking system outpaced the growth in total liquidity in 1981 as it had in the previous three years. Net domestic assets increased by 22.2 per cent, in relation to the liquidity stock at the beginning of the period, while liquidity growth was 15.8 per cent. Thus, the rate of increase in net domestic assets exceeded that of total liquidity by 6.4 percentage points in 1981, or by slightly more than the 5.9 percentage point difference experienced in 1980. Corresponding to these developments was a greater deterioration in the net foreign asset position of the banking system in 1981. Net foreign assets were ₱ 4,340 million lower at end-1981, at minus ₱ 14,876 million, than at the outset of the year and compared with a deterioration of ₱ 3,372 million in 1980. The decline in net foreign assets in 1981 amounted to over a quarter of the increase in net domestic assets.

With the sharp widening of the fiscal deficit in 1981, National Government recourse to the banking system greatly expanded--rising by 326 per cent--to ₱ 5,277 million from ₱ 1,238 million in 1980 and compared with declines recorded in 1979 and 1978. The net credit requirements of the National Government from the banking system almost totally explain the increase in net credit to the public sector of 53 per cent from ₱ 10,573 at end-1980 to ₱ 16,152 million at end-1981. About 20 per cent of the increase in net credit to the public sector in 1981 was extended by commercial banks compared with approximately half in 1980.

In contrast to the period 1978-80, expansion in credit to the private sector in relation to the end-1980 liquidity stock, did not outstrip the growth in total liquidity. Moreover, the growth rate for credit to the private sector decelerated further in 1981 to 12.2 per cent from 19.4 per cent in 1980 and from 29.2 per cent in 1979. The sluggish economic growth experienced in 1981 was a major factor accounting for the slower growth in credit to the private sector; although higher interest rates on bank loans may also have contributed. Furthermore, commercial banks, which were inundated with deposits from nonbank financial institutions, used their increased liquidity to improve their net foreign assets position rather than extend credit to enterprises experiencing financial distress or to the public sector. Net foreign assets of commercial banks rose from minus ₱ 13,925 million at end-1980 to minus ₱ 12,546 million at end-1981.

The outstanding stock of commercial bank credit to all sectors rose by 8.5 per cent in 1981--a 3.9 per cent real decline. In absolute terms, the greatest increase, as has typically been the case, was recorded by the manufacturing sector. Credit to the manufacturing sector rose by 13 per cent and represented 54 per cent of the total increase, or about the same proportion as in 1980; however, this was a major change from the period 1977-79 when only about a third of the increase in credit went to the manufacturing sector. The manufacturing sector had the largest share of outstanding bank credit accounting for nearly 36.5 per cent (Appendix Table XV).

f. Nonbank financial institutions

Financial institutions other than commercial banks (reflecting mainly the operations of the rural banks) traditionally have been the major source of lending to the agricultural sector but since end-1980, the banking system has loaned more than these other financial institutions (Appendix Tables XV and XVI). The relative rise in commercial bank lending to the agricultural sector is partially explained by the regulation requiring banking institutions to extend at least 25 per cent of their loanable funds in the form of agricultural credit.1/ Under certain conditions, the allocation target is satisfied by deposits with the Philippine National Bank and the Development Bank of the Philippines, purchases of "loan participation cer ificates" from other banks that have exceeded the target, and purchases of government securities, including CBCIs, whose proceeds are earmarked for agricultural credit. These exemptions are the principal reason that the allocative target has not been achieved; for example, during 1980-81, only 15 per cent of lending by commercial banks was to the agricultural sector. Nonbank financial institutions have retained their relatively greater orientation to the agricultural market as reflected in the higher proportion of agricultural credits in total nonbank lending than in total commercial bank lending.

Complete data on developments among nonbank financial institutions for 1981 were not available. Data through June 1981 indicate that for the consolidated nonbank financial system liabilities rose by 18.6 per cent, or about 5 percentage points less than the growth in liabilities of the banking system during the same period, whereas for the whole of 1980, the growth of nonbank financial liabilities was 21.3 per cent, or over 3 percentage points higher than the expansion in total liquidity of the banking system. This sharp change in the relative growth of bank and nonbank financial institutions in 1981 was attributable to the slower expansion of private nonbank financial institutions, which grew by only 7.7 per cent from June 1980 to June 1981, as compared with a 26.8 per cent increase in 1980 (December-December). Private nonbank financial institutions were the segment of the financial system most severely affected by the confidence crisis. Approximately ₱ 2.1 billion in deposit substitutes was withdrawn from December 1980 to June 1981--a 19.2 per cent decline (Appendix Table XVII). This outflow was a major

1/ This agricultural credit allocation requirement was promulgated in CBC No. 408 dated May 31, 1974.

factor in the increase in deposit substitutes of ₱ 2.8 billion recorded by the banking system during the same period which was in sharp contrast to the decline in deposit substitutes of the banking system of ₱ 1.5 billion that occurred during the same period a year earlier. Central Bank intervention in the form of emergency advances of ₱ 1.7 billion helped avert insolvency for private nonbank financial institutions by largely replacing the withdrawn deposit substitutes.

3. Monetary policies

In 1981, monetary policy was affected by the need to contain the effects of the confidence crisis and finance the deficit of the National Government. Nevertheless, the monetary authorities continued reforms by liberalizing interest rate ceilings, revamping rediscount policy, and undertaking measures to enhance the effectiveness of monetary policy.

In the face of massive shifts of funds from quasi-banks to commercial banks the Central Bank, in coordination with the Government, embarked on a major rescue operation. Initially, the Central Bank provided ₱ 1.6 billion directly to affected nonbank financial institutions through a special rediscounting facility that carried a penalty interest rate of 24 per cent for the first 60 days and increased by 2 per cent for each rollover of the outstanding advance. These advances were to be repaid from loans drawn against the newly created Industrial Rehabilitation Fund, which was capitalized at ₱ 1.5 billion with ₱ 1.0 billion subscribed by the Central Bank and ₱ 0.5 billion by the Government. The Fund was to provide medium-term loans or acquire equity in viable enterprises which were heavily indebted to nonbank financial institutions. These funds were intended then to reflow to nonbank financial institutions and in turn to be used to retire Central Bank advances. However, by end-1981, releases against the Industrial Rehabilitation Fund totalled only ₱ 450 million--substantially below the target of ₱ 1.5 billion--while Central Bank emergency advances had risen to ₱ 2.7 billion instead of having been eliminated as originally intended. The greater-than-envisaged increase in Central Bank advances was in response to continuing deposit withdrawals from nonbank financial institutions, but also from the need to strengthen the balance sheets of certain nonbank financial institutions in order to encourage mergers with stronger banks as well as enable them to continue providing credit to their industrial customers. During the second half of 1981, it was found that many off-balance sheet obligations (notes without recourse issued by nonbanks) had to be honored by the Central Bank to prevent a further loss of confidence in financial institutions and shore up the financial position of these entities. In addition to the Industrial Rehabilitation Fund, a further ₱ 680 million in credits for restructuring firms was granted by the Central Bank to the Development Bank of the Philippines and the Land Bank of the Philippines.

In early 1982, the Industrial Rehabilitation Fund and the rediscount window for the stock market were abolished and replaced by a new rediscount window for medium- and long-term loans and equity investments made by authorized universal banks. Universal banks can apply to rediscount up to 75 per cent of a loan with the maturity of the rediscount dependent on the nature of the project the loan is supporting. Under this facility, the Central Bank advances funds at an interest rate of 11 per cent for relending by universal banks at an interest rate of up to 16 per cent. The resources released by the elimination of the Industrial Rehabilitation Fund have been earmarked for this rediscount window.

A recurrence of the overissuance of commercial paper by financial and nonfinancial entities--a factor in the confidence crisis--is to be prevented by controlling the volume and quality of such instruments. The Securities and Exchange Commission will register all commercial paper, which will be printed at the Central Bank on serially numbered paper. A credit information system will improve the quality of information available on borrowers. Furthermore, the commercial paper market will be limited to debts of prime companies by a credit evaluation mechanism that requires a bank credit line to cover a portion of the total money market issue.

In the latter part of 1981, the penalty rate on Central Bank emergency advances was eliminated and a 12 per cent interest rate imposed. In early 1982, this rate was raised to 16 per cent or the average interbank call loan rate plus three percentage points, whichever is higher. These higher interest rates were intended to encourage borrowers to turn to other sources of financing, including the newly established medium- and long-term rediscount facility.

The removal of the ceiling on interest rates for deposits of two years or less, on July 1, 1981, eliminated the last deposit interest rate ceiling; the only remaining ceiling is on loans of one year or less (Table 11). The ceiling on secured loans is set at 16 per cent, while the maximum lending rate for unsecured loans is 18 per cent. Rediscount interest rates were raised in 1981, except for nontraditional export industries (Appendix Table XVIII). As a result, the average interest rate on outstanding rediscounts rose from 5.6 per cent in the fourth quarter of 1980 to 7.8 per cent in the fourth quarter of 1981.

During 1981, two new facilities were established which increased the Central Bank's influence over short-term interest rates. An overnight rediscount window was opened to enable commercial banks to cover their reserve deficiencies and permit the Central Bank to dampen interest rate movements in the interbank call market. At end-1981, ₱ 137 million had been rediscounted through this facility (Appendix Table XIX). Periodic pressure on short-term interest rates has also stemmed from withdrawal of peso funds from the money market by oil companies in order to make foreign exchange purchases to cover oil import payments. These payments were large relative to the domestic market and commercial banks did not have sufficient domestic assets eligible for rediscounting to satisfy the peso requirements of oil companies. Therefore, foreign exchange swaps of two-week duration were permitted to increase the peso resources of commercial banks. This facility would, thereby, reduce the abrupt withdrawal of peso funds from the money market by the oil companies and smooth

Table 11. Philippines: Interest Rate Ceilings, 1978-81

(In per cent per annum)

Instrument	Maturity (days)	Ceiling			
		12/1/78	12/1/79	12/1/80	12/1/81
Savings deposits 1/		7.0	9.0	9.0	No ceiling
Time deposits 1/	90-179	8.5	10.5	14.0	No ceiling
	180-359	9.0	11.0	14.0	No ceiling
	360-539	10.0	12.0	14.0	No ceiling
	540-730	11.0	13.0	14.0	No ceiling
	Over 730	12.0	14.0	No ceiling	No ceiling
Deposit substitutes	365 or less	15.0	17.0	17.0	18.0
	Over 365	15.0	17.0	17.0	No ceiling
	730 or less	15.0	17.0	17.0	n.a.
	Over 730	No ceiling	No ceiling	No ceiling	n.a.
Lending rates					
Secured loans 2/	730 or less	12.0	14.0	14.0	16.0 3/
Unsecured loans 2/	730 or less	14.0	16.0	16.0	18.0 3/
Secured loans 4/	Over 730	19.0	21.0	21.0	No ceiling
Unsecured loans 4/	Over 730	19.0	21.0	21.0	No ceiling

Source: Data supplied by the Central Bank of the Philippines.

1/ For deposit money banks. The ceilings for institutions not authorized to accept demand deposits have been set 0.5 percentage point higher.
2/ Excludes commissions, premiums, fees, and other charges which are not allowed to exceed 2 percentage points for deposit money banks and 3 percentage points for other financial institutions.
3/ Applies only to maturities of 365 days or less; otherwise, no ceiling.
4/ Includes commissions, premiums, fees, and other charges.

out short-term interest rate movements.1/ Notwithstanding this new foreign currency/peso swap arrangement, the outstanding level of swaps at end-1981 was virtually unchanged from the end-1980 level.

In past years, open market operations with CBCIs was a major instrument of credit control. However, during 1981, the authorities decided to restore primacy in open market operations to Treasury instruments and enlarge the capacity of the financial market to finance the fiscal deficit through Treasury debt instruments. To support this effort, a new system of marketing government securities was instituted in 1981 which gave underwriting responsibilities to accredited dealers. As part of this change, maturing CBCIs of ₱ 1.4 billion were replaced by new issuance of Treasury instruments. However, technical problems during the initial stages limited the issuance of Treasury instruments to ₱ 1.0 billion. The Government proceeds from these debt instruments were not used to finance the fiscal deficit in 1981 but were sterilized in the Central Bank to offset the expansionary effects on reserve money of reducing CBCIs.

V. External Sector

1. Summary of recent balance of payments trends

The current account deficit of the balance of payments continued to widen in 1981 both in absolute terms and relative to GNP, as has occurred in every year since 1977. In dollar terms, the 1981 current account deficit reached $2.4 billion or 6.2 per cent of GNP, compared to a 1980 deficit of $2.1 billion or 5.8 per cent of GNP (Table 12). The increase in the 1981 current account deficit was the result of an increase in the trade deficit to $2.5 billion, compared to $1.9 billion in 1980. The terms of trade continued to deteriorate in 1981, declining by 12 per cent, following a 17 per cent decline in 1980. The deterioration in the trade balance in 1981 occurred despite a sharp slowdown in the growth of merchandise imports to less than 9 per cent (Table 13), compared to an increase of nearly 26 per cent in 1980, as exports grew by only 2 per cent in value terms after a 26 per cent increase in 1980. At the same time, the deficit on services account narrowed to $0.4 billion in 1981, compared to a $0.5 billion deficit in 1980, and the net inflow of transfers increased from $0.4 billion in 1980 to $0.5 billion in 1981.

The inflow of nonmonetary capital also increased during 1981, reaching $1.9 billion, compared to inflows of $1.7 billion in 1980 and $1.0 billion in 1979. Despite this increase, a drawdown of net

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1/ Under this facility, commercial banks swap foreign exchange to obtain pesos which are lent to oil companies. These companies, in turn, purchase foreign exchange from commercial banks with these pesos, which are then used to unwind the earlier swap operation. Thus, commercial banks can meet the peso needs of the oil companies for a two-week period and reduce the oil companies' heavy reliance on withdrawals from the money market.

Table 12. Philippines: Summary Balance of Payments, 1977-81

	1977	1978	1979	1980	Prel. 1981
			(In millions of U.S. dollars)		
Goods, services, and transfers	-827	-1,172	-1,576	-2,051	-2,412
Trade balance	-764	-1,307	-1,541	-1,939	-2,490
Exports, f.o.b.	3,151	3,425	4,601	5,788	5,910
Imports, f.o.b.	-3,915	-4,732	-6,142	-7,727	-8,400
Of which: Petroleum	(-984)	(-1,015)	(-1,371)	(-2,226)	(-2,713)
Services and transfers	-63	135	-35	-112	78
Investment income (net)	-321	-406	-527	-732	-958
Other services (net)	73	228	137	186	566
Transfers (net)	260	313	355	434	470
Capital movements 1/	962	1,082	997	1,699	1,926
Long-term capital (net)	878	967	1,121	1,096	1,592
Direct investment (net)	216	171	99	45	392
Borrowing	662	796	1,022	1,051	1,200
Short-term capital, and errors and omissions 2/	84	83	-165	475	-66
Monetization of gold	—	32	41	128	400
Changes in net international reserves of banking system	135	-90	-579	-352	-486
		(In millions of U.S. dollars; end of period)			
Memorandum items:					
Gross official reserves	1,525	1,883	2,423	3,155	2,707
Total external debt	5,004	6,200	7,137	8,554	10,054
Public external debt	3,389	4,109	5,066	6,099	7,073
			(In per cent of GNP)		
Current account deficit	4.0	4.8	5.3	5.8	6.2
Merchandise exports	15.1	14.2	15.5	16.3	15.3
Petroleum imports	4.7	4.2	4.6	6.3	7.0
Nonpetroleum imports	14.1	15.4	16.1	15.5	14.7
Debt service	2.5	3.0	3.5	3.0	4.0
Interest	(0.9)	(1.1)	(1.6)	(1.7)	(2.2)
Amortization	(1.6)	(1.9)	(1.8)	(1.3)	(1.8)

Source: Data provided by the Central Bank of the Philippines.

1/ Includes errors and omissions, SDR allocations, and valuation adjustment, here included together with short-term capital; also includes monetization of gold.
2/ Includes errors and omissions, SDR allocations, and valuation adjustments.

Table 13. Philippines: Increases in Exports by Category, 1971-81

(In millions of U.S. dollars)

	Compound Annual Growth Rate	Percentage change over preceding year			Preliminary
	1971-81	1979	1980	1981	1981
Principal primary exports	10.2	29.0	14.8	-8.2	2,318
Coconut products	12.5	13.1	-20.3	-1.5	808
Sugar products	9.9	11.1	175.0	-8.5	603
Forestry products	6.7	49.4	2.0	-8.6	457
Copper concentrate	11.4	76.0	23.9	-17.4	450
Nontraditional exports	36.1	41.4	29.0	14.2	2,510
Manufactured	35.6	41.8	31.7	18.3	2,272
Primary 1/	42.3	39.0	13.0	-14.4	238
Other 2/	18.9	35.3	52.6	1.6	1,082
Total	17.5	34.3	25.8	2.1	5,910

Source: Data provided by the Central Bank of the Philippines.

1/ Mainly comprises coffee, rice, and iron ore agglomerates.

2/ Mainly comprises fruits and vegetables, gold, nickel, marine products, unmanufactured tobacco, petroleum products, and abaca fibers.

international reserves of $0.5 billion was required to finance the larger 1981 current account deficit. Therefore, the cumulative loss in net reserves since 1977 reached $1.5 billion.1/ At end-1981, gross official reserves stood at $2.7 billion, or slightly more than four months of imports in 1981.

2. Current account

a. Exports

Export earnings increased by only 2.1 per cent in 1981, compared with 25.8 per cent in 1980 and 34.3 per cent in 1979 (Table 13). Not only did the 1981 outturn represent sharply slower growth compared with recent years, but it was also far below the 17.5 per cent compound annual growth rate of the previous decade. The weak export performance in 1981 was partially a reflection of the sluggishness of external demand. Unit value of exports declined by 1 per cent in 1981, and volume increased by 3 per cent (Appendix Table XX). Sluggishness was especially notable in the four principal primary exports: coconut products, sugar, forestry products, and copper concentrate. The total value of these four exports declined by more than 2 per cent in 1981, with unit values declining by more than 6 per cent and export volume increasing by nearly 4 per cent; nevertheless, they still accounted for nearly 40 per cent of total exports. Other traditional exports, which comprised more than 18 per cent of exports in 1981, grew by less than 2 per cent. Nontraditional exports increased by 14 per cent in 1981, compared with 29 per cent in 1980 and 41 per cent in 1979.

In the case of coconut products, the Philippines is both the largest producer and exporter. Although prices for copra and coconut oil tend to move broadly in line with world market prices for other vegetable oils, during the past two years the world market price for coconut products has been far weaker than for other oils and oilseeds. In 1981 alone, while international prices for other vegetable oils increased by about 5 per cent, preliminary information indicates that the unit value of exports of coconut products fell by nearly 12 per cent, and the total value of the Philippines exports of these products fell by more than i per cent compared with the 1980 level. Apparently these changes result both from increased production and from changes in the structure of demand, as the price premium of coconut oil over soy oil has disappeared in world markets.

Exports of forest products and copper concentrates also suffered from weak external demand in 1981, with prices falling in world markets.

1/ As was noted in Section IV above, the Philippine authorities classify FCDU deposits as international reserve liabilities. Therefore, increases in FCDU deposits cause an increase in reserve liabilities of the banking system. If changes in these deposits were to be classified as short-term capital flows, capital movements as shown in Table XXV would be increased, and the changes in net reserves of the banking system would also be increased by a corresponding amount.

However, in the case of copper, a price decline of 13 per cent was exacerbated by more than 4 per cent decline in export volume; the total value of exports of copper concentrates fell by more than 17 per cent from the 1980 level. In the case of sugar, preliminary information indicates that the decline in export value of more than 8 per cent experienced in 1981 was a result of lower export volume, as NASUTRA (the State sugar marketing agency) temporarily suspended exports in 1981 to increase supplies to the domestic market.

Nontraditional exports have been the most dynamic element of Philippine export performance over the past decade, growing at a 36 per cent compound annual growth rate. A slowdown in growth of nontraditional primary exports (mainly coffee, rice, and iron ore agglomerates) began in 1980, with growth of these exports decelerating to 13 per cent, after a 39 per cent increase in 1979. In 1981, nontraditional primary exports declined by 14 per cent. Nontraditional manufactured exports increased by more than 18 per cent in 1981, yet this represented a substantial slowdown from previous years. Exports of garments and electrical and electronic equipment account for more than 60 per cent of nontraditional manufactured exports, but these exports grew by only 8 per cent in 1981, after a 43 per cent increase in 1980, mainly because of weaker external demand.

Exports of primary products have become relatively less important in recent years. In 1977 these exports accounted for 58 per cent of total exports, but by 1981, their share had declined to 39 per cent (Appendix Table XXI). The relative decline was sharpest in the case of coconut products, as these exports, which alone accounted for more than 24 per cent of total exports in 1977 represented less than 14 per cent of the total by 1981. At the same time, nontraditional exports have grown in relative importance; nontraditional manufactured exports accounted for less than 21 per cent of total exports in 1977, but for more than 38 per cent by 1981. During this period, these exports have enjoyed a broad range of subsidies and incentives, including credit subsidies, tax, and other fiscal incentives, as well as tariff preferences.

b. Imports

Preliminary information indicates that about two thirds of the nearly 9 per cent increase in import value experienced during 1981 was due to higher unit values, as import volume grew by only 3 per cent (Appendix Table XXII). The slowing of import growth in 1981 was not spread uniformly over all import categories (Table 14). The value of petroleum imports increased by more than 22 per cent in 1981 after a 62 per cent increase in 1980. However, preliminary information indicates that in volume terms, imports of petroleum and petroleum products grew by 3 per cent, after remaining roughly constant during 1980. Imports of consumer goods continued to grow at a relatively rapid pace (19 per cent) in 1981. The compound annual growth rate of these imports during the past decade was 16 per cent. Imports of capital goods increased by only 2 per cent in 1981 and imports of raw materials and intermediate goods increased by less than 1 per cent.

Table 14. Philippines: Increases in Imports by Category, 1971-81

(In millions of U.S. dollars)

	Compound Annual Growth Rate 1971-81	Percentage change Over Preceding Year 1979	1980	1981	Preliminary 1981
Non-oil imports	18.7	28.9	15.3	3.4	5,666
Capital goods	16.1	27.4	11.3	2.4	2,034
Raw materials and intermediate goods	21.2	32.1	15.6	0.6	2,871
Consumer goods	16.2	19.2	28.4	19.3	761
Petroleum and petroleum products	34.5	33.1	62.4	21.6	2,734
Total	21.6	29.8	25.8	8.7	8,400

Sources: Data provided by the Philippine authorities; and staff estimates.

Petroleum imports continued to become relatively more important during 1981, accounting for 32 per cent of total imports, compared to 29 per cent in 1980 (Appendix Table XXIII). At the same time, imports of raw materials and intermediate goods as well as imports of capital goods have become relatively less important, accounting for 34 per cent and 24 per cent, respectively, of total imports in 1981. Imports of raw materials and intermediate goods had accounted for 40 per cent of total imports, and capital goods, for about 29 per cent as recently as 1979.

c. Direction of trade

The geographic distribution of the Philippines' external trade has undergone only minor changes in recent years (Appendix Table XXIV) The United States and Japan remain the Philippines' major trading partners, together accounting for nearly 54 per cent of exports and 43 per cent of imports during 1980 (the latest year for which data are available). However, the share of Philippine exports going to the United States declined from 35 per cent of total exports in 1977 to 27 per cent in 1980. At the same time, Japan's share has increased from 23 per cent in 1977 to nearly 27 per cent in 1980, and the share of the EEC countries has varied between a high of 20 per cent in 1979 and 17 per cent in 1980.

On the import side, the share of the United States has grown from 20 per cent of total imports in 1977 to 23 per cent in 1980, while that of Japan has declined from 25 per cent in 1977 to 20 per cent in 1980. The increase in petroleum prices has raised the relative share of Middle Eastern oil exporting countries in imports from 18 per cent in 1977 to 21 per cent in 1980. The EEC countries accounted for less than 11 per cent of total imports during 1980 compared to 12 per cent in 1977 and 14 per cent in 1979.

d. Services and transfers

Developments in the services and transfers accounts have been dominated by increases in interest payments on external debt, and by growth in remittances of Filipinos working abroad. As a consequence of the increase in external debt and higher interest rates in international capital markets, interest payments abroad have increased from 0.9 per cent of GNP in 1977 to 2.2 per cent in 1981 (Table 12). At the same time, remittances of Filipinos working abroad have grown from approximately 0.6 per cent of GNP in 1977 to 2.1 per cent of GNP in 1981. The growth in remittances has been, in large part, a result of the authorities' program of coordinating the foreign employment of Filipinos, especially in construction activity in Middle Eastern countries. These workers are required by law to remit 50 to 70 per cent of their earnings, depending on the terms of their employment. The growth in net transfers from $0.3 billion in 1977 to $0.5 billion in 1981 has been a result of the growth in that portion of personal remittances which are classified as transfers, presumably from Filipinos abroad who are not subject to the minimum remittance requirement.

3. Capital movements

Net capital inflow in 1981 totalled $1.9 billion, compared to $1.7 billion in 1980 and $1.0 billion in 1979 (Appendix Table XXV). Not only did the net capital inflow increase substantially during 1979-81, but the composition shifted as well. While net recourse to medium- and long-term loans remained virtually unchanged during this period, net use of exceptional financing 1/ increased from less than $0.1 billion in 1979 to $0.2 billion in 1981. Recourse to short-term capital 2/ grew from less than $0.1 billion in 1979 to $0.8 billion in 1980, declining again to $0.2 billion in 1981. Direct investment grew from less than $0.1 billion in both 1979 and 1980 to nearly $0.4 billion in 1981, reflecting foreign equity participation in certain specific projects. Finally, the Central Bank sharply increased the monetization of gold, from $0.04 billion in 1979 to $0.1 billion in 1980 and $0.4 billion in 1981. By law, all primary gold production must be sold to the Central Bank at market prices. The Central Bank carries these gold holdings as an asset valued at purchase price. Any subsequent sale of gold may, therefore, produce profits (or losses) which are reflected in the balance of payments as monetization of gold. The 1981 increase in monetization apparently

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1/ Includes capital inflow from IMF Trust Fund and from IBRD Structural Adjustment Loans.

2/ Excluding FCDU deposits as explained in footnote 1 on page 42.

resulted not so much from increased gold production or sales as from profits on sales of gold which had been acquired at low prices relative to the current market price.

The overall balance of payments deficit in 1981 of $0.5 billion was financed through a $0.7 billion drawdown of net reserves of the Central Bank, as the commercial banks' net reserve position strengthened by $0.2 billion . The gross reserves of the Central Bank declined by $0.45 billion to $2.7 billion, while the commercial banks gained $0.3 billion in reserve assets. Therefore, at end-1981, the net international reserves of the banking system were negative $1.3 billion, while gross reserves (official and other) totalled $5.3 billion.

4. External debt

On the basis of preliminary data, the Philippines' medium- and long-term external debt continued to grow in 1981 at the pace of recent years. Debt outstanding (disbursed) at end-1981 stood at $10.1 billion, more than 17 per cent above the end-1980 level (Table 15). In 1980, the rate of increase was nearly 20 per cent and in 1979, 15 per cent. Of the total debt outstanding, some 70 per cent was public sector debt, about the same proportion as in recent years. Some $2.0 billion of the public sector debt outstanding at end-1981 was contracted under the Consolidated Foreign Borrowing Program, by which the Central Bank contracts debt in foreign currency under its own name for onlending to other Philippine entities, both public and private. Total medium- and long-term debt outstanding reached 25.9 per cent of GNP, compared to 24.1 per cent in 1980 and 24.0 per cent in 1979. The net debt (defined as debt outstanding less gross official reserves) increased sharply to 19.0 per cent of GNP in 1981, due in part to the decline in gross official reserves.

Although the authorities had anticipated a sizeable increase in applications for approvals of external debt in 1981 related to the major industrialization projects, the total of debt approved during 1981 declined to $2.6 billion from the 1980 total of $3.4 billion. The lower-than-anticipated approvals were due to delays in finalizing certain major investment projects. However, debt disbursed increased to $1.9 billion in 1981 from $1.6 billion in 1980. In addition, the "pipeline" of external debt, including external debt contracted but undisbursed plus debt approved but not yet contracted, continued to grow in 1981.

The major effort undertaken during 1978-79 to improve the maturity structure of the external debt was largely responsible for the decline in amortization payments (including prepayments) during 1980 to $0.5 billion from $1.0 billion in both 1978 and 1979. Amortization payments during 1981 totalled $0.7 billion. Although information is not complete for 1981, it appears that the average maturity of external debt at end-1981 will be above the end-1980 level of 13.2 years, and the average grace period will be more than five years. The relative share of floating

Table 15. Philippines: Medium- and Long-Term External Debt Operations, 1977-81

	1977	1978	1979	1980	1981
		(In millions of U.S. dollars)			
Outstanding debt at end of period 1/	5,004	6,200	7,137	8,554	10,054
Outstanding debt at beginning of period	3,932	5,004	6,200	7,137	8,554
Net drawings	899	832	1,114	1,053	1,210
Drawings	1,229	1,791	2,148	1,600	1,896
Amortization (-)2/	330	959	1,034	547	686
Adjustments 3/	173	364	-177	364	290
Debt service 4/	513	721	1,028	1,064	1,540
Amortization	330	453	542	456	687
Interest	183	268	486	608	853
Prepayment	—	506	492	92	4
Net debt 5/	3,479	4,317	4,714	5,399	7,357
		(In per cent)			
Debt outstanding/GNP	24.0	25.6	24.0	24.1	25.9
Net debt/GNP	16.7	17.9	15.9	15.2	19.0
Debt service/GNP	2.5	3.0	3.5	3.0	4.0
Debt outstanding/exports of goods and nonfactor services	131.2	146.5	129.9	123.5	137.7
Net debt/exports of goods and nonfactor services	91.2	102.0	85.8	77.9	100.8
Debt service/exports of goods and nonfactor services	13.4	17.0	18.7	15.4	21.1

Source: Data provided by the Philippine authorities.

1/ Excludes loans of a maturity of 1 year or less, and debt to IMF.
2/ Includes prepayment of debt due in future years.
3/ Includes audit adjustment and exchange rate charges.
4/ Excluding prepayments of debt due in future years, and payments to IMF.
5/ Total medium- and long-term external debt outstanding less gross official reserves.

rate debt is estimated to have increased during 1981, and the average spread on this debt is expected to have declined in 1981, as it has since 1978.

The increase in amortization payments and the increase in total interest charges on floating rate debt due to high levels of reference rates (LIBOR, SIBOR, etc.) resulted in an increase in debt service payments on medium- and long-term external debt from $1.3 billion in 1980 to $1.6 billion in 1981 (including payments to IMF). Therefore, the debt service ratio 1/ increased to 23 per cent in 1981, compared to 18 per cent in 1980, and debt service payments increased from 3.0 per cent of GNP in 1980 to 4.0 per cent in 1981. Official debt service projections for 1982-87 based debt outstanding and/or approved as of September 30, 1981 indicate that debt service payments will increase sharply again in 1982 (Appendix Table XXVII).

By statute (RA 6142), the Central Bank is required to control approvals of external debt, so that the debt service ratio (as defined in the statute) does not exceed 20 per cent. Although the statutory definitions are somewhat complicated, debt service includes both service on medium- and long-term as well as short-term external debt. The denominator for the debt service ratio includes all external receipts, both capital and current, of the preceding year. As so defined, the ratio increased to 19.0 per cent in 1981 from 18.7 per cent in 1980 (Appendix Table XXVIII), thus approaching the authorities' statutory limit.

Although annual data on external debt classified by type of creditor are only available through 1980, it appears that in recent years the Philippines has become relatively more reliant on financial institutions as a source of credit (Appendix Table XXIX). The share of financial institutions as holders of medium- and long-term external debt (including both public and private debt) increased to 52 per cent by 1980 compared with 42 per cent in 1977. At the same time, the share of debt deriving from suppliers credits declined from 24 per cent in 1977 to less than 13 per cent in 1980.

VI. Exchange and Trade System

The Philippines has an exchange system under which the exchange rate is determined largely on the basis of demand and supply in the exchange market. However, the authorities intervene when necessary to maintain orderly conditions in the exchange market and for other policy objectives. The U.S. dollar is the intervention currency, and at end-1981, the exchange rate was ₱ 8.2 = US$1.

1/ Defined as the ratio of amortization and interest payments on medium- and long-term external debt (including payments to the IMF) to exports of goods and nonfactor services.

During 1975-80, the peso/U.S. dollar rate moved within a narrow band (Appendix Table XXX). However, due to the depreciation of the dollar against other major currencies, the peso depreciated in real effective terms through late 1978 (Chart 5). During 1979-80, the relatively high rate of inflation in the Philippines brought about an appreciation of the peso in real effective terms of more than 18 per cent over 1978, bringing the real effective exchange rate back to its 1975 level. During 1981, the peso depreciated gradually by about 7.9 per cent with respect to the dollar. Given the general strengthening of the dollar in international markets in early 1981, the peso appreciated in trade-weighted nominal effective terms by more than 6 per cent between December 1980 and July 1981 (Appendix Table XXX). During August-December 1981, the peso depreciated by more than 6 per cent in nominal effective terms as the dollar depreciated slightly in world markets. In real effective terms, the peso appreciated by more than 9 per cent during December 1980-July 1981. Although complete information is not yet available, it appears likely that the peso depreciated in real effective terms by more than 5 per cent during August-December. Therefore, the peso would have appreciated in real effective terms by more than 3 per cent (December 1980-December 1981), and by nearly 2 per cent on a period average basis.

The Philippines maintains restrictions on payments and transfers for current international transactions, including: (1) the requirement of prior approval by the Central Bank for foreign exchange sales for specified imports; and (2) limits established by the Central Bank on foreign exchange sales for specified invisible payments.

Import items are divided into ten categories according to type of good and the degree to which they are determined to be essential by the authorities. Foreign exchange sales for importation of items under three categories--nonessential consumer goods (NEC), semi-unclassified consumer goods (SUC), and unclassified consumer goods (UC)--require prior approval and are generally tightly restricted or effectively banned. In 1980, imports under these three categories accounted for 1.6 per cent of the value of total imports.

Imports of items under the NEC category are restricted mainly for balance of payments reasons, while those under the UC category are restricted mainly for purposes of domestic protection; both categories contain some items restricted for other reasons such as health and national security. As of end-May 1980, the number of tariff items in these three categories was 1,306. As the first step in a phased liberalization of exchange restrictions on imports to be implemented in tandem with the tariff reform discussed in Annex I, effective January 1, 1981 agent banks were authorized to sell foreign exchange freely for 263 of these 1,306 tariff items. A further 610 items are scheduled to be liberalized in 1982 and 87 items in 1983. Liberalization of the remaining items subject to exchange restrictions, as well as items subject to trade restrictions, is being reviewed.

There are several other regulations governing imports, including the following: (a) Importation of certain items require clearance certificates from specified government agencies; foreign exchange for such imports is automatically made available upon presentation of the appropriate clearance certificate to the Central Bank. These imports are restricted mainly for protection and health reasons; the certificates requirement is only for monitoring purposes. (b) Payments for imports of certain commodities (wheat, raw cotton, and leaf tobacco) are permitted when financed through certain official credit arrangements. This regulation is intended to ensure utilization of available external commodity assistance; if it can be demonstrated that such assistance is not available, imports of the relevant commodities are allowed. (c) Importation of plant, machinery, equipment, and spare parts under deferred payments arrangements with maturity periods longer than 360 days is subject to prior approval by the Central Bank. If payment terms are cash or within 360 days, prior approval by the Central Bank is necessary for importation by any single importer of nonagricultural machinery and equipment with an aggregate value in excess of $50,000 within a calendar month, with the exception of certified export-oriented firms, and other importers who have obtained prescribed certification from the Board of Investment (BOI). These regulations are geared to foreign debt management and the monitoring of investment priorities. (d) Trade with state trading companies, excepting Yugoslavia, must be effected through the Philippine International Trading Corporation. (e) Certain authorized agent banks require marginal import deposits of 50 per cent against the opening of letters of credit.

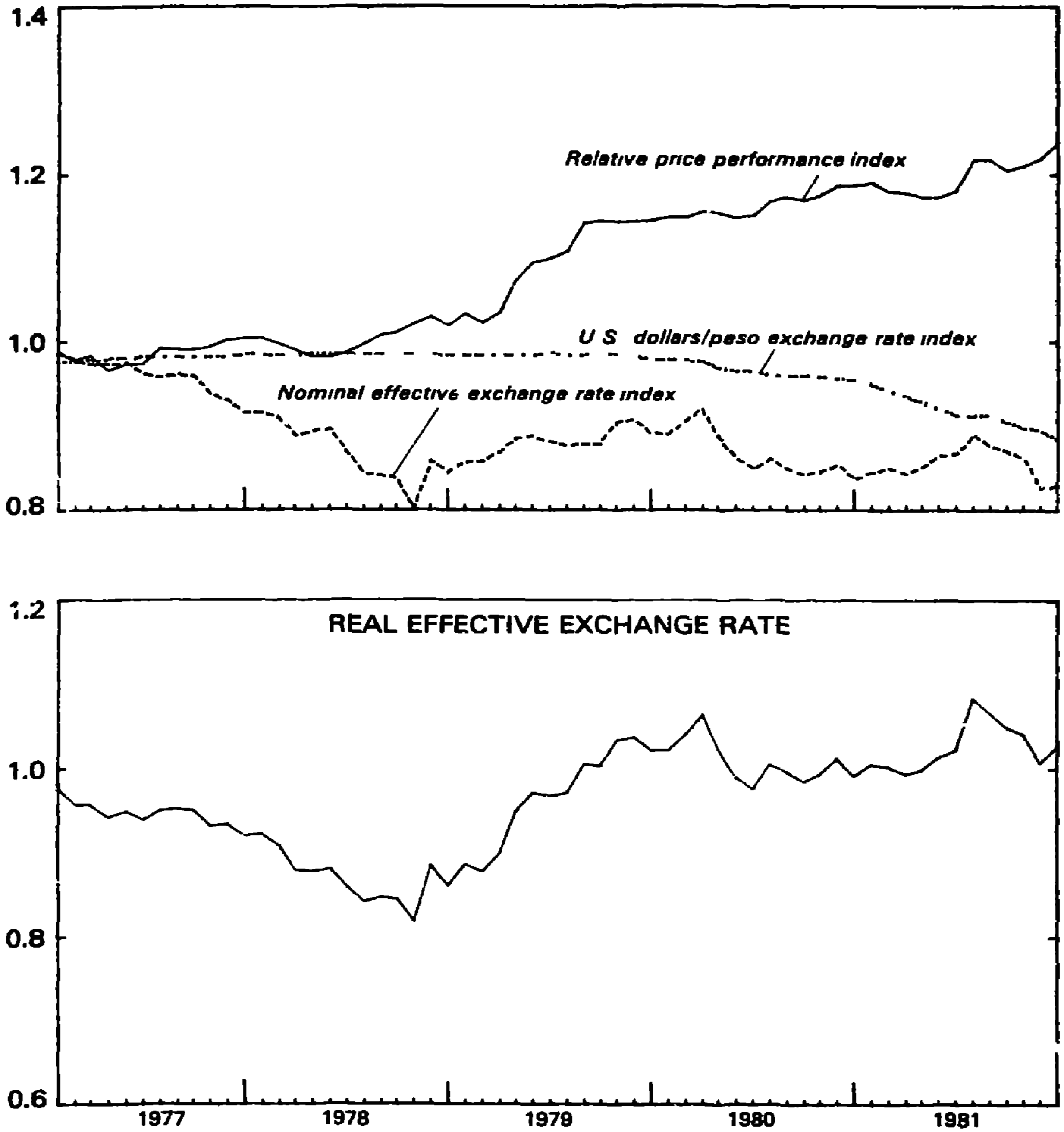
Limits established by the Central Bank for purchases of foreign exchange for invisible payments mainly comprise the following: (a) Exchange for travel abroad: business travel abroad, foreign exchange allowances depend upon whether the firm does or does not have foreign exchange earnings, upon the rank of the employee, and upon the destination; these allowances vary from $35 per day to $150 per day plus representation allowances; nonbusiness travel abroad, the allocation is limited to $1,000 per year for travel to Africa, North America, South America, Australia, Europe, Japan, the Middle East, and New Zealand; for travel to Guam, Hong Kong, or any other neighboring country, the limit is $600 per year. (b) Exchange for educational expenses abroad for students undertaking degree courses at duly accredited institutions: for studies in the United States, $250 a month for living and other out-of-school expenses, plus the cost of tuition, books, etc.; for studies in Australia, Europe, Japan, and New Zealand, $150 a month; any scholarship allowances are deducted from these amounts. (c) Remittances to dependents of residents: $250 a month for each dependent living in the United States, $200 a month if living in Australia, Europe, Japan, or New Zealand, and $100 a month if living in other areas; allowances for dependents are provided only for close relatives under conditions prescribed by the Central Bank. (d) Remittances of royalties or rentals on patents, trademarks, and copyrights are freely permitted (net of taxes) for contracts registered with the Central Bank, provided that the royalties do not exceed 5 per cent of the wholesale price of the commodity that is manufactured locally under the royalty contract (2 per cent in the case of

CHART 5

PHILIPPINES

INDICES OF NOMINAL EFFECTIVE EXCHANGE RATE, RELATIVE PRICE PERFORMANCE, AND U.S. DOLLAR/PESO EXCHANGE RATE, 1977-81

(1975 = 100)



Sources IMF *International Financial Statistics,* and staff estimates marketing service contracts), and certain other stipulations. (e) Remittances of the producer's share of earnings made on motion picture films and rentals on television films are freely permitted provided that the shares or rentals do not exceed 60 per cent of net proceeds from films. (f) Profits earned and dividends declared by nonresidents before January 1, 1973 may be remitted over a two-year period; the unremitted amounts outstanding are relatively small. Remittances of profits and dividends (net of taxes) accruing to nonresidents out of net profits realized since January 1, 1973 are permitted in full provided that remittances are not financed from domestic credit. (g) Applications for certain invisibles for which no basic allowance has been set are considered on their merits by the Central Bank.

The major changes in the exchange and trade system in 1981 are given below.

March 9: Imports of citizen band radio receivers were prohibited for purposes of national security.

April 14: Allowances for purchases of foreign exchange for travel abroad were increased substantially. For nonbusiness travel the permitted allowance was raised from $500 to $1,000 per annum for travel to Africa, North and South America, Canada, New Zealand, Australia, Europe, the Middle East, or Japan. For all other countries, the annual allowance was raised from $200 to $600. Travelers under 12 years of age are entitled to half of the standard allowance.

For business travel, a system of allowance was introduced which provides varying amounts depending upon whether the firm does or does not have foreign exchange earnings, upon the rank of the employee, and upon whether the destination is or is not one of the countries or areas enumerated above for nonbusiness travel. The higher allowances for export-oriented firms introduced on September 8, 1980 remain in force. Under the new regulations, senior officials of firms which have foreign exchange earnings are entitled to $100 per day for travel to the enumerated areas and $70 per day to all other areas; the corresponding amounts for other employees of firms with foreign exchange earnings are $70 and $50. Senior officials of firms which do not have foreign exchange earnings are entitled to $70 per day for travel to the enumerated areas and $50 per day for all other areas; the corresponding amounts for other employees of such firms are $50 and $35. These per diem amounts may be purchased for up to 20 days per trip; applications for travel abroad for a fifth or subsequent time within one calendar year will be subject to careful review by the agent banks to prevent abuse (MAAB No. 7).

June 26: All imports valued at more than $1,000 must be covered by letters of credit and shall be subject to the release certificate requirement. Imports by prequalified producers and/or importers under documents against acceptance (D/A) and open account (O/A) arrangements are exempt. Certain imports valued at less than $1,000 are exempted from the release certificate requirement if they are imported free of cost to the importer (Circular 808).

November 10: The authentication requirement on commercial invoices was abolished, and an import processing fee of ₱ 250 was imposed on all imports covered by a Formal Entry having an invoice value of ₱ 5,000 or more.

December 15: Unless specifically authorized by the Central Bank or allowed under existing international agreements or Central Bank regulations, no person shall take or transmit or attempt to take or transmit foreign exchange in any form out of the Philippines, directly, through other persons, through the mails, or through international carriers.

Table I. Philippines: Growth Rates of Expenditure on Gross National Product at Constant 1972 Prices, 1977-81

(In per cent per annum)

	1977	1978	1979	1980	1981 1/
Consumption	7.3	4.4	4.4	4.8	4.7
Private	7.6	4.6	4.5	4.8	4.7
Government	5.0	3.3	3.8	4.8	4.7
Gross domestic capital formation	3.9	6.3	7.4	6.0	2.4
Fixed capital formation	6.1	6.4	7.5	8.9	3.6
Construction	10.6	4.5	5.5	9.6	4.5
Government	17.2	7.8	8.5	5.0	5.1
Private	6.5	2.1	3.3	13.2	4 1
Machinery and equipment	1.6	8.4	9.5	8.3	2.8
Increase in stocks	-5.0	6.2	6.9	-8.3	-5.0
Exports of goods and services	18.7	-1.3	9.9	15.5	-3.4
Imports of goods and services	6.4	12.5	11.4	6.5	-6.1
Expenditure on gross national product	6.1	6.5	5.9	5.4	4.9
Memorandum item:					
Growth rates of GNP at current prices	16.1	15.6	23.2	21.1	18.7

Source: Data provided by the Philippine authorities.

1/ Preliminary official estimate.

Table II. Philippines: Distribution of Expenditures on Gross National Product, 1970 and 1977-81

(At current prices)

	Percentage Share of GNP					
	1970	1977	1978	1979	1980	1981 1/
Consumption	79.2	77.1	75.8	74.4	75.5	74.8
Private	70.8	67.0	65.9	66.0	67.4	66.9
Government	8.4	10.1	9.9	8.4	8.1	7.9
Gross domestic capital formation	21.5	28.7	28.9	29.9	30.5	30.1
Fixed capital formation	16.0	23.6	23.7	24.7	25.5	25.2
Construction	6.2	12.8	12.4	13.1	13.8	13.8
Government	1.0	5.3	5.3	5.8	5.8	5.8
Private	5.2	7.5	7.1	7.4	8.0	7.9
Machinery and equipment	9.8	10.8	11.3	11.6	11.8	11.5
Increase in stocks	5.5	5.1	5.2	5.2	5.0	4.8
Exports of goods and services	19.4	19.0	17.7	19.0	20.5	18.8
Imports of goods and services	19.7	22.5	23.2	24.3	26.0	24.2
Statistical discrepancy	1.3	-1.4	1.5	1.4	0.5	1.4
Gross domestic product	101.7	100.9	100.5	100.4	100.9	100.9
Net factor income from abroad	-1.7	-0.9	-0.5	-0.4	-0.9	-0.9
Gross national product	100.0	100.0	100.0	100.0	100.0	100.0

Source: Based on data provided by the Philippine authorities.

1/ Preliminary official estimate.

Table III. Philippines: Growth Rates of Gross Domestic Product by Industrial Origin at Constant 1972 Prices, 1977-81

(In per cent per annum)

	1977	1978	1979	1980	1981 1/
Agriculture, fishery, and forestry	5.0	4.8	5.3	4.9	4.3
Mining and quarrying	16.8	3.9	17.5	4.8	1.7
Manufacturing	7.5	6.8	5.4	5.9	5.1
Construction	6.0	6.9	7.0	9.7	5.8
Electricity, gas, and water	4.9	5.2	16.2	8.5	7.8
Transportation, communications, and storage	4.5	5.6	2.0	4.6	4.1
Commerce	2.6	6.4	6.4	5.5	5.0
Service	5.3	5.0	5.5	5.8	4.9
GDP at market prices	6.0	5.8	5.7	5.8	4.8

Source: Data provided by the Philippine authorities.

1/ Preliminary official estimate.

Table IV. Philippines: Distribution of Gross Domestic Product by Sector, 1970 and 1977-81

(At current prices)

	Percentage Share of GDP					
	1970	1977	1978	1979	1980	1981 1/
Agriculture, fishery and forestry	27.7	27.5	26.4	25.4	23.3	22.5
Mining and quarrying	2.8	1.6	1.9	2.7	3.0	3.1
Manufacturing	22.6	24.3	25.4	25.1	25.8	26.4
Construction	3.6	7.3	7.1	7.2	7.8	7.8
Electricity, gas and water	0.7	0.9	0.9	1.0	1.0	1.0
Transportation, communications and storage	4.2	5.4	5.5	5.6	6.2	6.2
Commerce	24.8	21.9	22.7	22.9	23.1	23.0
Services	13.6	11.1	11.1	10.3	10.2	10.0
GDP at market prices	100.0	100.0	100.0	100.0	100.0	100.0

Source: Based on data provided by the Philippine authorities.

1/ Preliminary official estimate.

Table V. Philippines: Production of Major Commodities, 1977-81

(Percentage changes from previous year)

	1977	1978	1979	1980 1/	1981 1/
Agriculture, fishery and forestry	3.8	9.7	5.6	2.1	...
Agricultural crops production 2/	4.4	10.8	8.5	...	...
Rice	4.8	6.8	4.4	5.6	-2.7
Corn	2.8	0.4	10.9	0.2	...
Coconut products 3/	-11.1	2.1	-22.3	3.4	...
Sugarcane	-6.5	-12.2	-3.3	3.2	...
Fruits and nuts	6.5	23.5	25.6	18.3	...
Fishery	10.8	3.3	1.3	--	...
Forestry	-7.0	-0.3	-9.0	-16.9	...
Mining and quarrying	16.1	-3.9	4.8	9.6	...
Metallic ore mining	19.5	-9.5	7.0	10.4	...
Gold	11.4	5.0	-6.5	20.3	17.5
Copper in concentrates	11.5	-5.2	8.4	5.7	0.5
Nickel	141.4	-19.7	12.7	18.2	-5.8
Nonmetallic mining and quarrying	1.0	25.5	-3.4	6.6	...
Manufacturing	3.5	4.7	4.5	4.3	...
Food, beverage, and tobacco	4.4	5.3	7.3	2.0	...
Textiles and leather	10.7	2.7	3.6	-1.5	...
Wood and wood products	3.3	4.8	8.3	-0.7	...
Paper, paper products and printing	-4.9	9.2	5.4	15.6	...
Chemical, chemical products, petroleum coal, rubber and plastic products	3.1	6.1	2.6	4.0	...
Nonmetallic mineral products excluding petroleum and coal products	-4.9	6.7	6.8	22.6	...
Basic metals	4.2	2.7	-0.1	11.9	...
Metal products, machinery and equipment	-3.2	0.2	-2.1	9.9	...

Source: Data provided by the Philippine authorities.

1/ Actual or latest estimate.
2/ Crop year ending June 30 of year indicated.
3/ Copra equivalent.

Table VI. Philippines: National Government Budgetary Revenue, 1977-82

	1977	1978	1979	1980	1981 Latest est.	1982 Estimates
	(In billions of Philippine pesos)					
Tax revenue	17.0	20.5	25.9	30.5	31.7	36.0
Domestic-based taxes	10.7	12.7	16.5	18.9	20.7	23.8
Taxes on income and profits	(4.1)	(5.1)	(6.8)	(8.7)	(9.6)	(11.0)
Excise duties	(3.5)	(4.1)	(5.5)	(5.6)	(6.3)	(7.2)
Sales and business tax	(2.2)	(2.4)	(3.5)	(3.7)	(3.8)	(4.5)
Other 1/	(0.9)	(1.0)	(0.7)	(0.9)	(1.0)	(1.1)
Taxes on international trade and transactions	6.3	7.8	9.4	11.6	11.0	12.2
Import duties 2/	(5.7)	(7.4)	(8.7)	(11.2)	(10.7)	(11.9)
Export duties	(0.6)	(0.4)	(0.7)	(0.4)	(0.3)	(0.3)
Nontax revenue 3/	3.0	3.5	3.6	4.2	4.0	4.7
Total revenue	20.0	24.0	29.5	34.7	35.7	40.7
	(As per cent of total revenue)					
Tax revenue	85.0	85.4	87.8	87.9	88.8	88.5
Domestic-based taxes	53.5	52.9	55.9	54.5	58.0	58.5
Taxes on income and profits	(20.5)	(21.7)	(23.1)	(25.1)	(27.0)	(27.0)
Excise duties	(17.5)	(17.1)	(18.5)	(16.1)	(17.6)	(17.7)
Sales and business tax	(11.0)	(10.0)	(11.9)	(10.7)	(10.6)	(11.1)
Other 1/	(4.5)	(4.1)	(2.4)	(2.6)	(2.8)	(2.7)
Taxes on international trade and transactions	31.5	32.5	31.9	33.4	30.8	30.0
Import duties 2/	(28.5)	(30.8)	(29.5)	(32.3)	(30.0)	(29.3)
Export duties	(3.0)	(1.7)	(2.4)	(1.1)	(0.8)	(0.7)
Nontax revenue 3/	15.0	14.6	12.2	12.1	11.2	11.5
Total revenue	100.0	100.0	100.0	100.0	100.0	100.0

Source: Data provided by the Ministry of Finances.

1/ Includes property tax, documentary and stamp taxes, and unclassified tax revenue.
2/ Consists of customs duties and import taxes.
3/ Includes administrative fees and charges, property income, and minor amounts of grants.

Table VII. Philippines: National Government Budgetary Expenditure, 1977-82

	1977	1978	1979	1980	1981 Latest est.	1982 Estimates
	(In billions of Philippine pesos)					
Current expenditure	17.7	19.2	20.6	24.5	26.5	30.4
Personal services	6.3	7.5	8.4	9.3	10.0	11.4
Maintenance and other operating expenditure	9.7	9.6	9.2	11.4	12.0	13.5
Allotments to local governments	0.8	0.8	1.2	1.5	1.7	2.2
Interest payments	0.9	1.3	1.8	2.3	2.8	3.3
Capital expenditure	5.0	7.0	9.2	13.6	21.1	20.8
Infrastructure 1/	2.3	3.7	4.3	7.3	9.5	8.4
Other capital outlays 2/	0.5	0.7	0.7	1.1	2.7	3.6
Equity contribution	2.2	2.4	3.4	4.5	7.9 3/	6.6
Net lending	--	0.2	0.8	0.7	1.0	2.2
Total expenditure	22.7	26.2	29.8	38.1	47.6	51.2
	(As per cent of total expenditure)					
Current expenditure	78.0	73.3	69.1	64.3	55.7	59.4
Personal services	27.8	28.6	28.2	24.4	21.0	22.3
Maintenance and other operating expenditure	42.7	36.6	30.9	29.9	25.2	26.4
Allotments to local governments	3.5	3.1	4.0	3.9	3.6	4.3
Interest payments	4.0	5.0	6 0	6.1	5.9	6.4
Capital expenditure	22.0	26.7	30.9	35.7	44.3	40.6
Infrastructure 1/	10.1	14.1	14.4	19.2	20.0	16.4
Other capital outlays 2/	2.2	2.7	2.4	2.9	5.6	7.0
Equity contributions	9.7	9.2	11.4	11.8	16.6 3/	12.9
Net lending	--	0.7	2.7	1.8	2.1	4.3
Total expenditure	100 0	100.0	100.0	100.0	100.0	100.0

Source: Data provided by the Ministry of Finance.

1/ Consists of investment expenditure by the Ministry of Public Works and Highways and by the Ministry of Transportation and Communication under the Infrastructure Investment Program.

2/ Investment outlays not provided for under the Infrastructure Investment Program.

3/ Includes P 500 million, or 1.1 per cent of total expenditure, for contribution to the Industrial Fund.

Table VIII. Philippines: National Government Budgetary Revenue and Expenditure Components as a Percentage of Gross National Product, 1977-82

	1977	1978	1979	1980	1981 Latest est.	1982 Estimates
Total revenue	13.0	13.5	13.5	13.1	11.7	11.5
Tax revenue	11.0	11.5	11.9	11.5	10.4	10.2
Domestic-based tax	6.9	7.1	7.6	7.1	6.8	6.7
Taxes on income and profits	(2.6)	(2.9)	(3.1)	(3.3)	(3.2)	(3.1)
Excise duties	(2.3)	(2.3)	(2.5)	(2.1)	(2.1)	(2.0)
Sales and business tax	(1.4)	(1.3)	(1.6)	(1.4)	(1.2)	(1.3)
Other	(0.6)	(0.6)	(0.4)	(0.3)	(0.3)	(0.3)
Taxes on international trade and transactions	4.1	4.4	4.3	4.4	3.6	3.5
Import duties	(3.7)	(4.2)	(4.0)	(4.2)	(3.5)	(3.4)
Export duties	(0.4)	(0.2)	(0.3)	(0.2)	(0.1)	(0.1)
Nontax revenue	2.0	2.0	1.6	1.6	1.3	1.3
Total expenditure	14.7	14.7	13.6	14.4	15.6	14.5
Current expenditure	11.5	10.8	9.4	9.3	8.7	8.6
Personal services	4.1	4.2	3.8	3.5	3.3	3.2
Maintenance and other operating expenditure	6.3	5.5	4.2	4.3	3.9	3.9
Allotments to local governments	0.5	0.4	0.5	0.6	0.6	0.6
Interest payments	0.6	0.7	0.8	0.9	0.9	0.9
Capital expenditure	3.2	3.9	4.2	5.1	6.9	5.9
Infrastructure	1.5	2.1	2.0	2.7	3.1	2.4
Other capital outlays	0.3	0.4	0.3	0.4	0.9	1.0
Equity contribution	1.4	1.3	1.5	1.7	2.6	1.8
Net lending	--	0.1	0.4	0.3	0.3	0.7

Sources: Data provided by the Ministry of Finance, and staff estimate and projection of GNP for 1981 and 1982, respectively.

Table IX. Philippines: General Government Tax Ratios, 1978-82

(In per cent of GNP)

	1978	1979	1980	1978-80 Average	1981 Latest est.	1982 Estimates
National government tax revenue	11.5	11.9	11.5	11.7	10.4	10.2
Domestic based taxes	(7.1)	(7.6)	(7.1)	(7.3)	(6.8)	(6.7)
Taxes on international trade and transactions	(4.4)	(4.3)	(4.4)	(4.4)	(3.6)	(3.5)
Local government tax revenue 1/	0.7	0.7	0.7	0.7	0.7	0.7
National government plus local government tax revenue	12.2	12.6	12.2	12.3	11.1	10.9
Social security contributions 2/	0.8	0.7	0.7	0.7	0.7	0.6
General government tax revenue	13.0	13.3	12.9	13.1	11.8	11.7

Source: Data provided by the Ministry of Finance, and staff estimate and projection of GNP for 1981 and 1982, respectively.

1/ Excluding tax revenue allotments from the National Government.
2/ Consists of employers' and employees' contributions to the SSS and employees' contributions to the GSIS.

Table X. Philippines: Selected Average Interest Rates, 1977-81

(In per cent per annum)

		Rediscount rate 1/	Interbank call rate	Commercial bank loans	Weighted average interest rate (WAIR) 3/	LIBOR 4/
1977:	I	5.92	12.87	...	13.93	5.11
	II	5.87	11.33	...	13.26	5.56
	III	5.60	10.88	12.35	11.11	6.21
	IV	5.30	12.83	12.77	12.05	7.11
1978:	I	5.25	8.04	12.21	9.79	7.28
	II	5.01	9.44	12.34	10.14	7.84
	III	4.99	12.00	12.90	11.32	8.71
	IV	5.20	12.45	12.68	11.63	11.08
1979:	I	4.43	13.27	12.56	12.45	10.87
	II	4.52	14.59	12.37	13.01	10.62
	III	4.61	13.64	12.22	13.11	11.66
	IV	5.80	12.81	12.68	12.98	14.70
1980:	I	5.40	12.57	13.17	13.42	17.11
	II	5.85	13.34	13.26	13.88	11.15
	III	5.23	8.88	13.42	12.23	12.08
	IV	5.62	12.69	13.47	13.53	17.10
1981:	I	5.48	15.14	13.96	15.32	16.33
	II	4.71	16.11	14.12	15.91	17.47
	III	7.47	12.89	14.83	15.96	18.44
	IV	7.76	16.22	n.a.	16.18	13.80

Sources: Data supplied by the Central Bank of the Philippines; and International Financial Statistics.

1/ Central Bank loans to commercial banks.
2/ Based on total outstanding loans.
3/ Based on money market instruments.
4/ Three-month deposits for U.S. dollars.

Table XI. Philippines: Central Bank of the Philippines - Reserve Money, 1978-81

(In millions of Philippine pesos)

		1978	1979	1980				1981			
		Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June	Sept.	Dec.
I.	Net foreign assets	5,716	5,646	4,441	5,020	4,435	3,389	-546	-935	-3,370	-2,330
	Assets	14,106	18,146	18,949	20,313	20,414	23,609	21,433	19,554	19,243	20,983
	Liabilities	8,390	12,500	14,508	15,293	15,979	20,220	21,979	20,489	22,613	23,313
II.	Net claims on Government	3,097	4,025	3,569	3,169	2,957	4,630	5,670	7,518	7,601	8,868
	Claims on Government	5,727	6,324	6,297	6,358	6,080	6,965	7,438	9,475	10,607	11,328
	of which:										
	Contribution to IRF	--	--	--	--	--	--	--	500	500	500
	Government deposits	2,630	2,299	2,728	3,189	3,123	2,335	1,768	1,957	3,006	2,460
III.	Claims on other official entities	741	681	670	650	617	555	537	518	473	460
IV.	Claims on commercial banks	3,645	6,743	6,857	7,162	7,933	10,206	9,555	10,479	11,227	12,473
	of which:										
	Emergency assistance	--	--	--	--	--	--	--	110	201	2,180
V.	Claims on other financial institutions	3,267	4,131	4,361	4,564	4,613	4,860	6,479	6,730	7,316	6,909
	of which:										
	Emergency assistance to nonbanks	--	--	--	--	--	--	--	1,648	1,612	501
	Equity participation of										
	DBP	--	--	--	--	--	--	--	--	280	540
	LBP	--	--	--	--	--	--	--	--	140	140
VI.	Bonds (CBCIs)	9,907	11,941	11,857	12,187	11,655	11,439	11,597	10,987	10,598	10,061
VII.	Other items (net)	5,534	5,344	5,903	4,295	3,750	3,991	3,506	1,457	1,959	1,366
	of which:										
	Due from Administrator - IRF	--	--	--	--	--	--	--	1,000	1,000	1,000
	IRF deposits	--	--	--	--	--	--	--	1,266	1,184	1,054
VIII.	Reserve money 1/	12,093	14,629	13,944	12,673	12,650	16,192	13,604	14,780	14,608	17,685

Source: Data supplied by the Philippine authorities.

1/ Equals the sum of items I through V less VI plus VII.

Table XII. Philippines: Liquidity Multiplier and Monetary Ratios, 1977–81

		Liquidity multiplier 1/	Monetary Ratios: Currency Deposits 2/	Monetary Ratios: Reserve Deposits 3/
1977:	I	5.00	16.8	11.9
	II	5.01	16.1	14.0
	III	5.06	16.0	13.5
	IV	4.48	18.1	14.8
1978:	I	4.47	17.2	14.6
	II	4.49	16.3	14.1
	III	4.54	16.3	13.8
	IV	4.29	18.6	14.3
1979:	I	4.38	16.7	14.0
	II	4.69	17.2	13.4
	III	4.66	16.5	13.9
	IV	3.92	19.1	14.7
1980:	I	4.24	17.3	14.0
	II	4.57	16.5	12.9
	III	4.84	15.2	13.2
	IV	4.19	17.7	14.3
1981:	I	5.02	15.8	12.2
	II	4.84	15.5	13.1
	III	4.92	14.9	13.2
	IV	4.44	17.5	11.5

Sources: Philippine Financial Statistics; the Central Bank of the Philippines; and staff calculations.

1/ Defined as ratio of liquidity to reserve money.
2/ Defined as ratio of currency in circulation to deposit liabilities including deposit substitutes.
3/ Defined as ratio of banking system reserves (i.e., cash in vault, balances at Central Bank, eligible government securities, and eligible foreign securities and balances) to deposit liabilities including deposit substitutes.

Table XIII. Philippines: Reserve Position of Commercial Banks, 1977-81

	Dec. 1977	Dec. 1978	Dec. 1979	Dec. 1980	Dec. 1981
	(In millions of Philippine pesos)				
Total reserves	5,460	6,185	6,992	8,172	8,221
Philippine National Bank	1,243	1,236	1,983	1,626	1,623
Other commercial banks	4,217	4,949	5,009	6,546	6,598
Required reserves	5,270	6,308	6,942	7,549	8,649
Philippine National Bank	1,039	1,230	1,517	1,390	1,790
Other commercial banks	4,231	5,078	5,425	6,159	6,859
Excess reserves (deficiency -)	190	-123	50	623	-429
Philippine National Bank	204	6	466	236	-167
Other commercial banks	-14	-129	-416	387	-262
	(In per cent)				
Total reserves/required reserves	3.6	-1.9	0.7	8.3	-5.0

Sources Philippine Financial Statistics; and data supplied by the Central Bank of the Philippines.

Table XIV. Philippines: Legal Reserve Requirements, 1970, 1975-81

(In per cent)

End Year	Commercial Banks 1/			Development Bank of the Philippines		Thrift Institutions		Rural Banks			All Financial Institutions
	Demand deposits	Savings deposits	Time deposits	Savings deposits	Time deposits	Demand deposits	Savings and time deposits	Demand deposits	Savings deposits	Time deposits	Deposit Substitutes
1970	20.0	20.0	20.0 2/	10.0 3/	10.0 3/	10.0	10.0	14.0	12.0	10.0 2/	n.a.
1975	20.0	20.0	20.0 2/	8.0 3/	3.0 3/	8.0	8.0	14.0	8.0	8.0 2/	5.0
1976	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	8.0 4/	8.0 4/	14.0	8.0	8.0 2/	9.5
1977	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	8.0 4/	8.0 4/	14.0	8.0	8.0 2/	15.0
1978	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	8.0 4/	8.0 4/	14.0	8.0	8.0 2/	20.0
1979	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	20.0 4/	8.0 4/	14.0	8.0	8.0	20.0
1980	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	20.0 4/	8.0 4/	15.5	8.0	8.0	20.0
1981	20.0	20.0	20.0 2/	8.0 3/	8.0 3/	20.0 4/	8.0 4/	20.0	8.0	8.0	20.0
April 1982	19.0	19.0	19.0 5/	8.0 3/	7.0 3/ 6/	19.0 4/	7.0 4/ 6/	19.0	8.0	7.0 6/	19.0 5/

Source: Data supplied by the Central Bank of the Philippines.

1/ Effective January 17, 1977 the Land Bank and Amanah Bank were considered commercial banks for reserve requirements. Prior to that date they had the same reserve requirements as the Development Bank of the Philippines.

2/ Time deposits with maturities more than 730 days were exempted from reserve requirements.

3/ Holdings of CBCIs used as reserves should not exceed 10 per cent of required reserves.

4/ Holdings of CBCIs used as reserves should not exceed 20 per cent of required reserves.

5/ Under CBC No. 782 (2/27/81), reserve requirements on all types of deposits with a maturity of 730 days or less shall be 19.0 per cent effective January 1, 1982 and decreased at the rate of one percentage point every semester until it has been decreased to 16.0 per cent. Deposits with an original maturity of more than 730 days effective January 1, 1982 have a reserve requirement of 1 per cent which shall be increased one percentage point every semester until 5 per cent is reached.

6/ Under CBC No. 782 (2/27/81), reserve requirements on time deposits with original maturity of more than 730 days were lowered to 7 per cent on January 1, 1982 and will be reduced by one percentage point a semester until 5 per cent is reached.

Table XV. Philippines: Distribution of Commercial Bank Credit by Sectors, 1977-81

	Dec. 1977	Dec. 1978	Dec. 1979	Dec. 1980	Dec. 1981 1/
	(In millions of Philippine pesos)				
Agriculture	5,253.0	5,469.2	8,120.2	12,009.7	12,153.2
Mining	1,577.5	3,610.1	5,507.8	7,334.3	8,304.0
Commerce	11,714.2	13,879.8	14,045.6	11,210.7	11,517.6
Manufacturing	13,126.3	17,490.5	22,104.6	27,053.3	30,557.1
Construction	679.9	1,323.8	2,043.6	2,722.7	3,182.5
Services 2/	916.2	1,402.1	2,510.0	2,610.6	3,376.1
Real estate	2,017.4	2,273.8	2,620.4	2,297.9	2,734.3
Other	4,888.4	8,628.6	11,312.0	11,958.9	11,911.6
Total	40,172.9	54,077.9	68,264.2	77,198.1	83,736.4
	(In per cent)				
Agriculture	13.1	10.1	11.9	15.6	14.5
Mining	3.9	6.7	8.1	9.5	9.9
Commerce	29.2	25.7	20.6	14.5	13.8
Manufacturing	32.7	32.3	32.4	35.0	36.5
Construction	1.7	2.4	3.0	3.5	3.8
Services 2/	2.3	2.6	3.7	3.4	4.0
Real estate	5.0	4.2	3.8	3.0	3.3
Other	12.1	16.0	16.5	15.5	14.2
Total	100.0	100.0	100.0	100.0	100.0

Source: Data supplied by the Central Bank of the Philippines.

1/ Preliminary.
2/ Includes public utilities, transport, storage, and communications.

Table XVI. Philippines: Distribution of Credit of Other Financial Institutions by Sectors,1/ 1977-81

	Dec. 1977	Dec. 1978	Dec. 1979	Dec. 1980	Dec. 1981 2/
	(In millions of Philippine pesos)				
Agriculture	6,321.5	7,691.9	8,928.2	9,949.4	10,892.5
Commerce	271.5	349.1	677.2	1,334.0	2,300.2
Industry	4,753.3	5,966.6	6,639.8	9,494.6	11,342.3
Real estate	6,556.4	7,431.1	9,053.4	10,703.2	11,348.8
Consumption	1,606.8	1,892.0	2,452.6	3,325.6	3,479.9
Other	8,277.6	5,984.8	7,215.3	8,123.7	9,667.5
Total	22,787.1	29,315.5	34,966.5	42,930.5	49,031.2
	(In per cent)				
Agriculture	22.7	26.2	25.6	23.2	22.2
Commerce	1.0	1.2	1.9	3.1	4.7
Industry	17.1	20.4	19.0	22.1	23.1
Real estate	23.6	25.3	25.9	24.9	23.2
Consumption	5.8	6.5	7.0	7.7	7.1
Other	29.8	20.4	20.6	19.0	19.7
Total	100.0	100.0	100.0	100.0	100.0

Source: Data supplied by the Central Bank of the Philippines.

1/ Consists of credits of rural banks, specialized banks, and other Government nonbank financial institutions (SSS, GSIS, and ADA). Includes some double counting of interbank loans.

2/ Preliminary.

Table XVII Philippines: Summary Account of Nonbank Financial Intermediaries, 1977-81

(In millions of Philippine pesos)

	1977	1978	1979	1980				1981	
	Dec	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June
I. Consolidated System									
Net foreign assets	-2,641 /	-2,017 1	-316.3	-375.4	-137.8	-694.7	-389.3	-175.2	2.5
Net domestic assets	57,308.4	66,374.3	68,834.1	73,787.3	75,969.3	80,228.8	83,484.1	86.968.7	90,636.4
Credit to private sector	22,109 0	24,935.6	29,105 7	30,390.1	31,719.0	32,596.5	34,670.8	36,380.8	37,511.8
Mortgages	8,361 4	9,902.6	7,167.0	9,927.6	10,290.0	10,439.4	10,981.2	10,597.9	11,076.5
Investments	13,797.3	16,412 3	17,168 9	18,610.4	19,560.0	21,550.6	21,363.4	22,422.1	24,981.1
Other	13,040.7	15,123 8	15,392.5	14,859.2	15,400.3	15,642.3	16,468.7	17,567.9	17,067.0
Liabilities	54,846.7	64,357 2	68,517 8	73,411.9	76,831 5	79,534.1	83,094.8	86,793.5	90,638.9
Deposits	7,138.0	9,036.4	12,262 1	12,682.8	13,223.5	14,386.2	15,054.1	15,772.5	16,876.8
Shares	11,108.9	12,571 8	14,374.4	12,838 5	13,424.8	13,958 7	14,590.2	15,073.7	15,586.3
Loans payable	5,138.4	6,567 3	8,112 5	8,487 2	9,115.3	9,278.9	10,041.6	10.614.1	11,220.8
Other	31,461 4	36,181.7	33,768 8	39,403.4	41,067.9	41,910.3	43,408.8	45,333.4	47,043.0
II. Government Nonbank Financial Institutions									
Net foreign assets	--	--	--	--	--	--	--	--	--
Net domestic assets	12,398.8	14,247.2	16,062.2	16,845.7	17,541.6	18,146.1	17,742.0	19,953.2	20,784.7
Credit to private sector	7,631 6	8,824.2	9,599.0	10,088.3	10,480.7	10,477.2	11,215.9	11,581.0	12,242.9
Investments	1,655.1	2,045.2	3,554.7	3,542.3	3,794.2	4,462.5	3,817.5	4,692.4	5,209.3
Other	3,112.1	3,377.6	2,908.5	3,215.1	3,266.7	3,206.4	2,708.6	3,679.8	3,332.5
Liabilities	12,398.8	14,247.2	16,062.2	16,845.7	17,541.6	18,146.1	17,742.0	19,953.2	20,784.7
Deposits	--	--	--	--	--	--	--	--	--
Other	12,398.8	14,247.2	16,062.2	16,845.7	17,541.6	18,146.1	17,742.0	19,953.2	20,784.7

Table XVII (continued). Philippines. Summary Account of Nonbank Financial Intermediaries, 1977-81

(In millions of Philippine pesos)

	1977 Dec.	1978 Dec.	1979 Dec.	1980 Mar.	1980 June	1980 Sept.	1980 Dec.	1981 Mar.	1981 June
III. Rural (nondemand) and Savings Banks									
Net foreign assets	--	--	--	--	--	-30.3	-83.3	100.0	290.2
Net domestic assets	5,441.7	7,154.6	9,126.5	9,426.7	9,784.2	10,255.7	11,598.3	11,794.6	12,248.1
Credits to private sector	4,095.8	5,086.2	6,855.1	7,155.7	7,513.3	7,850.4	8,462.1	8,736.7	8,899.8
Investments	646.4	1,092.2	939.9	958.2	914.5	979.2	1,141.0	1,176.6	1,234.4
Other	699.5	976.2	1,331.5	1,312.8	1,356.4	1,426.1	1,995.2	1,881.3	2,113.9
Liabilities	5,441.7	7,154.6	9,126.5	9,426.7	9,784.2	10,225.4	11,515.0	11,894.6	12,538.3
Deposits	3,316.6	4,568.5	5,845.5	6,015.5	6,223.8	6,384.3	6,928.9	7,336.1	7,725.9
Other	2,125.1	2,586.1	3,280.8	3,411.2	3,560.4	3,841.1	4,586.1	4,558.5	4,812.4
IV. Development and Specialized Government Banks 1/									
Net foreign assets	-2,461.7	-2,017.1	-316.3	-375.4	-137.8	-664.4	-306.0	-275.2	-287.7
Net domestic assets	18,192.0	20,105.3	23,100.9	23,934.0	25,201.5	26,750.9	28,090.0	29,090.6	31,274.4
Credit to private sector	10,381.6	11,025.0	12,651.6	13,146.1	13,725.0	14,268.9	14,992.8	16,063.1	16,369.1
Investments	4,255.7	4,801.1	5,359.0	5,644.4	6,076.6	6,868.1	7,047.8	7,007.5	[illegible]
Other	3,554.7	4,279.2	5,090.3	5,143.5	5,399.9	5,613.9	6,049.4	6,020.0	[illegible]
Liabilities	15,730.3	18,088.2	22,784.6	23,558.6	25,063.7	26,086.5	27,784.0	28,815.4	30,986.7
Deposits	3,801.7	4,442.5	6,384.1	6,634.2	6,967.7	7,964.0	8,085.0	8,393.9	9,018.6
Loans payable	5,130.4	6,567.3	8,112.5	8,487.2	9,115.3	9,278.9	10,041.6	10,614.1	11,222.8
Share capital	4,679.2	5,134.7	5,923.5	6,047.1	6,385.5	6,654.8	7,074.8	7,295.6	7,591.5
Other	2,111.0	1,943.7	2,364.5	2,390.1	2,595.2	2,188.8	2,582.6	2,511.8	3,153.8

Table XVII (concluded). Philippines: Summary Account of Nonbank Financial Intermediaries, 1977-81

(In millions of Philippine pesos)

	1977	1978	1979	1980				1981	
	Dec.	Dec.	Dec.	Mar.	June	Sept.	Dec.	Mar.	June
V. Private Nonbank Financial Institutions									
Net foreign assets	--	--	--	--	--	--	--	--	--
Net domestic assets	21,275.9	24,867.2	20,544.5	23,580.9	24,442.0	25,076.1	26,053.8	26,130.3	26,329.2
Mortgages	8,361.4	9,902.6	7,167.0	9,927.6	10,290.0	10,439.4	10,981.2	10,597.9	11,076.5
Investments	7,240.1	8,473.8	7,315.3	8,465.5	8,774.7	9,240.8	9,357.1	9,545.6	9,046.1
Other	5,674.4	6,490.8	6,062.2	5,187.8	5,377.3	5,395.9	5,715.5	5,986.8	6,206.6
Liabilities	21,275.9	24,867.2	20,544.5	23,580.9	24,442.0	25,076.1	26,053.8	26,130.3	26,329.2
Deposits	19.7	25.4	32 3	33.1	32.0	37.9	40.2	42.3	42.3
Share capital	6,429.7	7,437.1	8,450.9	6,791.3	7,039.3	7,303.9	7,515.4	7,778.1	7,994.8
Other	14,826.5	17,404.7	12,061.3	16,756.5	17,370.7	17,734.3	18,498.2	18,309.9	18,292.1
Of which:									
Deposit substitutes	...	...	8,907.8	9,374.6	10,835.4	11,455.3	11,327.8	9,576.9	9,150.7
Emergency advances from Central Bank	...	...	...	...	...	...	...	1,492.7	1,745.2

Source: Data supplied by the Philippine authorities.

1/ Excludes the Development Bank of the Philippines and the Land Bank of the Philippines.

Table XVIII. Philippines: Rediscount Policy of Central Bank, 1980-81

	Loan value		Rediscount rate		Maximum Lending rate 1/	
	12/31/80	12/31/81	12/31/80	12/31/81	12/31/80	12/31/81
	(In per cent)		(In per cent per annum)			
Eligible paper with original maturity of one year						
Supervised credits 2/	100.0	100.0	1.0	3.0	12.0	12.0
Nonsupervised credits 3/	80.0	80.0	3.0	8.0	12.0	14.0
Small- and medium-scale industries	80.0	80.0	3.0	8.0	12.0	14.C
Export industries						
Nontraditional	100.0	80.0	4.0	3.0	10.0	12.0
Traditional 4/	80.0	80.0	6.0	8.0	12.0	14.0
Special programs 5/	80.0-100.0	100.0	4.0-3.0	3.0	10.0-6.0	6.0
Eligible paper with original maturity of more than one year						
Supervised credits 2/	100.0	100.0	1.0	3.0	12.0	12.0
Other						
Two-year or less original maturity	80.0	80.0	10.0	10.0	16.0	16.0
More than two-year original maturity	80.0	80.0	12.0	Lendin rate minus 6%	18.0	No ceilin

Source: Data supplied by the Central Bank of the Philippines.

1/ Includes service charges.
2/ Includes food production programs (i.e., rice), agrarian reform, cotton, and certain cottage industries.
3/ Includes basic food production (milling of rice and corn).
4/ Traditional exports are defined as commodities where export value in 1979 was US$10 million or more. Prior to June 26, 1981 definition was export value in 1968 of US$5 million or more. All other commodities are treated as nontraditional exports.
5/ Includes National Grain Authority procurement of corn, sorghum, soybeans, and mango, Food Terminal, Inc., and Grains Quedan.

Table XIX. Philippines: Loans Extended by Central Bank to Commercial Banks, 1979-81

(In millions of Philippine pesos)

	1979				1980				1981			
	I	II	III	IV	I	II	III	IV	I	II	III	IV
Total 1/	4,649.4	4,626.5	5,117.3	5,815.2	6,373.3	6,695.6	7,458.7	9,720.6	9,027.6	10,002.7	10,659.3	11,963.9
Rediscount facilities	4,464.7	4,458.3	4,776.1	5,456.1	6,099.5	6,319.2	7,122.5	9,078.6	8,549.5	9,326.1	10,153.8	11,382.6
Agriculture 2/	915.7	715.1	642.2	972.9	1,050.5	992.6	1,217.8	1,246.0	1,387.2	1,331.6	1,643.4	1,408.8
Mining	14.4	6 9	14.4	--	--	--	--	--	--	--	--	--
Exports 3/	2,838.3	3,103.0	3,307 4	3,442.8	4,002.9	3,845.9	4,385.6	6,317.5	5,715.9	6,391.5	6,702.3	5,845.9
Emergency and special credits	575.7	588.5	664.0	719.9	713.3	927.4	910.2	839.9	872.0	1,084.9	1,241.0	3,263.7
Other 4/	130.7	44.8	148.1	320.8	322.8	553.3	608.9	675.2	574.4	518.1	567.1	784.2
Repurchase agreement	184.7	168.2	341.2	358.8	273.8	376.4	336.2	642.0	478.1	676.6	505.5	581.3
Regular	30.5	14.0	187.0	204.6	119.6	173.0	110.0	413.7	254.1	459.5	290.4	237.7
Hotel financing	124.4	124.2	124.2	124.2	124.2	173.4	180.2	185.3	181.0	174.1	169.7	168.4
Special financing	30.0	30.0	30.0	30.0	30.0	30.0	46.0	43.0	43.0	43.0	41.4	38.7
Overnight lending	--	--	--	--	--	--	--	--	--	--	4.0	136.5

Source: Data supplied by the Central Bank of the Philippines.

1/ Excludes overdrafts and consolidated foreign borrowing.
2/ Consists of loans for rice and corn production.
3/ Includes facilities for traditional and nontraditional exports, sugar, and NASUTRA.
4/ Includes loans for agricultural production such as fishing, poultry, orchards, tobacco, palay trading, and small-scale industries.

Table XX. Philippines: Export Indices 1978-81
(1978 = 100)

	1978	1979	1980	Est. 1981
		(Volume indices)		
Principal primary products	100.0	90.0	97.6	101.4
Of which: Coconut products	100.0	76.5	85.5	95.5
Sugar and products	100.0	85.0	160.5	109.4
Forest products	100.0	97.7	76.4	86.1
Copper concentrates	100.0	117.1	127.6	121.6
Nontraditional manufactures	100.0	110.1	143.7	157.8
Other nontraditional exports	100.0	129.8	156.1	147.4
Other	100.0	103.9	104.2	179.7
Total exports	100.0	101.1	125.8	129.5
		(Unit value indices)		
Principal primary products	100.0	143.4	143.2	134.1
Of which: Coconut products	100.0	147.8	105.4	93.0
Sugar and products	100.0	108.0	192.2	258.8
Forest products	100.0	152.8	167.0	141.5
Copper concentrates	100.0	150.2	170.8	148.0
Nontraditional manufactures	100.0	128.2	135.2	139.3
Other nontraditional exports	100.0	107.6	109.5	113.8
Other	100.0	129.0	159.6	129.5
Total exports	100.0	132.9	134.3	133.3
		(Value indices)		
Principal primary products	100.0	129.1	139.7	136.0
Of which: Coconut products	100.0	113.1	90.1	88.8
Sugar and products	100.0	91.8	308.4	283.1
Forest products	100.0	149.3	127.6	121.9
Copper concentrates	100.0	175.9	218.0	180.0
Nontraditional manufactures	100.0	141.1	194.4	219.8
Other nontraditional exports	100.0	139.7	171.0	167.8
Other	100.0	134.0	166.3	232.7
Total exports	100.0	134.3	169.0	172.6

Source: Data provided by the Philippine authorities.

Table XXI . Philippines: Composition of Exports, 1977-81

	1977	1978	1979	1980	Prel. 1981
	(In millions of U.S. dollars)				
Principal primary products	1,829	1,704	2,199	2,524	2,318
Coconut products	(763)	(910)	(1,029)	(820)	(808)
Sugar and products	(535)	(216)	(240)	(659)	(603)
Forest products	(263)	(328)	(490)	(500)	(457)
Copper concentrates	(268)	(250)	(440)	(545)	(450)
Nontraditional manufacturers	660	1,028	1,458	1,920	2,272
Of which: Garments	(246)	(327)	(405)	(500)	(610)
Electrical and electronic equipment and components	(116)	(244)	(397)	(643)	(780)
Other nontraditional exports 1/	172	177	246	278	238
Other 2/	490	516	698	1,066	1,082
Total	3,151	3,425	4,601	5,788	5,910
	(In per cent share)				
Principal primary products	58.0	49.8	47.8	43.6	39.2
Coconut products	(24.2)	(26.6)	(22.4)	(14.2)	(13.7)
Sugar and products	(17.0)	(6.3)	(5.2)	(11.4)	(10.2)
Forest products	(8.3)	(9.6)	(10.6)	(8.6)	(7.7)
Copper concentrates	(8.5)	(7.3)	(9.6)	(9.4)	(7.6)
Nontraditional manufactures	20.9	30.0	31.7	33.2	38.4
Of which: Garments	(7.8)	(9.5)	(8.8)	(8.6)	(10.3)
Electrical and electronic equipment and components	(3.7)	(7.1)	(8.6)	(11.1)	(13.2)
Other nontraditional exports 1/	5.5	5.2	5.3	4.8	4.0
Other 2/	15.6	15.0	15.2	18.4	18.4
Total	100.0	100.0	100.0	100.0	100.0

Source: Data provided by the Philippine authorities.

1/ Mainly coffee, rice, and iron ore.
2/ Mainly fruits and vegetables, gold, nickel, marine products, unmanufactured tobacco, and abaca fibers.

Table XXII. - Philippines: Import Indices, 1978-81
(1978 = 100)

	1978	1979	1980	Est. 1981
		(Volume indices)		
Capital goods	100.0	110.8	115.6	112.5
Raw materials and intermediate goods	100.0	109.4	116.6	110.4
Consumer goods	100.0	109.6	122.4	122.4
Subtotal: non-oil imports	100.0	110.8	117.3	113.2
Petroleum and petroleum products	100.0	99.2	99.0	101.9
Total imports	100.0	109.2	111.8	108.5
		(Unit value indices)		
Capital goods	100.0	114.1	121.6	129.6
Raw materials and intermediate goods	100.0	118.5	129.2	139.1
Consumer goods	100.0	105.9	119.4	143.5
Subtotal: non-oil imports	100.0	115.3	124.9	135.5
Petroleum and petroleum products	100.0	136.5	219.6	259.2
Total imports	100.0	117.7	144.3	162.6
		(Value indices)		
Capital goods	100.0	126.4	140.6	145.8
Raw materials and intermediate goods	100.0	129.6	150.7	153.5
Consumer goods	100.0	116.1	146.2	175.6
Subtotal: non-oil imports	100.0	126.8	146.5	153.4
Petroleum and petroleum products	100.0	135.4	217.5	264.0
Total imports	100.0	128.6	161.3	176.4

Source: Data provided by the Philippine authorities.

Table XXIII. Philippines: Composition of Imports, 1977-81

	1977	1978	1979	1980	Prel. 1981
			(In millions of U.S. dollars)		
Petroleum and petroleum products	984	1,015	1,371	2,226	2,713
Non-oil imports	2,931	3,717	4,771	5,501	5,687
Capital goods	(1,077)	(1,401)	(1,785)	(1,986)	(2,034)
Raw materials and intermediate goods	(1,470)	(1,899)	(2,489)	(2,877)	(2,892)
Consumer goods	(384)	(417)	(497)	(638)	(761)
Total	3,915	4,732	6,142	7,727	8,400
			(In per cent share)		
Petroleum and petroleum products	25.1	21.4	22.3	28.8	32.3
Non-oil imports	74.9	78.6	77.7	71.2	67.7
Capital goods	(27.6)	(29.6)	(29.1)	(25.7)	(24.2)
Raw materials and intermediate goods	(37.5)	(40.1)	(40.5)	(37.2)	(34.4)
Consumer goods	(9.8)	(8.9)	(8.1)	(8.3)	(9.1)
Total	100.0	100.0	100.0	100.0	100.0

Source: Data provided by the Philippine authorities.

Table XXIV. Philippines: Direction of Trade, 1977-80

(In per cent)

	Exports, f.o.b.				Imports, f.o.b.			
	1977	1978	1979	1980	1977	1978	1979	1980
United States	35.3	33.8	30.1	27.4	20.4	21.0	22.8	23.1
Japan	23.1	23.9	26.1	26.5	24.9	27.2	22.8	19.8
European Economic Community	18.5	18.5	20.2	16.9	12.0	12.6	13.9	10.7
Of which: Germany	(4.4)	(4.2)	(4.9)	(4.4)	(3.4)	(3.9)	(4.5)	(4.2)
Netherlands	(8.9)	(8.2)	(7.8)	(6.3)	(1.2)	(1.5)	(1.6)	(1.5)
United Kingdom	(2.2)	(2.6)	(3.0)	(2.5)	(3.7)	(3.6)	(3.2)	(2.3)
France	(1.4)	(1.6)	(2.7)	(1.6)	(2.0)	(2.1)	(2.8)	(1.2)
Middle East	1.0	1.7	1.3	2.0	18.1	14.9	15.7	21.1
Of which: Saudi Arabia	(0.4)	(0.6)	(0.4)	(0.5)	(8.3)	(5.6)	(6.0)	(10.3)
Kuwait	(0.1)	(0.1)	(--)	(0.1)	(3.5)	(3.4)	(4.6)	(5.3)
Iraq	(--)	(0.5)	(0.4)	(0.8)	(3.0)	(3.1)	(3.0)	(2.5)
ASEAN	4.0	6.1	4.1	6.5	6.7	5.8	5.9	6.3
Of which: Indonesia	(0.7)	(2.6)	(1.0)	(1.8)	(3.9)	(3.1)	(3.0)	(2.3)
Malaysia	(0.9)	(1.1)	(1.2)	(1.6)	(1.6)	(1.2)	(1.5)	(2.0)
Singapore	(2.1)	(2.1)	(1.4)	(2.0)	(0.8)	(1.1)	(1.3)	(1.6)
Australia	1.9	2.2	2.0	1.7	4.3	3.5	3.4	2.8
Hong Kong	1.6	2.6	3.4	3.3	1.6	2.3	2.5	2.5
South Korea	0.1	1.9	3.1	3.5	0.6	1.1	1.5	1.8
USSR	4.1	1.2	1.8	3.3	0.1	0.1	0.1	0.3
China, Peoples' Republic of	3.4	1.4	1.1	0.8	2.0	2.4	2.0	2.7
Other	7.0	6.7	6.8	8.1	9.3	9.1	9.4	8.9
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Data provided by the Philippine authorities.

Table XXV. Philippines: Capital Account of the Balance of Payments, 1977-81

(In millions of U.S. dollars)

	1977	1978	1979	1980	1981
Capital movement	962	1,082	997	1,699	1,926
Direct investment (net)	216	171	99	45	392
Nuclear power project (net)	-13	-12	11	43	43
Exceptional financing (net)	19	59	60	52	200
Trust Fund	(19)	(59)	(60)	(52)	(--)
IBRD Structural Adjustment Loan	(--)	(--)	(--)	(--)	(200)
Other medium- and long-term loans (net)	556	749	951	956	957
Other short-term capital (net)	411	263	80	765	202
Monetization of gold	--	32	41	128	400
Allocation of SDRs	--	--	28	29	27
Errors and omissions	-227	-180	-273	-319	-295

Source: Data provided by the Philippine authorities.

Table XXVI. Philippines: Net International Reserves of the Banking System, 1977-81

	December 31				
	1977	1978	1979	1980	1981
	(In millions of U.S. dollars)				
Net international reserves	243	153	-426	-778	-1,265
Gross reserves	2,263	3,195	3,731	5,059	5,315
Central Bank	1,525	1,883	2,423	3,155	2,707
Commercial banks	738	1,312	1,308	1,904	2,608
Reserve liabilities	2,021	3,042	4,157	5,837	6,580
Central Bank	602	689	1,179	2,150	2,406
Commercial banks	1,419	2,353	2,978	3,687	4,174
Of which: FCDU deposits	(1,160)	(1,878)	(2,402)	(3,077)	(3,049)

Source: Data provided by the Philippine authorities.

Table XXVII. Philippines: Projected Debt Service Payments on Medium- and Long-Term Debt, 1982-87 1/

(In millions of U.S. dollars)

	1982	1983	1984	1985	1986	1987
Service payments on debt outstanding as of September 30, 1981						
Public sector	1,079	1,222	1,281	1,320	1,288	996
Interest 2/	665	692	673	600	483	355
Amortization	414	530	608	720	805	641
Private sector	682	669	641	652	498	361
Interest 2/	324	298	269	234	169	113
Amortization	358	371	372	418	329	248
Total	1,761	1,891	1,922	1,972	1,786	1,357
Service payments on debt approved but not drawn as of September 30, 1981 3/						
Public sector	120	157	205	268	475	605
Interest 2/	64	91	115	134	183	209
Amortization	56	66	90	134	292	396
Private sector	141	197	242	248	271	281
Interest 2/	87	108	108	96	98	96
Amortization	54	89	134	152	173	185
Total	261	354	447	516	746	886
Total service payments	2,022	2,245	2,369	2,488	2,532	2,243
Interest	1,140	1,189	1,165	1,064	933	773
Amortization	882	1,056	1,204	1,424	1,599	1,470

Source: Data provided by Philippine authorities.

1/ Excludes IMF.
2/ Interest on floating rate loans assumed to be 15 per cent per year.
3/ Including debt contracted but undisbursed and debt approved but not yet contracted.

Table XXVIII. Philippines: External Debt Service Ratios, 1977-81, as Defined Statutorily

(In millions of U.S. dollars)

	1977	1978	1979	1980	1981
Total foreign receipts 1/	5,289	5,593	6,741	7,874	9,203
Current receipts	3,258	3,814	4,371	5,562	7,093
Capital receipts	2,031	1,779	2,370	2,312	2,110
Debt service payments 2/	727	1,007	1,253	1,473	1,753
Debt service ratios per Statute 3/ (in per cent)	13.7	18.0	18.6	18.7	19.0

Source: Data provided by Philippine authorities.

1/ As defined under External Debt Service Limitation Law (RA. 6142).
2/ Includes amortization and interest payments on short-, medium- and long-term external debt.
3/ Limit for debt service ratios as defined by Statute is 20 per cent.

Table XXIX. Philippines: Structure of Medium- and Long-Term External Debt (Disbursed), 1977-80 1/

	1977	1978	1979	1980
	(In millions of U.S. dollars; and end of period)			
Total	5,004	6,200	7,137	8,554
By creditor				
Suppliers' credits	1,203	1,172	862	1,089
Financial institutions	2,116	2,689	3,663	4,457
Bonds	501	776	890	966
Multilateral loans	579	761	959	1,222
Bilateral loans	605	801	763	820
By maturity				
Over 1 year up to and including 5 years	308	258	181	168
Over 5 years up to and including 12 years	2,903	3,514	3,984	4,802
Over 12 years up to and including 15 years	362	475	513	)
Over 15 years	1,431	1,952	2,459	) 3,584
By interest rate				
No interest	55	78	74	...
Over 0 per cent up to and including 3 per cent	197	244	412	...
Over 3 per cent up to and including 6 per cent	582	747	719	...
Over 6 per cent up to and including 9 per cent	2,207	2,941	3,284	...
Over 9 per cent	272	283	294	...
Floating rate	1,691	1,906	2,354	3,186
	(In per cent share)			
Total	100.0	100.0	100.0	100.0
By creditor				
Suppliers' credits	24.0	18.9	12.1	12.7
Financial institutions	42.3	43.4	51.3	52.1
Bonds	10.0	12.5	12.5	11.3
Multilateral loans	11.6	12.3	13.4	14.3
Bilateral loans	12.1	12.9	10.7	9.6

Source: Data provided by the Central Bank of the Philippines.

Table XXIX. (concluded) Philippines: Structure of Medium- and Long-Term External Debt (Disbursed) 1977-80 1/

	1977	1978	1979	1980
By maturity				
Over 1 year up to and including 5 years	6.2	4.2	2.5	2.0
Over 5 years up to and including 12 years	58.0	56.7	55.8	56.1
Over 12 years up to and including 15 years	7.2	7.7	7.2)	
Over 15 years	28.6	31.5	34.5)	41.9
By interest rate				
No interest	1.1	1.3	1.0	...
Over 0 per cent up to and including 3 per cent	3.9	3.9	5.8	...
Over 3 per cent up to and including 6 per cent	11.6	12.1	10.1	...
Over 6 per cent up to and including 9 per cent	44.1	47.4	46.0	...
Over 9 per cent	5.5	4.6	4.1	...
Floating rate	33.8	30.7	33.0	37.2

Source: Data provided by the Philippine authorities.

1/ Original maturity over 1 year, excludes IMF credit.

Table XXX. Philippines: Exchange Rate Movements, 1975-81 1/

	Peso/US$ rate	Peso/SDR rate	Trade Weighted Index 2/ Nominal	Real 3/
1975	7.25	8.80	100.0	100.0
1976	7.44	8.59	99.3	97.6
1977	7.40	8.64	96.1	94.6
1978	7.37	9.22	86.7	86.8
1979	7.38	9.53	88.1	96.9
1980	7.51	9.78	86.7	100.8
1981	7.90	9.32	85.6	102.5
1978 I	7.37	9.00	90.5	90.3
II	7.36	9.03	88.6	87.2
III	7.36	9.31	84.1	84.5
IV	7.37	9.56	83.5	85.4
1979 I	7.38	9.51	86.1	88.7
II	7.38	9.41	88.5	96.3
III	7.37	9.60	87.8	99.3
IV	7.38	9.61	90.1	103.1
1980 I	7.42	9.67	90.5	104.2
II	7.49	9.72	86.6	99.6
III	7.55	9.97	85.1	99.5
IV	7.58	9.75	84.5	99.9
1981 I	7.68	9.54	84.6	99.8
II	7.86	9.29	86.1	101.1
III	7.96	9.03	87.8	106.6
IV	8.10	9.41	83.9	102.5
1981 June	7.95 4/	9.18 4/	86.7	102.3
July	7.95	9.03	89.0	108.3
August	7.96	8.93	87.6	106.5
September	7.99	9.14	86.9	104.9
October	8.06	9.31	86.0	104.1
November	8.11	9.46	82.6	100.6 5/
December	8.20	9.54	83.0	102.7 5/

Sources: IMF, International Financial Statistics and staff calculations.

1/ All data are period averages.
2/ A decrease in the number indicates a depreciation.
3/ Adjusted for changes in relative consumer prices.
4/ End of period.
5/ Based on real exchange rate movements of a smaller basket of currencies, which comprise 87 per cent of the larger basket.

Tariffs and Fiscal Incentives

1. Tariffs

In early 1981, the Philippine authorities began a comprehensive reform of the external tariff to be implemented over the four-year period 1981-85. The objectives of the reform are to increase efficiency and international competitiveness of Philippine industry by lowering the overall level of protection and having more uniform tariff rates across and within sectors. Under the reform, overall effective rates of protection for the economy will be reduced from 36 per cent to 23 per cent and for the manufacturing sector from 44 per cent to 29 per cent.

The first phase of the reform, involving a reduction in nominal peak rates (i.e., rates in excess of 50 per cent) to no more than 50 per cent, was implemented in two steps: on January 1, 1981, and on January 1, 1982. In January 1981, a program for phased realignment of tariff rates in 14 major industry subsectors over the next four years was introduced.1/ These 14 industry subesectors are: food processing; textiles and garments; leather and leather products; pulp and paper; iron and steel; cement; automotive; wood and wood products; motorcycles; ceramics/glass; electrical/electronics; domestic appliances; machineries; and furniture. In August 1981, after a review of the remaining line items of the Tariff Code, a four-year program for phased realignment of tariff rates was introduced for the following ten industry subsectors: agricultural and forest products; pharmaceuticals, cosmetics and perfumery; detergents, miscellaneous chemical products, basic industrial chemicals, fertilizers and pesticides; miscellaneous manufactures; sundries; railway and air transport; basic nonferrous metal, mining and quarrying; petroleum refinery; plastic, rubber and rubber products; and photographic, cinematographic and optical products.2/ The realignment of tariff rates, has to date, been implemented as scheduled. While most of the modifications in tariff rates involve reductions, for certain items the new tariff rates are higher, especially for capital goods which have had low rates and/or which the authorities believe can be produced economically in the Philippines. Typical increases are from rates of 10 per cent and 20 per cent to 20 per cent and 30 per cent, respectively.

The impact of the tariff reform on government revenue is difficult to assess. In the budget for 1981 the revenue loss was estimated at ₱ 120 million, but this estimate was later revised upward to ₱ 400 million. For 1982, the authorities estimate an additional revenue loss of ₱ 180 million, resulting from the tariff changes implemented in January 1982. The authorities have also prepared "high" and "low"

1/ The tariff changes involving reductions in nominal peak rates and realignment of tariff rates in these 14 major industry subsectors are embodied in Executive Orders 609 and 632A which took effect on January 1, 1981.

2/ The tariff changes in these ten industry subsectors are embodied in Executive Order 706 which took effect on August 16, 1981.

estimates of the impact on revenue for 1985, after the completion of the reform, depending on alternative assumptions about the responsiveness of domestic supply and demand to changes in tariffs. According to these estimates, government revenue will remain unchanged (low estimate) or increase by 5 per cent (high estimate) as a result of the tariff reform. The low revenue estimate assumes that imports will increase by 5 per cent in value terms, while the high revenue estimate is based on a 14 per cent increase in the value of imports.

2. Fiscal incentives

The widespread fiscal incentives system (mainly in the form of tax concessions and exemptions as well as tax credits and subsidies) has had, over the years, a significant effect on the structure of industrial production.1/ Although the Investment Incentives Act of 1967 and the Export Incentives Act of 1970 were substantially modified in subsequent years, the system of fiscal incentives has continued to suffer from a number of shortcomings. First, it has had a capital-cheapening effect, encouraging an industry mix and a choice of technology that were excessively capital intensive. Second, to the extent that the investment incentives *de facto* have discriminated against small- and medium-size enterprises and labor-intensive industry, they have indirectly discouraged regional dispersal since these industries are ones that might be expected to locate outside Metro Manila. Third, there appear to have been substantial costs in terms of revenue foregone.

The authorities are currently in the process of finalizing a major reform of the system of fiscal investment and export incentives which would alleviate some of the present system's shortcomings. Thus, the number of incentives would be sharply reduced, and incentives would focus more clearly on achieving such specific objectives as employment creation, export promotion, and regional dispersal of industry, and would be more closely linked to performance. The costs of the new system of fiscal incentives are difficult to assess; preliminary estimates indicate that the amount of revenue foregone will be reduced, but great uncertainty is attached to any such estimates. The authorities expect that the new system will become effective from January 1, 1983; for a transition period, however, the present system will continue to operate for certain incentives.

1/ A detailed review of the system of fiscal incentives is presented in *Philippines--Use of Fund Resources--Supplementary Material*, SM/78/132.

Development Plan, 1983-87

The major quantitative macroeconomic targets of the Five-Year Development Plan (1983-87) are set out in the table below. In addition to the targets indicated in the table, it is projected that GNP at current prices will be ₱ 775 billion in 1987, resulting in a per capita income of ₱ 13,680, compared to ₱ 5,471 in 1980. The inflation rate is projected to average around 9 per cent yearly during the Plan period. The average annual growth rate for employment is projected to be 3.7 per cent, while overseas employment is expected to reach 500,000 by 1987, compared to 200,000 in 1981.

Real GNP is projected to grow by 6.5 per cent on average in 1983-87, assuming moderate world economic recovery and structural adjustment measures. Real private consumption expenditure is projected to increase at a faster pace (5.4 per cent) than in recent years because of higher incomes, moderate price increases, and liberalized imports of consumer goods. Gross domestic capital formation is projected to increase by 7 per cent in real terms during the Plan period, somewhat higher than the growth achieved in recent years. Export volume is expected to rise by 10 per cent per annum; the share of nontraditional manufactured exports to total exports is expected to increase significantly.

During the Plan period, the industrial sector is expected to be the leading growth sector. Manufacturing output is projected to increase by 7.9 per cent, largely attributed to the Government's industrial restructuring program. The Plan aims at industrial development along the lines of comparative advantage, which would imply primarily labor-intensive industries, together with selected capital-intensive industries based on domestic raw materials. Mining and quarrying output is projected to grow by 6.6 per cent per annum, reflecting higher world prices, development of new mining areas, and increased processing capacity of local firms. The growth rate of the agricultural sector is projected at 5 per cent per annum, almost the same growth as the previous Plan period. Agricultural expansion will be sustained by increased productivity. It is estimated that 2.0 million hectares would be irrigated in 1987, compared to 1.4 million hectares in 1982. Rice cultivation, which is largely based on irrigated land, is projected to increase by 3.7 per cent annually during the Plan period. Emphasis will also be placed on the development of nontraditional foodcrops.

Philippines: Targeted Plan Growth Rates

(At constant prices)

	Targeted growth rate, 1983-87 (Per cent per annum)
Expenditures on gross national Product	
Personal consumption	5.4
Government consumption	6.8
Gross domestic capital formation	6.9
Fixed capital formation	7.1
Construction	7.3
Of which: Government	5.9
Private	8.5
Durable equipment	6.9
Increase in stocks	-5.2
Exports of goods and nonfactor services	9.9
Imports of goods and nonfactor services	7.4
Gross national product	6.5
Industrial origin of gross national product	
Agriculture, fishery, and forestry	5.0
Industry	7.7
Of which: Mining and quarrying	6.6
Manufacturing	7.9
Construction	7.3
Electricity, gas, and water	8.9
Services	6.1

Source: NEDA, Philippine Development Plan, 1983-87.

Foreign Currency Deposit and Offshore Banking Systems--A Short History

The financial system of the Philippines is relatively well developed and incorporates commercial banks, thrift banks, specialized banks such as the Development Bank of the Philippines and the Land Bank of the Philippines, investment houses, finance companies, and pension and insurance funds. One element of this complex financial structure is the foreign currency operations of Foreign Currency Deposit Units (FCDUs) and Offshore Banking Units (OBUs). These institutions were created to channel offshore funds to the Philippines for lending operations approved by the Central Bank.

In 1970, the monetary authorities of the Philippines under Monetary Board Resolution 1104 and Central Bank Circular 304 permitted residents and nonresidents to open foreign exchange accounts in authorized local commercial banks. Foreign currency could be deposited into demand, savings, or time accounts. One objective of this change was to provide incentives for residents living overseas, particularly workers that held foreign exchange in bank accounts abroad, to deposit foreign currency in the Philippines. Toward this goal, the regulation provided that the withdrawal of funds could take place without restrictions other than those agreed by the customer and the bank (e.g., as to maturity); that any future changes in Central Bank regulations would not apply to existing deposits; and that numbered accounts were permitted. Usury ceilings were not applicable to foreign currency deposits or loans. The circular did not alter the surrender requirement on exports and inward receipts of current transactions but it did exempt foreign exchange deposited by residents in an authorized account from the surrender requirement. A reserve requirement of 15 per cent on which the Central Bank pays interest was imposed on these foreign currency deposits. The remainder of foreign currency deposits could be redeposited abroad or with the Central Bank, lent to domestic residents in foreign exchange, or swapped with the Central Bank to fund peso loans. Any loan to a domestic borrower (either in domestic or foreign currency) must receive prior approval of the Central Bank through MEDIAD just as all external borrowings do. Loans are made to firms that are export-oriented as defined by Central Bank regulations or are registered with the Board of Investments under the Export Incentives Act (R.A. No. 6135). Except for foreign exchange converted under a swap arrangement, deposit liabilities must be matched with an asset in the same foreign currency; thus, no exposure to risk arising from exchange rate changes is permitted (i.e., no open foreign exchange position). To ensure that adequate foreign exchange cover is provided, foreign currency loans are limited to short-term maturities which are readily marketable.

In 1972, to provide a firmer legal basis for the operation of foreign currency accounts, legislation was passed (R.A. No. 6426--Foreign Currency Deposit Act of the Philippines) which formalized the earlier decision of the Monetary Board--in particular, the withdrawal privileges, secrecy provisions, and operating rules discussed above. Eligibility requirements for banks to accept foreign currency deposits were also formalized and included: paid-in capital of ₱ 20 million; ratio of capital account to total risk assets of not less than 15 per cent; and no suspension of lending operations in the previous six months. Banks already operating under Central Bank Circular (CBC) No. 304 were authorized automatically. While banks under CBC 304 were permitted to "pay interest in foreign currency or such deposits outside the regulatory ceilings" under the new Act they were limited to the maximum provided by law. The Monetary Board implemented the new Act by issuing CBC No. 343, and institutions authorized to open a FCDU were termed "343" banks. After authorization by the Central Bank, a commercial bank only had to create a new entry in its balance sheet to accommodate foreign exchange accounts in order to go into business.

In late 1976, further efforts were made to attract foreign exchange resources to the Philippines and to promote Manila as a regional financial center. Presidential Decree (PD) No. 1034 established offshore banking units (OBUs) to strengthen the linkage between the Philippines and foreign banking centers, create employment opportunities, and develop expertise in international finance, and enhance the flow of resources to the Philippines. The Monetary Board in CBC 546 (November 26, 1976) issued implementing regulations for the offshore banking system. Only banks organized outside of the Philippines are qualified to operate as an OBU and are required to show a sufficiently strong liquidity and net worth position as well as the necessary managerial and international banking skills. Typically these requirements would be met by a subsidiary or a branch of a major foreign international bank. An OBU is free to engage in normal banking functions with nonresidents and other OBUs in any currency other than Philippine pesos and is outside the regulatory framework of banks operating in the Philippines. Thus, an OBU is not restricted, as "343" banks are, by any usury law, reserve requirement, foreign exchange cover requirement, or limitation on loan maturities with nonresidents. Transactions by OBUs with residents fall into two broad categories--those made with Foreign Currency Deposit Banks (i.e., "343" banks) or the newly created Foreign Currency Deposit Unit (FCDU) and loans to residents which require prior Central Bank approval.

The OBUs were intended to be a convenient source of foreign exchange for the newly-created FCDUs which were an outgrowth of the foreign currency deposit banks. The Monetary Board under CBC No. 547 (November 26, 1976), which was issued the same day the OBU regulations were promulgated, expanded the operating authority of qualified banks under CBC No. 343. Specifically, banks with capital of at least ₱ 150 million and competence in conducting foreign currency transactions were eligible to apply for the expanded powers available under CBC No. 547, which included the authorization to maintain foreign currency accounts with OBUs and other FCDUs; the ability, with the prior approval of the Central Bank, to extend longer maturity foreign currency loans; invest in longer maturity foreign currency debt instruments whether readily marketable or not; borrow from nonresidents, OBUs and FCDUs; exemption from the 15 per cent reserve requirement; and inclusion of foreign currency deposits with OBUs and other FCDUs and foreign loans and investments of beyond one-year maturity in eligible assets, which satisfy the foreign exchange cover requirement that was initially maintained at 100 per cent.1/

The above described regulations have essentially established three tiers of institutions involved in foreign currency intermediation in the Philippines--the "343" banks, the "547" banks, (both of which are part of the foreign currency deposit system) and the OBUs. Within the foreign currency deposit system, the institutions that are less capitalized and less experienced in international markets are the "343" banks (11 operating institutions), while the "547" banks are major Philippine banks or foreign banks operating in the Philippines (29 operating institutions). Given that both "343" banks and "547" banks operate as part of the domestic banking system in the Philippines and their operations are merged into the balance sheets of their parent banks, the differing regulations reflect prudential restrictions to protect the financial system. Similarly, the regulatory freedom given to OBUs was combined with more stringent qualifications to protect the integrity of the offshore banking system, which has been limited to 21 operating OBUs.

Foreign banks, which can operate as either an OBU or FCDU, have greater freedom for their foreign exchange operations as an OBU but have greater access to the domestic market as a resident bank with a FCDU. In particular, as a domestic bank with a FCDU, they have the option of sourcing funds in Philippine pesos or foreign exchange for making loans in either Philippine pesos or foreign exchange with the exception that the Philippine peso cannot be used to make a foreign currency loan--a restriction that also applies to OBUs. Among the main attractions for a foreign bank in having an OBU is the closer ties to customers in the Philippines and that it can benefit from certain fiscal incentives that are available. The principal fiscal incentive is a lower income tax rate on interest payments paid by the borrower. This tax is a withholding tax paid by residents and is treated as the final tax.

The OBUs were designed to attract offshore resources to fund loans to resident enterprises in the Philippines either directly or indirectly through FCDUs and have largely functioned in that manner. Total assets of OBUs have risen from about $750 million at end-1977 to about $4,500 million at end-1981 for an average annual rate of expansion of over 50 per cent. However, most of this rapid growth occurred in the early years of the offshore banking system; thus, as the system has matured the rate of expansion has slowed, with total assets rising on the order of 10 to 15 per cent in 1981. Initially, offshore sources accounted for only 48 per cent of liabilities but that share had increased to nearly 85 per cent by end-1981. Similarly, the proportion of assets booked in the Philippines rose

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1/ Under CBC No. 623 (August 11, 1978) the percentage of the foreign currency liability that had to be matched in a foreign currency asset of the same currency was reduced to 70 per cent from 100 per cent. This would effectively permit the FCDU to have an open position in the exchange market equivalent to 30 per cent of its deposits.

from 51 per cent at the end of 1977 to about 76 per cent at the end of 1981. During the same period, the percentage of onshore assets lent directly with nonbank residents expanded to 45 per cent at end-1981 from 19 per cent at end-1977. About half of the interbank placements over this period were with FCDUs. Thus, the offshore banking system has succeeded in attracting offshore funds to the Philippines for predominantly onshore lending either directly or indirectly through FCDUs.

Data from the monetary accounts indicate that following a period of rapid growth from 1975 to 1980, which corresponds with the period of rapid expansion of OBUs, deposits in FCDUs did not increase in U.S. dollar terms in 1981, even though in peso terms FCDU deposits continued to rise due to the depreciation of the Philippine peso vis-a-vis the U.S. dollar. At end-1981, FCDU deposits were ₱ 25.0 billion (about $3.0 million), or about the same amount in U.S. dollar terms as at end-1980 although substantially greater than in December 1977 (₱ 8.6 billion or $1.2 billion). Available information indicates that in 1981, as in previous years, the bulk of these deposits (nearly 80 per cent) were interbank deposits (e.g., OBUs, banks in foreign financial centers), while about 15 per cent represented deposits of nonbank residents of the Philippines. These deposits were used to fund loans in foreign exchange to the private sector and the public sector, to make peso-denominated loans using pesos obtained from the Central Bank in a swap arrangement, to redeposit with the Central Bank, or to lend to the Central Bank as part of the latter's consolidated foreign borrowing program (CFBP). Excluding the proceeds of the CFBP which were onlent, about half of FCDU deposits were employed to make foreign currency loans to the private sector, while the proportion that went to the public sector was less than 5 per cent. The remainder of the foreign exchange was placed with the Central Bank as redeposits, medium- and long-term loans, as part of the CFBP, or through swap operations.

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