PHILIPPINE ECONOMIC POLICY AND THE 1997 ASIAN FINANCIAL CRISIS

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In the Philippines, a sound economic policy has remained an ideal, if not, an obsession for academicians and policy-makers alike especially in the Post – Martial law era – 1986 to the present. Given the development of the sociopolitical environment, there have been paradigmatic shifts in the approaches and perspectives on national well being and economic development. However, let it be recognized that challenges and conundrums continuously occur in both theory and policy. And as policy functions both as a preference for capturing the ideal conditions and a response to a given predicament, it is inevitable for policy debates to re-surface, be re-evaluated, and even, be reconsidered.

This paper attempts to inquire into the economic and political environment of the Philippines before and amidst the 1997 Asian currency crisis. Likewise, it attempts to look at the different policy responses made by the Philippines and to give an evaluation of its utility or contribution to “easing out the problem”. Structurally, the paper is divided into four parts: (1) The economic scenario before the Asian currency crisis; (2) The causes of the Asian currency crisis vis-à-vis the Philippine economy and the impact of the currency crisis on the local economy; (3) An assessment of the Policy responses; and (4) Issues, Prospects and New Challenges faced by the growing Philippine economy.

The Economic Scenario before the Asian Currency Crisis

Was there really a currency crisis that hit the Philippines? This has been the perennial question that preoccupied the minds of the various people who ventured into analyzing and studying the economic conditions in the post-1997 period.

Mixed impressions of the conditions prior to July 1997 have led to an ambiguity in the making of policy and it was very vital for the Philippine economic managers to prove that a crisis indeed existed.

There have been two different views on the Philippine economy prior to 1997. First, would be the point of view that the Philippine economy, after the 1986 Edsa uprising, was growing in a relatively positive pace (e.g. Sicat 1999). It has been noted that in 1996, the Gross National Product had an annual growth rate of more than 6%. There was also a noticeable 30% growth rate in
exports. There were also substantial increases in investment in both short-term portfolio investments and foreign direct investments. Foreign direct investments (FDIs) from 1992 to 1995 increased impressively with a rate of more than 80%.

More so, an improvement in the handling of foreign debt should be taken into consideration especially with the 1992 Brady debt deal – a policy that eased out the debt service burden making debt obligations equal to about 16% of the export receipts in 1994. It was all “smooth sailing” for the Philippine economy because the economic fundamentals were strong. Economic liberalization was taken seriously as a “backbone policy” translated to good export performance and an improving balance of trade. Nothing went wrong and everything was in place. Or so it seemed.

Contrary to the previous optimistic view, there were a few scholars and policymakers who believed that prior to this regional crisis in 1997, the Philippines was already experiencing economic problems of its own and the 1997 crisis merely highlighted the pathologies and deficiencies of policy contingencies and preparations.

The Philippines was already beset with economic problems. The economic fundamentals were not that strong to handle radical shifts in currency behavior brought about by trade. Structural reform in the financial sector was not yet complete after the onslaught of crony capitalism and structural transition from the period of martial law to the post-Cory Aquino administration. Add to this were events and national situations which directly affected economic stability — in 1990-1991 earthquake and Mt. Pinatubo eruption. There was also the Gulf war and the series of coup attempts in December of 1990. In 1997-1998, there was the El Nino phenomenon, which directly reduced agricultural output to about 6.5-6.7%.

Moreover, with the consideration of economic liberalization, the Philippines had a rather more-than-mediocre economic performance as compared to its Asian neighbors. Competitiveness was noticeably diminishing as indicated by comparative growth rates. The Philippines from 1988-1992 had a GDP growth rate of 3.2% as compared to its Asian developing counterparts of 7.4%. From 1993-1996, while the Philippines boasted of a 4.2% GDP growth rate, its counterparts enjoyed an 8.6% (de Dios, 17). Comparing the first semester of 1996 vs. 1995 and the first semester of 1997 vs. 1996, there have been deceleration in the growths of sectors: agriculture by .4%, industry by .8%, manufacturing by 1.7%, all rendering the GDP lower by 3% and the GNP lower by 1.6%.

There was an observable decline and general weakness in export performance, although it is also noteworthy to mention the stability of growth in the electronics, communication and transport equipment markets. Due to the deceleration of industrial growth, the slow paced growth and, even stagnation of other markets, a problematic pegged exchange rate, tight monetary policy and high interest rates, the problem worsened and blew out of proportion creating a crisis highlighting that which is an implied economic frailty.

The causes of the currency crisis and its impact to the local economy

In so far as the manifestations of the currency crisis are concerned, most scholars agree on several indicators. Primarily in
the national economic level, the liberalization of the real estate and property markets created a "bubble" on the property sector, which boosted property stocks. There was also an increasing influx of short-term portfolio investments and it came to a point that prior to July 1997, the amount of these portfolio investments far exceeded that of the foreign direct investments. Add to this, the expansion of domestic credit attributed to a very lenient commercial banking policy. In the period of 1992–1996, domestic credits had a growth rate of about 50% per annum. Foreign exchange liabilities increased from $4.7B in 1993 to about $17.8B in June of 1997. Exports were decreasing and external debt amounted to $44.8 B.

The overvaluation of the peso for the longest time was protected by the Central Bank by pulling out from its foreign reserves. It seemed so obvious that at the forefront of the crisis was the active role of the central bank to concentrate all policy responses toward the banking sector. Particularly in 1994, the opening of the banking sector to foreign banks resulted to 22 branches from a mediocre start of 4. This is in spite of undeveloped securities market.

However, it was the lack of reform policies in the financial sector that indirectly affected the greater scope of the economy. Historically, the financial sector was dominated by profit orientation backed up by political concession especially in the Marcos regime. The uncorrected structures still remained. Furthermore, the influx of short-term capital made it convenient for speculators to take advantage of circumstances brought about by the foreign capital market.

The aforementioned assumes an exclusive participation of Philippine policy in the promotion of the crisis within its boarders. This can be quite a limited view since the currency crisis was more a regional phenomenon affecting the East Asian 4 – South Korea, Thailand, Malaysia and Indonesia – than a local, national economic predicament.

All eyes on the Thai Baht. The devaluation of the Thai currency brought about a seemingly herd-like behavior creating a contagion that would slowly diffuse the crisis in the different local economies within the Asian region.

The impact of such created increased the prices of local commodities by virtue of the weakening peso. The policymakers remained alarmed since undergoing such stressful situations would make one question the over-all backbone policy of economic liberalization. The environment seemed to revolt against the policy itself. There was clamor for further economic reform policy while enterprises closed and mass retrenchment occurred. Given a rising unemployment rate, increases in commodities and an unstable political scenario due to the upcoming 1998 elections, the currency crisis was confronted not only with vigilant disapproval but also ideologically-based policy alternatives.

Policy Responses

The Central Bank tried to protect the peso by using its international reserves. However, this resulted to an increase in the nominal dollar value of the peso from 26 to 32. By the time January 1998 came, the exchange rate was already P43/$1. The sales of dollars and the increase in the overnight interests rates was appreciated by some of the economic managers as they justified it to be export advantageous. Afterwards, the Central bank decided to deflate monetary
policy in order to reduce the growth rate of credit to about 28.9% interests rates drastically rose.

The IMF consideration was also instrumental due to the $1.3B load package, which prevented the Philippines from getting an early graduation from the IMF. However, scholars have stressed that the prescriptions of the IMF do not dominate public policy and the consideration of alternative policies other than those forwarded by the IMF were at a high. Generally, policy limitations/failures were centered on the following: exchange rate policy and the stimulation of greater opportunities for FDI influx.

As suggested by most economists, given the multi-variability of factors related to the crisis, competitiveness and the focus on market-based solutions should be greatly considered in the endeavor of policy solution formulation. However, policy responses made by the central bank, the immediate pegging of the exchange rate in order to protect the peso and the sequential increase of interest rates brought greater harm than the crisis itself. The dilemma remains as to what general policy stand should remain; whether the process of opening up the economy (liberalization) should be stifled if not delayed or, the more extreme measure would be returning to a policy of protection.

Given these, the analyses of policy responses should be looked at from the perspective of a combination of political and economic dimensions since policy action in this case is characterized by the participation of the government in an exceptional case of market failure/difficulty.

By focusing on the productivity growth, greater investment returns are expected. In policy terms though, productivity growth seems to have declined in the past two decades. By increasing productivity, markets expand and the exchange rate policy is vital in this regard.

Another pertinent solution that seemed to aid the Philippines in the currency crisis is the remittance of its overseas contract workers of dollars. The influx of these supplemented the demand for dollars and helped ease out the tension brought about by shocks in the foreign currency market. Policy however, plays a role in this regard as migration and employment policies would have an indirect impact on the influx of money and the growth in local business.

Finally, an avenue of policy for economic reformation should consider the vitalization of Foreign Direct Investments. As proposed in policy, (and which is still lacking in operation), FDIIs are meant to boost up the economy by helping increase productivity and employment. The entry, however, of FDIIs in the country is dependent on a few factors: level of wages as compared to the Philippines’ Asian neighbors, investment infrastructure and even, the level of political risks in investing.

The Asian currency crisis brought about positive lights in the conceptualization and the re-analysis of the plight of the Philippine economy. It has been agreed upon by economists, that as the central bank’s behavior of protecting the peso and increasing interest rates remained, the chances for increased productivity and investment remained nil. The defense of the peso was to nominal to be a consideration and that economists suggested that what the speculators did (devaluation of the peso) was what the central bank should have done a few years back. As observed in Indonesia in the 1980’s and China in the 1990’s engineered aggressive depreciation can in fact restore competitiveness.
Issues, Prospects and New Challenges in the growing Philippine economy

1998 characterized a shift in the political leadership from President Fidel Ramos to President Joseph Estrada. Given the regional economic environment, there has been the volatility of Asian currencies which introduced instabilities, high interest rates, a double-digit inflation and a budget deficit. The El Nino indeed “dried up” the agricultural sector which made the Estrada administration consider the revitalization of the agricultural sector and to make it the top priority of his administration. This, however, requires a genuine land reform program which goes contrary to the interests of the traditional, landed elites of the country, some occupying seats of government power in the national and local levels. Other critics of the Estrada administration remain forceful in asserting that Estrada should concentrate economic policy on the industrial sector to answer to the calls for greater productivity. Writ large, the government of President Estrada remains vague in its over-all economic policy direction.

The year 1999 and the first two quarters of 2000 would be best described as a period of increased instability in the economy due to more factors exogenous to the market. In spite of the reports of government of a positive growth rate in the economy, clamor for change in political leadership still remained. It was also during this time that the Philippines underwent a security issue involving the Abu Sayaff, allegedly a religious fundamental group who kidnapped several foreigners.

As mentioned by a Swiss consultant firm, the scenario in the Philippines remains grim for investment since it is plagued with religious and ethnic conflicts, low productivity and a very unstable political system. Early this year, constituencies and civil society organizations burdened with social issues such as poverty, low income and the gross inequality in wealth distribution, began to question the legitimacy of the political leadership.

The President of the Philippines has been accused of plunder, corruption and immorality. These accusations were based on investigative reports as well as on witnesses who could attest to the on-going corrupt practices of government leaders especially the president. Corrupt practices on mass housing, illegal gambling and even the intertwined relationship between private businesses and public concessions given to these businesses are instrumental in the weakening of the peso and the over-all economic performance.

In merely a four days in the month of June 2000, the peso declined from 39 = $1 to almost 50 = $1. This reinforces the increased incidence of protest against the leadership of the land and the residual effect of the Asian currency crisis, the policies that come to its rescue and the political context remain effective, if not, detrimental to the national economy. There is now an on-going impeachment trial of the President.

At present, it would be suggested that the 1997 Asian currency crisis carried over to a more political dimension in terms of its repercussions to the Philippine economy. Hypothetically, had the previous leadership remained with a clear-cut policy direction and even legitimacy given to the political authority, scholars would presume that things would be even better.

Philippine Economic Reformation in the Post Asian currency Crisis era faces challenges in its feasibility given the present
conditions and the failures/limitations of the policies that immediately answer to the crisis. The cumulative nature of problems and context remain and government can do only so much. Policy responses may have the capability to minimize risk and uncertainties in the economy. However, risks and uncertainties are also results of factors that are not only market-based but also politically motivated. This dynamic interaction between the market, policy formulation and implementation and the politics that comes along with both are dimensions that have to be considered in the future analysis of the effects and responses of critical periods in the regional and national economies vis-à-vis the Philippines.

REFERENCES


