AN ASSESSMENT OF FISCAL POLICY IN THE PHILIPPINES, 1986-1988

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I. INTRODUCTION

One of the most robust conclusions of the numerous studies analyzing the roots of the 1983-1985 Philippine economic crisis is the deleterious role played by profligate fiscal policy. It will be recalled that the period 1978-1982 witnessed the rapid expansion of public investments at a time when government revenue performance was deteriorating. This resulted in massive fiscal deficits that were largely financed by foreign borrowings. It cannot be denied that the high levels of government debt in the past pose severe constraints on the government budget in the current period.

Against this backdrop, it is not surprising to find that the adjustment policies undertaken in response to the economic crisis assigned a major role to fiscal policy. The effective management of the size of the fiscal deficit and its financing is an important feature of any attempt to effect a correction of the external/internal disequilibria that persistently hound the country's economic managers. At the same time, the imperatives of turning the economy around and providing the prerequisites of sustained economic growth dictate that the structure of the tax system be reformed and the composition of the government

*This is Chapter V of a bigger study entitled "An Assessment of the Performance of the Aquino Government in Selected Policy Areas, 1986-1988."

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expenditures be realigned to minimize, if not eliminate, the existing distortions in the prevailing framework of economic incentives.

The purpose of this paper is to review the conduct of fiscal policy in the Philippines in 1986-1988, the first three years of the Aquino administration. The approach that is followed in this study is to examine how well the policy actions undertaken in the period under study fit into the policy pronouncements that are embodied in the Medium-Term Development Plan (1987-1992). Section 2 examines the variations in the broad fiscal aggregates: government revenues, expenditures, the fiscal balance and its financing. It also attempts to evaluate the thrust of fiscal policy in terms of its impact on aggregate demand. Section 3 focuses on the tax reform initiatives while Section 4 examines the changing size and composition of the government budget. The public enterprise sector -- its rationalization as well as privatization issues -- meanwhile, is the subject of Section 5. Finally, Section 6 summarizes and highlights the major findings of the preceding sections.

II. THE FISCAL DEFICIT AND ITS FINANCING

The Medium-Term Development Plan states that one of the primary objectives of the fiscal sector is "to manage the deficit and minimize its negative impact on the economy." This section will not only review the size of the fiscal deficit but also its financing. In addition, the role of fiscal policy in the area of demand management in 1986-1988 is also appraised.

A. The Size of the Government Resource Gap

Total government revenues rose from an average of 11.4 percent of GNP in 1983-1985 to a 13.8 percent average in 1986-1988 (Table 1). On the other hand, the growth of government current expenditures outpaced that of total government revenues such that current expenditures increased from 8.9 percent of GNP in the crisis years to 12.9 percent in the first three years of the Aquino administration. As a result, national government savings (or the national government's current surplus) declined by 1.7 percent of GNP during the period under study from its average of 2.6 percent in 1983-1985 to 0.9 percent in 1986-1988. It is noted that while the rise in government current expenditures is partly due to the increase in interest payments engendered by the country's sizeable public debt, it is also traceable in part to the increase in the non-interest component of current expenditures like personal services. (More on this in Section 4.)

, 1980-1988

Levels (In ₱M)

Percent of

	1980-82	1983-85	1986-88	1986	1987	1988			1986-88	1986	1987 Planned	1987 Actual	1988 Planned	1988 Actual
Total Revenues	108870	171454	295320	79245	103214	112861	12.0	11.4	13.8	12.9	14.5	14.7	15.9	13.7
Tax	95756	151219	241766	65491	85923	90352				.7	12.5	12.2	12.5	11.0
Nontax	13114	20235	53554	13754	17291	22509	1.5			.2	2.0	2.5	3.4	2.7
penditures	138806	200091	366504	110497	119907	136100	15.4			0	17.3	17.0	18.6	16.5
Current Expenditures	82652	132670	276024	66921	95503	113600	9.1			9		13.6		13.8
of which:														
Interest Payments	8285	30057	104456	21612	36905	45939	0.9	2.(		5		5.2		5.6
)ital Outlays	52333	58927	63355	28428	17327	17600	5.8	3.9		6		2.5		2.1
:t Lending					1077	4900	0.4	0.6		5		1.0		0.6
Current Surplus/(Deficit)	26218	38784	19296	12324	7711	-739	2.9			)		1.1		-0.1
Overall Surplus/(Deficit)	-29936	-28637	-71184	-31252	-16693	-23239	-3.3	...		1	-2.8	-2.4	-2.7	-2.8
Primary Surplus/(Deficit) I	-21615	1420	33272	-9640	20212	22700	-2.4	0.	1	)		2.9		2.8
Primary Surplus/(Deficit) II	-17380	9914	60397	5508	27289	27600	-2.0		2	1		3.9		3.4

Source of Basic Data: Bureau of Treasury, NSCB, and NEDA.

Since capital expenditures inclusive of net lending to government corporations have not changed significantly between the two periods, this implies that government savings have financed a markedly smaller proportion of government investments, from 66.4 percent in 1983-1985 to 29.9 percent in 1986-1988.

Concomitantly, the overall deficit has ballooned from an average of 1.9 percent of GNP in the last three years of the Marcos regime to a 3.3 percent average in the first three years of the Aquino government. On a year by year basis, the Aquino administration has been successful in cutting down the ₱31.2 billion deficit (equal to 5.1 percent of GNP) in 1986 to 2.4 percent and 2.8 percent of GNP in 1987 and 1988, respectively (Table 1). The huge deficit in 1986 is the biggest ever in the last two decades. It was largely brought about by the election spending at the start of that year. In 1987, the reduction was primarily due to the fact that the intake from nontax sources exceeded its target level. In 1988, because revenue shortfalls (planned levels less actual levels) from both tax and nontax sources were substantial (amounting to 2.2 percent of GNP), the government scaled down its cash outlays in order to keep the budgetary balance in line with Plan targets.

While the period 1983-1985 may not be a good reference period because it includes the worst economic crisis in the post-war period, it is worth noting that the fiscal deficit in 1986-1988 is as large as that in 1980-1982 when the Marcos regime embarked on an active expansionary countercyclical expenditure program. There is one big difference, however, in the composition of national government expenditures in the Marcos and the Aquino years. While capital outlays inclusive of net lending amounted to 6.2 percent of GNP in 1980-1982, it was equal to only 4.3 percent in 1986-1988. On the other hand, interest payments soared from 0.9 percent of GNP in 1980-1982 to 2.0 percent in 1983-1985 and, finally, to 4.9 percent in 1986-1988. Hence, while the primary fiscal balance registered deficits equivalent to 2.4 percent of GNP in 1980-1982, it posted surpluses of 0.1 percent and 1.6 percent in 1983-1985 and 1986-1988, respectively (Table 1). 1/ This indicates how "current-year" fiscal actions

1/ For the purposes of this paper, the primary fiscal balance is defined as being equal to the overall fiscal balance less interest payments. It provides a measure of the fiscal surplus (deficit) that results from the discretionary elements of government expenditure in the current period. During and after the crisis years, the net lending item has been increasingly used to service the debt of government owned and/or controlled corporations (GOCCs). Thus, an alternative measure of the primary balance would be one where not only interest payments but also net lending are netted out of the overall balance. If this second definition of the primary balance is used, we observe a deficit of 2.0 percent of GNP in 1980-1982, and surpluses of 0.7 percent and 2.8 percent in 1983-1985 and 1986-1988, respectively.

have contributed positively to the overall deficit in the Marcos years prior to the economic crisis and how they have detracted from the same during the crisis years and, to a larger extent, in the first three years of the Aquino administration. In this sense, fiscal policy in the Aquino years may be characterized as conservative.

B. The Financing of the Fiscal Deficit

The size of the fiscal deficit, as well as the manner by which it is financed, has widespread repercussions on the rest of the economy. For one, domestic debt-financing may crowd out private investments while money creation may lead to an inflationary situation. For another, external debt-financing may result in balance-of-payments problems in the medium- and/or long-run.

Net foreign borrowing was the most important source of financing the deficit of the national government in 1980-1982, accounting for almost one-half of the aggregate in that period. In the subsequent years, external financing became increasingly less important as foreign loans became more scarce because of the country's external debt problem. Thus, the ratio of external borrowings to the fiscal deficit declined from 24.8 percent in 1983-1985 to 20.5 percent in 1986-1988 (Table 2).

On the other hand, the ratio of money creation (measured here by the change in net claims of the Central Bank (CB) on the national government) to the fiscal deficit averaged 36.5 percent in 1980-1982 compared to one-tenth of one percent in 1983-1985 and negative 81.9 percent in 1986-1988 (Table 2). In fact, money financing of the national government deficit has been negative since 1983 except in 1985. This implies that during most of the 1983-1985 economic crisis and all throughout the first three years of the Aquino government, the national government has detracted from the growth of reserve money. The contractions in the net CB claims on the national government were so large in 1987-1988 that for the first time since 1974, the CB became a net debtor in relation to the national government; i.e., government deposits with the CB exceeded CB holdings of government securities (Annex Table 1). These observations hold even if we look at the consolidated public sector, i.e., national government plus government corporations. Despite the dimunition of national government sourced expansion of reserve money, the actual level of the base money aggregate exceeded its target level in 1987-1988 while actual inflation started to rise in the second quarter of 1987 and even surpassed its target value in 1988.

At the same time, domestic debt financing funded an increasingly substantial proportion of the national government deficit. Hence, while this source funded only 34.8 percent of the deficit in 1980-1982, it accounted for 119.2 percent and 224.1 percent of the national government deficit in 1983-1985 and

	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	1986	1987	1988
	3387	12146	14404	7431	100[illegible]	1141	31252	16693	23206
	2404	5992	4596	5436	20	-340	3580	6781	4242
	2126	9516	8527	4633	162	3252	31041	33069	37023
money crea	1879	3505	4379	-18	-42	68	30	-32228	-18243
debt financing	247	6011	4148	4651	205	84		65297	55266
memo item:									
change in cash	1143	3362	-1281	2638	8207	1771	3369	23157	18059

percentage distribution	1980	1981	1982	1983	1984	1985	1986	1987	1988	1975-82	1983-85	1986-88
surplus/(deficit)	100.0	100.0	100.0	100.0	100.	100.0	100.0	100.0	100.0	37.5	100.0	100.0
net foreign financing	71.0	49.3	31.9	73.2	19.	-3.1	11.5	40.6	18.3	43.4	24.8	20.5
net domestic financ	62.8	78.3	59.2	62.3	161.	118.9	99.3	198.1	159.5	67.4	119.3	142.1
money creation	55.5	28.9	30.4	-0.2	-42.	38.3	-25.1	-193.1	-78.6	32.6	0.1	-81.9
debt financing	7.3	49.5	28.8	62.6	203.	80.6	124.4	391.2	238.2	34.8	119.2	224.1
memo item:												
change in cash	33.7	27.7	-8.9	35.5	81.5	15.9		138.7	77.8	10.8	44.1	62.7

1/.
Calculated based on data fro eau of Treasury and CBP.

1986-1988, respectively (Table 2). Note that the ratios exceeded unity in 1987-1988 because in these years, the national government has chosen to build up its cash reserves by amounts that are substantial relative to the deficit. Most of the increase in the national government's cash reserves in these years were deposited with the CB and gave rise to the negative net CB claims to the national government that was cited earlier.

The increase in the national government's cash balances with the CB and the simultaneous issuance of national government domestic debt instruments to cover the same may be viewed in several ways: (1) it is reflective of a perceived need to maintain a desired cash balance for the national government; (2) the new disbursement scheme instituted by the national government effectively increased the liquidity of the financial system and the national government increased its deposits with the CB to counteract the implied expansionary monetary impact of the former action; (3) the combined deficit of the national government and the government corporations is not truly reflective of the deficit of the public sector because the Central Bank undertakes quasi-fiscal activities, for and in behalf of the national government, that results in the big CB deficits that are recorded for the period (Table 3); and (4) the said action is nothing but a stabilization measure for the purpose of meeting target levels of monetary base. The data belie the first and the second possibilities since they show that (i) the cash reserves of the national government expressed as a ratio of either GNP or total disbursements have risen considerably in the period (Table 4); and (ii) there is no significant increase in the national government cash balances held outside the Treasury and the Central Bank during the years under study (Annex Table 2). On the other hand, it is not clear from the data that are available whether the CB deficits that were actually posted in the period were the result of quasi-fiscal activities or not. If they are not, then government domestic borrowing in excess of the conventionally measured deficit in 1986-1988 may be interpreted as being reflective of the government's reliance on said fiscal instrument to perform the monetary objective of mopping up excess liquidity in the system.

Regardless of the interpretation that is adopted, the fact remains that there has been a substantial increase in the issue of government securities that are left in private sector hands. The findings of earlier studies on the significant crowding out effects of changes in privately held domestic government debt and innovations in government expenditures (Gochoco 1988) indicate that such practice tends to exert undue pressures on the interest rate and consequently, on the level of private investment and growth. An examination of the movement in interest rates and the public/private sector allocation of net domestic credits in 1986-1988 suggests that substantial crowding out of private sector investment may have occurred in the period. Note that while the 91-day Treasury Bill rates were high on the average, in 1986 they

Table 3
CONSOLIDATED PUBLIC SECTOR DEFICIT, 1986-1988

Particulars	(Levels in Billion Pesos) 1986	1987	1988
1. National Government Deficit	-31.2	-20.1	-23.2
2. Monitored Corporation Deficit	-6.8	-2.2	2.1
3. National Government Financing of Monitored Corporation	11.7	8.4	5.4
4. National Government Transfers to PNOC			-1.5
5. Public Sector Borrowing Requirement (PSBR)	-26.3	-14.9	-19.5
6. Local Government (LGs) Surplus	0.3	0.3	0.5
7. Central Bank Deficit	-18.2	-10.9	-16.9
8. Government Financial Institutions' (GFIs) Surplus	-12.0	1.3	2.1
9. SSS/GSIS Surplus	5.5	5.1	4.7
10. National Government Financing to LGUs and GFIs	21.0	0.3	1.4
CONSOLIDATED PUBLIC SECTOR DEFICIT	-29.7	-18.8	-25.4

Source: Department of Budget and Management (DBM).

Table 4
CASH BALANCES OF THE NATIONAL GOVERNMENT
AS A RATIO TO GNP AND TOTAL DISBURSEMENTS,
1976-1988

1976-1982	Ratio of Cash Balance to GNP (%)	Ratio of National Government Cash Balance to Total Disbursement (%)
1976-1982	5.2	34.5
1983-1985	4.9	36.4
1986-1988	7.4	43.5

ource of Basic Data: Bureau of Treasury and NSCB.

were on the downtrend for most of the year. From 1987 onwards, interest rates were on the uptrend as the national government consistently over-borrowed in the domestic credit market (Annex Table 3). On the other hand, the private sector's share in net domestic credit expansion declined significantly in 1986 and 1987. This occurred as the total public sector ate up huge portions of the change in net domestic credit in the period despite the contraction in the national government's share (Annex Table 4).

Furthermore, the resultant pressure on the fiscal deficit itself from the aforementioned reliance on the issuance of domestic securities is not negligible. The incremental interest payment attributable to the national government's "over-borrowing" is equivalent to 18.1 percent (₱3.0 billion) and 12.2 percent (₱2.8 billion), respectively, of the national government deficit in 1987 and 1988. 2/

On another level, a comparison of the obligation and the cash disbursement program of the government shows that there has been a shift in the cash management style of the government starting in 1987. While the difference in the cash disbursement and the national government obligation program net of amortization payments averaged 0.6 percent of GNP in 1975-1984 (exceeding the 1.0 percent level only once) this measure reached 1.1 percent and 1.7 percent, respectively, in 1988 and 1989 (Table 5). This suggests that the government is increasingly financing its obligation program by means of building up its arrears. It should be pointed that such a behavior might lead to (1) an increase in the cost of government purchases as government suppliers adjust their prices to reflect the additional cost of money arising from delayed payments on the part of the government; and (2) some crowding out as this effectively withdraws financial resources from the private sector.

C. The Thrust of Fiscal Policy

While the actual budget surplus (deficit) is the most commonly used summary indicator of the overall impact of fiscal policy, it is severely limited by the fact that it does not distinguish the effects of changes in the government budget on aggregate income and the effects of changes in aggregate income on the budget. In fact, the fiscal budget and aggregate income are simultaneously determined. An alternative measure of the overall thrust of fiscal policy that has been proposed in the literature is the net fiscal impulse measure. This measure estimates the "net stimulative/restrictive effects of the

2/ The additional interest payments were computed by multiplying the change in the cash balances of the national government by the average T-Bill rate in the period.

Table 5
COMPARISON OF OBLIGATION AND CASH DISBURSEMENT PROGRAM
OF THE NATIONAL GOVERNMENT
(Percent of GNP)

	Cash Outlays	Obligation Program*	Difference
1986	18.0	17.7	0.3
1987	17.2	17.4	-0.2
1988	17.2	16.1	-1.1
1989	18.9	17.2	-1.7
1990	18.3	16.9	-1.4

* net of loan repayments

Source: Department of Budget and Management (DBM) and Bureau of Treasury (discretionary aspects of) fiscal operations of the government in the current year and is, therefore, relevant to the assessment of their impact on aggregate demand." The net fiscal impulse breaks down the change in the actual budget balance into the budgetary effects of discretionary fiscal changes (arising from new tax measures and the expansion or contraction of government expenditures) and the change in the cyclically neutral budget deficit. It may be decomposed into two components: the revenue impulse and the expenditure impulse. The revenue impulse is usually negative while the expenditure impulse is positive and generally large enough to swamp out the effects of the former. The net fiscal impulse measure, like the actual budget deficit, suffers from the balanced budget multiplier problem. This means that both measures assume that a tax cut and an increase in government expenditure of the same amount exert equal stimulus on aggregate demand contrary to the well-known results of multipier analysis in macroeconomics.

The net fiscal impulse (equivalent to 4.1 percent of GNP) was highly expansionary in 1986. This appears to be in line with the government's attempt to stimulate growth by increasing government expenditures. This was the essence of the government's pump-priming efforts in that year. The revenue impulse was negative and larger than that in earlier years as a result of increased collection from nontax revenue sources. On the other hand, the expenditure impulse in 1986 is very expansionary and overpowers the aforementioned contractionary impulse from the revenue side. It is worth noting that the government does not score high in fiscal marksmanship in this year. The change in the cyclically neutral deficit (defined in this paper as that which is necessary to meet the target GNP) is just mildly expansionary and is equal to only 0.8 percent of GNP. This is more than four times as large as the change in the actual deficit which is equal to 3.3 percent of GNP in 1986 (Table 6).

In 1987, some sectors expressed fears that the economy might overheat since capacity utilization was deemed to be near the maximum level then. In line with this, we observe a contractionary net fiscal impulse in 1987 equivalent to 2.1 percent of GNP. The fiscal contraction in 1987 was primarily brought about by the huge improvement in the government's revenue intake coupled with a small contraction in the expenditure impulse. Again, the government is markedly off-target with the actual contraction in the budget deficit being equal to more than five times the change in the cyclically neutral deficit.

In 1988, shortfalls in revenue collections reversed the small contractionary expenditure impulse. Hence, while the government ostensibly cut its expenditures, poor revenue yields made the net fiscal impulse positive, i.e., expansionary. Furthermore, the change in the cyclically neutral deficit is in the opposite direction of the change in the actual budget deficit.

Table 6
NET FISCAL IMPULSE AS A PROPORTION OF GNP, 1986-1988
(%)

	1986	1987	1988
Net Fiscal Impulse (1) a/	4.1	-2.4	0.5
Tax Impulse (2)	-1.3	-1.9	0.6
Expenditure Impulse (3)	5.3	-0.5	-0.1
Change in Actual Deficit (4)	-3.3	2.10	-0.80
Change in Cyclically-Neutral Deficit (5)	0.8	-0.40	-0.30

a/ (1) = (2) + (3) = -(4) + (5)

III. TAX POLICY

The Medium-Term Development Plan states that one of the objectives of fiscal policy is "to improve the efficiency, equity and elasticity of the revenue system." Specifically, it asserts that "the tax reform shall be directed at improving the elasticity of the tax system; ensuring that similarly situated individuals and entities bear the same tax burden; withdrawing or modifying taxes that impair incentives to production, exports and growth; and simplifying the tax structure to improve tax administration and compliance. Thus, the design of tax measures shall not be solely dictated by the need for government revenues. The equity and efficiency objectives of the tax system shall be given considerable weight."

Against this backdrop, the 1986 Tax Reform Program was initiated by the government via the issuance of a series of Executive Orders (EOs). These measures represented the first attempt at a comprehensive reform of the tax system in the country. While numerous tax changes were introduced almost annually prior to 1986, they were mostly addressed to revenue creation objectives and are generally piecemeal in nature.

The major components of the 1986 Tax Reform Package are: (1) a movement from a schedular to a global approach to the taxation of individual income from compensation, business, trade and exercise of profession; separate taxation of incomes of spouses; and an increase in the levels of personal exemption; (2) an increase in the final withholding tax rate on interest income and royalties from 17.5 percent and 15 percent, respectively, to a uniform 20 percent and the phasing out of the final withholding tax heretofore levied on dividends; (3) the unification of the earlier dual tax rate (of 25 percent and 35 percent) on corporate income at 35 percent; (4) the introduction of the value added tax in place of the sales/ turnover tax and a host of other taxes; (5) the conversion of the unit rates previously used for excise taxes to ad valorem rates; (6) the abolition of export taxes except that on logs; and (7) the general revision in the valuation of real property for tax purposes. In 1987, the government also enacted a new investment incentives code replacing the one promulgated in 1983.

In what follows, an attempt is made to evaluate selected aspects of the reform program using as yardsticks the professed policy goals of the said program.

A. Tax Elasticity

While some improvement in total revenue performance is registered in 1986-1988, the bulk of this came from nontax revenues rather than from tax sources. This resulted as nontax income grew at an unprecedented 42.6 percent average annual growth rate in 1986-1988 due to the proceeds of the Presidential Commission on Good Government (PCGG)-sequestered assets and the privatization of government-owned and/or controlled corporations (GOCCs), their subsidiaries and acquired assets. On the other hand, tax collections increased by only 13.9 percent annually in the same period (Annex Table 5). Thus, tax revenues rose from 10.6 percent of GNP in the decade immediately preceding the period under study to 11.3 percent in 1986-1988 while nontax revenues increased from 1.6 percent to 2.5 percent of GNP (Annex Table 6).

Estimates indicate that the elasticity of tax revenue with respect to GNP in 1986-1988 is not significantly different from that in 1975-1985 despite the increased tax collections in the later period that was noted in the preceding paragraph. To wit: 3/

$$\ln TAXREV = \underset{(-2.04)}{-0.80} + \underset{(28.18)}{0.89} \ln GNP - \underset{(-0.68)}{2.42} D + \underset{(0.72)}{0.19} \ln GNP*D$$

$$R^2 = 0.99 \qquad F = 568.16 \qquad RMSE\% = 4.54\%$$

where D = 1 in 1986-1988; 0, otherwise.

Similarly,

$$\ln TAXREV = \underset{(-1.59)}{-2.17} + \underset{(8.75)}{1.0^{**}} \ln GNP + \underset{(0.92)}{1.58} D_1 - \underset{(-0.94)}{0.13} \ln GNP*D_1$$

$$\qquad - \underset{(-0.27)}{1.05} D_2 + \underset{(0.26)}{0.08} \ln GNP*D_2$$

$$R^2 = 0.99 \qquad F = 310.75 \qquad RMSE\% = 4.26\%$$

where D1 = 1 in 1980-1985; 0, otherwise, and D2 = 1 in 1986-1988; 0, otherwise. However, the best equation obtained from this exercise is:

$$\ln TAXREV = \underset{(-6.52)}{-1.96^{**}} + \underset{(41.12)}{0.98^{**}} \ln GNP + \underset{(1.39)}{1.36^{*}} D_1 - \underset{(-1.49)}{0.11^{*}} \ln GNP\ D_1$$

$$R^2 = 0.99 \qquad F = 635.66 \qquad RMSE\% = 4.31\%$$

This implies that the elasticity of the tax system is significantly lower in 1980-1985 than in 1975-1979 and 1986-1988 combined.

3/ Numbers in parenthesis are t-statistics. "**" indicate that the corresponding coefficient is significant at 1 percent level; *, at 10 percent level.

B. The Tax Structure

1. The Individual Income Tax

The tax reform package for the individual income tax is embodied in Executive Order (EO) 37. It provides for the application of a uniform (1 percent to 35 percent) graduated rate schedule to the sum of compensation, business, trade and professional income in contrast to the previous system's one percent to 35 percent rate schedule for compensation income and five percent to 60 percent rate schedule for business, trade and professional income. The differentiation in the definition of the taxable base of these two types of income that was characteristic of the old regime was retained. Thus, compensation income is taxed on a modified gross income basis (i.e., gross income less personal exemptions) while business/trade and professional income is taxed on a net income basis (i.e., gross income less personal exemptions less deductions for business expense). Spouses, while still required to file their income tax returns jointly, are now given the option to compute their taxes separately. Furthermore, personal exemption was increased from ₱4,000 to ₱6,000 and ₱8,500 to ₱12,000 for single and married taxpayers, respectively.

The upward adjustment in personal exemptions effectively exempts from tax a typical family of six earning less than ₱26,500 per annum. In contrast, prior to 1986, the same family would be taxed if it has an income of ₱20,000 or more. 4/ This implies that if our typical family had an income that is equal to the poverty threshold, it is exempt to the extent of 50 percent of its income in 1985 and 66 percent of its income in 1986. Thus, the pre-reform situation connotes a wider tax base and a greater potential revenue at the expense of taxing people well below the subsistence level. Note, however, that because the adjustment in personal exemptions in 1986 is a once-and-for-all change, inflation will have completely eroded by 1989 the relief granted to families in the vicinity of the poverty threshold.

The move to allow spouses to compute taxes separately was designed to mitigate the efficiency losses that arise when the secondary earner in a family (usually the wife) is subjected to a higher marginal tax rate than the single individual. This consideration is particularly important given the increasing participation of women in the labor force in the Philippines. There is also some evidence (in other countries) that the elasticity of the labor supply of married women is higher than that of other groups. Furthermore, note that the imputed income from housework of the nonworking wife is untaxed while work-

4/ The poverty threshold for a family of six is ₱39,384 and ₱39,924 in 1985 and 1986, respectively.

related costs incurred by the working wife is not tax deductible. All these suggest that this reform measure is sound from both the efficiency and the equity perspective.

The dual rate schedule of the previous system violates the horizontal equity principle in income taxation. Specifically, taxpayers in the same income bracket (or decile) were subjected to varying effective tax rates depending on the source of their income. 5/ Nonwage earners bore the highest effective tax rates (ETRs) while wage earners had the lowest. The mixed income earners were situated in between. The within-income group variance in the ETRs was largest for the first five income deciles with ETRs of the nonwage earners being at least four times as large as those of wage earners. At the upper end of the income distribution, the variation in ETRs was somewhat smaller but still high such that the ETR of nonwage earners in the tenth decile is almost twice that of wage earners (Table 7).

The earlier regime is not only detrimental to the attainment of horizontal equity between wage and nonwage earners but also inhibited the efficient allocation of resources. The differential tax wedge on the incomes received by salaried and nonsalaried individuals may have distorted the incentive structure affecting the behavior of these economic agents.

It has been shown elsewhere that there is a wide variance in the deductions actually claimed against gross income by nonwage earners (NTRC 1986). This indicates that evasion via excessive deductions had also jeopardized the "equal treatment of equals" principle even within the group of nonsalaried taxpayers. 6/

In sharp contrast, the 1986 Tax Reform Package treats all taxpayers in the same income bracket equally regardless of their source of income (in principle, at least). Thus, Table 8 shows that the ETRs for wage, nonwage and mixed income earners are to a large extent uniform within each income grouping. Whatever kinks

5/ The estimation of the effective tax rates across income deciles are explained in detail in Manasan 1990a (forthcoming).

6/ Some writers have averred that nonwage earners have to be taxed at a higher rate precisely because they have the opportunity to evade taxes while wage earners do not. While this may be a valid solution from the revenue generation point of view, it does not necessarily address the equity and efficiency issues raised above. Not all taxpayers evade taxes and not all evaders do so with the same intensity. Because of this, it is unlikely that under the old system, evasion will somehow equalize ETRs between wage and nonwage earners in the same income decile and within the group of taxpayers who obtain their income from nonwage sources.

Table 7
EFFECTIVE TAX RATES OF THE INDIVIDUAL INCOME TAX ACROSS INCOME DECILES UNDER THE PRE-1986 TAX REFORM PACKAGE
(%)

Decile	All	Wage Only	NonWage Only	Mixed
1	0.12	0.00	0.19	0.00
2	0.09	0.00	0.14	0.02
3	0.19	0.005	0.32	0.07
4	0.25	0.01	0.43	0.11
5	0.53	0.19	0.81	0.30
6	0.97	0.41	1.49	0.56
7	2.15	1.58	1.77	1.55
8	3.77	2.36	5.11	3.36
9	6.84	4.55	8.66	6.73
10	17.45	11.72	20.85	16.17

Source: Manasan, 1990a (forthcoming).

were left are due to the special exemption of ₱4,000 given to those earning wages of less than ₱20,000 a year. 7/ This modification, as we have already pointed out, should improve both horizontal equity and efficiency properties of the tax.

A priori, it is not clear what the impact of these reforms is on the overall progressivity of the individual income tax. However, the estimates in this assessment of the Suit's index of progressivity indicates that, abstracting from evasion, vertical equity has, in fact, been enhanced (Annex Table 7).

In principle, then, the 1986 tax measures promote (1) horizontal equity, (2) vertical equity, and (3) efficiency. In practice, however, tax evasion problems complicate the situation. It should be pointed out that the 1986 Tax Reform Package originally included a provision for imposing ceilings on certain types of business deductions, primarily to deter excessive claims for tax deductions. Unfortunately, this proviso was never implemented. Again, it is difficult to simulate the impact of tax evasion on the estimates of ETRs and the tax progressivity index in this paper because of lack of data at the micro level. What is clear, however, is that tax evasion drives a wedge in the ETRs of wage and nonwage earners in the same income bracket. This implies that the potential gains in horizontal equity and efficiency cited above are not fully realized. The effect on vertical equity is indeterminate but it is likely to be negative if evasion rates in higher income levels are, in fact, greater than those in lower income levels. 8/ In addition, the revenue potential is eroded not only because of evasion but also because of the lower ETRs across all income deciles after the reform (Tables 7 and 8).

To sum up, the 1986 reform of the individual income tax is an excellent reform on paper, as far as the tax structure is concerned. Sad to say, it is sorely deficient in providing the administrative support to all the good intentions provided therein.

2. Tax on Passive Incom

Before 1986, the so-called passive income which consists mostly of capital income was taxed at differential rates: 17.5 percent on interest income, 15 percent on dividends and royalties, and five percent (based on gross selling price) on

7/ It is not clear what this special exemption aims to achieve. In fact, it represents a loophole that may be used by tax evaders.

8/ This hypothesis has both theoretical and empirical support (Allingham and Sandmo 1972 and NTRC 1986).

Table 8
EFFECTIVE TAX RATES OF THE INDIVIDUAL INCOME TAX ACROSS INCOME DECILE UNDER THE 1986 TAX REFORM PACKAGE
(%)

Decile	All	Wage Only	NonWage Only	Mixed
1	0.0	0.0	0.0	0.0
2	0.0	0.0	0.0	0.0
3	0.007	0.0	0.012	0.0005
4	0.008	0.003	0.013	0.003
5	0.03	0.008	0.043	0.008
6	0.09	0.10	0.10	0.03
7	0.30	0.30	0.31	0.24
8	1.01	1.12	1.12	0.57
9	3.10	3.10	3.10	3.10
10	9.46	9.46	9.45	9.40

Source: Manasan, 1990a (forthcoming).

sales of real property, 0.25 percent (based on gross selling price) on sales of stock listed and traded through a local stock exchange and a 10-20 percent tax on net capital gain from sale of stocks that are not traded through the local stock exchange. The 1986 Tax Reform Package instituted the phasing out of the tax on dividends such that by January 1, 1989, the tax rate on this income source was down to zero. At the same time, the tax reform scheme also increased the interest income, royalties and winnings to 20 percent. No changes were introduced in the taxation of capital gains from stock or real property transactions.

The elimination of the tax on dividends may be viewed as an attempt to eliminate the double taxation of corporate income that is inherent in the practise of taxing dividends and corporate income at the same time. The earlier tax regime was thus seen as being biased in favor of noncorporate relative to corporate capital. This is so because such a system implicitly levied a higher tax rate on income from capital from corporate sources relative to other forms of capital income. It also effectively provided a disincentive to the distribution of dividends and, consequently, posed a hindrance to the development of the equities market. From this perspective, the removal of the tax on dividends is deemed to promote the development of the capital market as well as greater efficiency in the allocation of capital resources and greater incentive to increased investment.

On the other hand, the imposition of a final tax of 20 percent on interest income, royalties and winnings results in unequal effective tax rates.on income from said sources vis-à-vis labor income. In particular, low income taxpayers earning some interest income would be taxed at higher rate than those in the same bracket who do not have any interest income because of the final character of the tax. Also, the tax on capital gains appears to be relatively low, particularly for stocks that are traded in the local stock exchange. Meanwhile, the practise of taxing capital gains on real property and other stock transactions based on gross selling price will result in non-discriminatory rates on various form of capital income only by accident. The present system is thus nonneutral with respect to the allocation of savings into alternative forms. In this sense, this practise is not only inefficient but also inequitable.

3. The Corporate Income Tax

Prior to 1986, the corporate income tax was levied on a graduated basis: 25 percent on the first slab of ₱100,000 of net income and 35 percent on net income in excess of said amount. The 1986 Tax Reform Program imposes a uniform 35 percent tax on corporate net income.

There is no economic basis for taxing corporate income at progressive rates. Graduation in rates has a built-in bias against large and/or profitable enterprises. While the promotion of small/medium enterprises may be desirable, the corporate income tax is not the proper instrument to address this objective.

At the same time, the 35 percent rate used is in line with that of the other ASEAN countries. Thus, the Philippines remains competitive with the other ASEAN capitals in attracting foreign capital (Table 9). While a lower rate might be desirable from the point of view of stimulating domestic as well as foreign investments, the revenue needs of the government are, perhaps, of more immediate importance at this point.

4. The Sales Tax and the Value Added Tax

The value added tax (VAT) was formally introduced in the Philippines with the signing of Executive Order 273 in June 1987. It actually took effect on January 1, 1988. In addition to the manufacturer's sales tax (with VAT-like features) and the turnover tax, the VAT replaced the miller's tax, the contractor's tax, the broker's tax, the tax on lessors of personal property and a host of fixed taxes. The VAT imposes a uniform 10 percent tax on the sale and importation of most goods and services. Exports are zero-rated while agricultural products, major inputs to agriculture with no alternative uses, e.g., fertilizers, pesticides, animal feeds, etc., most petroleum products, books and other printed materials, utilities, financial, medical, educational, transport, communication and other services and sales and/or services rendered by entities whose gross annual turnover is less than ₱200,000 are exempt. 9/ Furthermore, the VAT is complimented by the imposition of excise taxes ranging from 15 percent to 100 percent on automobiles and 20 percent on jewelries, perfumes and yachts. 10/

On the other hand, the manufacturer's sales tax that was in place before the VAT had a four-pronged rate structure. Then, the tax rates were differentiated according to the essentiality of the goods; 0, 10, 20, and 30 percent, respectively, for agricultural products, essentials, ordinary, and non-essential goods. In addition, a 1.5 percent turnover tax based on gross selling price was levied on each subsequent sale. Taxes on certain inputs may be credited against outputs taxes. However, the earlier tax credit system is more limited than the one under

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9/ Zero-rated and exempt goods do not pay taxes on their outputs. However, zero-rated goods are given a rebate on the taxes paid on their inputs while exempt goods are not.

10/ Unlike petroleum products, alcoholic and tobacco products are covered by the VAT so that the excise taxes levied on the latter are over and above the VAT and may be viewed in the same light as the aforementioned sumptuary taxes.

Table 9
NOMINAL AND MARGINAL EFFECTIVE TAX RATE ON CORPORATE INCOME
IN ASEAN COUNTRIES

	Nominal Tax Rate		Marginal Effective Tax Rate a/	
	n=10 b/	n=20	n=10	n=20
Indonesia c/	15.0 25.0 35.0	15.0 25.0 35.0	45.0 50.0 55.0	35.0 37.5 40.0
Malaysia	40 + 5	40 + 5	48.7	44.5
Philippines	35.0	35.0	48.7	42.5
Singapore	33.0	33.0	25.0	17.5
Thailand	35.0	35.0	43.75	33.7

a/
The marginal effective tax rate is defined as ((b-a)/b)*100) where b is the before tax internal rate of return; a is the after tax internal rate of return. In our analysis, we have assumed that the hypothetical investment is 100% equity financed and earns an IRR of 20% before tax.

b/
n refers to the life of the hypothetical investment.

c/
Indonesia has a three-tiered rate structure.

VAT. In particular, under the previous system, only taxes on inputs that physically form part of the finished product may be credited against output taxes. Under VAT, tax credits are allowed for taxes on all inputs which are within the VAT ambit. 11/

In evaluating the VAT, it should be emphasized that like the sales tax, the intended base of the VAT is consumption. From an efficiency perspective, the question then is: how successful is the VAT in eliminating the taxation of intermediate inputs? 12/ Equity considerations, on the other hand, prod us to ask: How does the implied distribution of the tax burden of VAT compare with that of the taxes it replaced?

To answer these queries, Stern's (1987) approach to the estimation of ETRs on sectoral consumption was used in this study. 13/ Essentially what is involved in this procedure is the adding up of the successive layers of taxes on output, taxes on inputs into outputs, taxes on inputs into inputs, etc., via the use of the inverse matrix of the input-output tables, given the statutory tax rates and the legal provisions on the rebate or "creditability" of input taxes, so as to arrive at some estimate of the effective tax rate on the consumption of the different commodity groupings. The VAT, in principle, ensures that inputs are not taxed. In practice, because of the exemption of certain goods from VAT, the taxation of intermediate goods is not completely eliminated.

In this paper's analysis, excise taxes on automobiles and non-essential goods are included because they are an integral part of the VAT package, especially in terms of equity considerations. Annex Table 8 presents the estimated nominal rates, T; effective tax rates, E; and their difference, (E-T). The nominal rates are equal to the legal rates adjusted for tax credit allowances. (E-T) is a measure of the extent to which inputs are taxed and, hence, is indicative of the distortions arising therefrom. In general, ETRs are higher before VAT than

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11/ This implies that since petroleum products are exempt from VAT, no credit may be claimed when petroleum products are used as inputs into the production of other goods.

12/ There is a consensus in the economic literature that the taxation of inputs "may lead to inefficiencies in that different industries will face different relative prices so that the marginal rate of transformation between inputs or between an input and an output would be unequal across industries" (Ahmad and Stern 1987).

13/ Methodological details are contained in Manasan 1990b (forthcoming).

after VAT. Also, the variation in the ETRs is greater before the implementation of the the VAT. The average ETR prior to the VAT system is 14.4 percent compared to the 6.5 percent average ETR after VAT. In 1987, ETRs ranged from 1.3 percent to 34.6 percent. In 1988, they varied from 0.4 percent to 13.3 percent only. These arise not only because of the generally higher statutory rates but also because of the greater degree of tax cascading implied in the old regime. The latter is also reflected in the higher (E-T) estimates for 1987 relative to those of 1988: 7.2 percent average before VAT against 3.3 percent average after VAT. Despite the improved system of rebating input taxes under VAT, (E-T) remains high in 1988, very often accounting for more than 50 percent of ETR estimates. This may be attributed to the large number of goods exempted under the Philippine VAT. To sum up, the VAT in the Philippine setting has resulted in a lower taxation of inputs and, consequently, in some improvement in production efficiency but some distortions in production incentives still remain.

The ETRs in Annex Table 8 were combined with the 1985 FIES data on the distribution of income and expenditures to arrive at the implied tax burden estimates per income decile. Estimates of the distributional impact of the VAT, and introduction of excise taxes on non-essentials are shown in Table 10. Suit's index of progressivity has increased marginally from -0.052 to -0.047. This implies that the VAT system is slightly more progressive than the system it replaced.

5. Excise Taxes

Before 1986, excise taxes on alcoholic, tobacco and petroleum products were levied in the form of unit taxes based on volume of production combined with an ad valorem component. The Tax Reform Package completely eliminated the unit tax such that now these excises are on an ad valorem basis only.

Yoingco (1986) showed that the effective tax rates on tobacco and alcoholic products are essentially unchanged by the reform. This implies that the changes introduced in the excise tax on alcoholic and tobacco products would have a neutral impact on the distribution of after-tax income. 14/ What the reform measure has achieved is to introduce an element of automaticity in the revenue response of these taxes with respect to changes in economic activity. A comparison of the rate of growth of excise taxes relative to GNP shows that in 1986-1988, the rate of growth of the sum total of all excise taxes have, in fact, outpaced GNP

14/ This statement does not imply that excise taxes on these two products are not regressive but rather it avers that the new taxes are not any more regressive than what they used to be.

Table 10
EFFECTIVE TAX RATE, CUMULATIVE DISTRIBUTION OF INCOME AND TAX BURDEN ACROSS INCOME DECILE, BEFORE AND AFTER VAT
(%)

Decile	Cumulative Distribution of Income	Cumulative Distribution of Tax Burden		Effective Tax Rates	
		Before VAT	After Vat	Before VAT	After Vat
1	2.020	2.558	2.483	2.907	2.512
2	5.229	6.329	6.192	2.697	2.362
3	9.323	10.949	10.751	2.591	2.276
4	14.313	16.463	16.208	2.536	2.234
5	20.333	22.976	22.670	2.483	2.194
6	27.594	30.704	30.367	2.443	2.166
7	36.530	40.121	39.749	2.419	2.145
8	47.906	51.712	51.349	2.339	2.084
9	63.561	67.565	67.185	2.324	2.067
10	100.000	100.000	100.000	2.043	1.840
Suit's Index		-0.052	[illegible]7		

Source: Manasan, 1990b (forthcoming)

despite the reduction in the excises on petroleum products and a constant rate structure for the other excises since 1986 (Annex Table 5).

There is one disturbing note in the reform of excise taxes on tobacco products. This is the reintroduction of a higher rate on imported (65 percent) relative to domestically produced cigarettes (40 percent and 50 percent, depending on whether the cigarettes carry a foreign brand or not). This has the same protective effect as a 15-25 percent tariff on cigarette imports. 15/ While the government may have valid reasons for wanting to promote the domestic manufacture of cigarettes, it is best that it should do so by means of tariff protection. This will ensure that such support to the local cigarette industry is evaluated within the context of the total protection structure and trade policy itself. Note that the use of discriminatory sales/excise taxes was eliminated as a complimentary measure to the 1980-1985 Tariff Reform Program and this new development represents some backsliding in this regard.

On the other hand, the excise tax rate on petroleum products rose from an average tax rate equivalent to 26.3 percent of the wholesale posted price in January 1986 to a peak of 36.8 percent in March 1987. In August 1987, it was reduced to an average rate of 25.4 percent. Concomitantly, the structure of petroleum product taxes across the various products has also undergone some changes. First, the excise tax rate on fuel oil, an important intermediate input, went up relative to that of other petroleum products between January 1986 to August 1987. From then on, the excise tax on fuel oil was reduced to zero (Annex Table 9). Second, the differential taxation of gasoline and diesel widened further in favor of diesel, i.e., gasoline became more heavily taxed relative to diesel.

The excise tax on fuel oil which was increased from a rate of 16.6 percent prior to the Aquino administration to 28.5 percent in March 1987 may have distortionary effects on the production structure. This results from the fact that:(1) fuel oil is a major input in the production of a number of goods like cement, fertilizer, steel, logging and wood processing, textiles, rice, sugar, and coconut oil milling, food processing, etc.; and (2) there is no existing tax credit proviso for taxes paid on petroleum products under either the old sales tax system or the

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15/ Manasan (1986) analyzed the protective effect of differential indirect tax rates prevalent in the seventies and early eighties.

present value added tax. 16/ Following the approach used in the estimation of the effective tax rates on sectoral consumption in the preceding sub-section, the ETRs on the consumption of different commodities and services as well as the implied taxation of inputs arising from the taxation of fuel oil were estimated. Annex Table 10 shows that the (E-T) estimates range from 0.3 percent to 10.8 percent. This wide variability in the (E-T) estimates is indicative of the production distortions introduced by the taxation of fuel oil. This highlights the positive impact of the elimination of the excise tax on fuel oil in August 1987. On the other hand, estimates of the Suit's index of progressivity suggest that the changes in the taxation of petroleum products under the Aquino government are, in fact, slightly progressive (Table 11). 17/ Finally, it is worth noting that the increase in the average tax on petroleum products between January 1986 and March 1987 exacerbated the Philippines' tendency to price petroleum products higher than its Asian neighbors in the first half of the eighties (Habito and Intal 1987). The reduction in the average tax on petroleum products in August 1987 effectively brought it back to its pre-Aquino government level which is still higher than that of the other Asian countries.

6. Export Taxes

The export tax is an ad valorem tax levied on the gross f.o.b. value of certain exports. Prior to the formulation of the 1986 Tax Reform Package, exports of logs were taxed at 20 percent, copra at 15 percent, coconut oil at nine percent, copra meal/cake and desiccated coconut at eight percent, abaca, lumber and veneer, and pineapple and pineapple juice at four percent, and banana at two percent.

16/ Under the old sales tax system, taxes on petroleum products are not creditable against the sales tax on the output because petroleum products do not physically form part of the end product. On the other hand, under the value added system that is currently in place, taxes on petroleum products are not creditable against output taxes because petroleum products are exempted from the VAT.

17/ This observation abstracts from the increase in the tax on fuel oil in the first one-and-a-half years of the Aquino administration. A more accurate description of the distributional impact of the modifications in the petroleum product taxes would show that there has been a deterioration in the progressivity of these taxes from the start of the present administration up to August 1987. From then on, there is some improvement in the same.

Table 11
EFFECTIVE TAX RATE, CUMULATIVE DISTRIBUTION OF INCOME AND TAX BURDEN ACROSS INCOME DECILE, BEFORE AND AFTER REMOVAL OF EXCISE TAX ON FUEL OIL
(%)

Decile	Cumulative Distribution of Income	Cumulative Distribution of Tax Burden		Effective Tax Rates	
		Before Removal	After Removal	Before Removal	After Removal
1	2.020	1.780	1.747	3.059	2.016
2	5.229	4.511	4.443	2.955	1.957
3	9.323	7.882	7.777	2.858	1.896
4	14.313	12.038	11.890	2.891	1.922
5	20.333	17.125	16.937	2.933	1.954
6	27.594	23.307	23.078	2.956	1.971
7	36.530	31.234	30.965	3.079	2.056
8	47.906	42.001	41.710	3.286	2.201
9	63.561	57.313	57.004	3.395	2.276
10	100.000	100.000	100.000	4.066	2.749
Suit's Index		.0749	.0788		

Source: Manasan, 1990b (forthcoming).

Export taxes impose a penalty on exports. This bias is in addition to that arising from the undervaluation of the foreign currency that the existing industrial protection system defends. Thus, the elimination of export taxes on all exports except logs is expected to result in improvements in resource allocation. In fact, a large part of the reduction in the bias against agriculture relative to manufacturing that was posted in the last three years may be attributed to the removal of export taxes on most products (Medalla 1990). On the other hand, the retention of the export tax on logs is designed to promote resource conservation and to encourage the domestic processing of logs which has been shown in previous studies to be an activity in which the country has comparative advantage (Power and Tumaheng 1983). Furthermore, the revenue loss does not appear to be high, representing less than three percent of total tax collection in 1975-1985 (Annex Table 6).

7. Fiscal Incentives

In 1987, a new Omnibus Investments Code (EO 226) was signed into law. It replaced the Investment Incentive Policy Act of 1983 (BP 391). A comparison of the incentives granted under EO 226 and BP 391 is presented in Table 12. EO 226 replaced the performance-based incentives in the form of tax credits for net value earned and net local content provided under BP 391 with an income tax holiday for a period that varies from three to eight years. Tax and duty free importation of capital equipment is made available to both exporting and non-exporting firms under the 1987 incentive regime while under BP 391, this privilege was granted to exporting firms only. 18/

One of the arguments raised to support the shift to the new incentive legislation is the perceived need on the part of the Philippines to be more competitive with her neighboring countries in attracting foreign investments. A comparison of BP 391 incentives with the investment incentives of the other ASEAN member countries in terms of their impact on the internal rate of return (IRR) of a hypothetical project, using the approach developed in Manasan (1986, 1988b), indicate that while BP 391 incentives to non-exporting firms are less generous than those of the other countries, Philippine incentives to exporting firms are markedly more attractive (Table 13). Because the income tax holiday is the centerpiece of the incentive schemes available in the other countries, it is likely that Table 13 has overestimated the actual benefits accruing to foreign investors in said countries. First, the absence of tax sparing agreements

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18/ BP 391 allowed non-exporting firms to defer payment of all taxes and duties on capital equipment for a period of five years while nonpioneer non-exporting firms are permitted to defer only 50 percent of these taxes.

Table 12
COMPARISON OF INCENTIVES UNDER BP391 AND EO226

entive	BP 391				EO 226			
	Domestic Producer		Export Producer		Domestic Producer		Export Producer	
	Pioneer	Non-Pioneer	Pioneer	Non-Pioneer	Pioneer	Non-Pioneer	Pioneer	Non-Pioneer
. Exemption from duties and taxes on imported capital equipment			100%	100%	100%	100%	100%	100%
. Deferment of duties and taxes on imported capital equipment, to be repaid within 5 years	100%	50%	N/A	N/A	N/A	N/A	N/A	N/A
Tax credit on domestic capital equipment equivalent to duties and taxes on similar foreign equipment			100%	100%	100%	100%	100%	100%
Tax credit on domestic capital equipment to be repaid within 5 years	100%	100%	N/A	N/A	N/A	N/A	N/A	N/A
Tax credit on net value earned for five years	10%	5%	10%	5%	N/A	N/A	N/A	N/A
Tax credit on net local content for five years			10%	10%	N/A	N/A	N/A	N/A
Tax holiday	N/A	N/A	N/A	N/A	6-8 years a/	4-7 years a/	6-8 years a/	4-7 years a/
Net operating loss carry over	Yes	Yes	Yes	Yes	No	No	No	No
Deduction from taxable income of 50% of incremental labor expense for 5 years	No	No	No	No	Yes b/	Yes b/	Yes b/	Yes b/

These are applicable to new projects. Expanding firms are entitled to 3 year tax holiday. isting firms are not entitled to the tax holiday at all.

Redundant for firms enjoying tax holiday.

ce: Manasan, 1989a (unpublished).

Table 13
INTERNAL RATE OF RETURN OF A HYPOTHETICAL FIRM a/
UNDER SELECTED INCENTIVE SCHEMES IN ASEAN COUNTRIES, 1988

	Indonesia b/		Malaysia		Philippines		Singapore		Thailand	
	n=10	n=20	n=10	n=20	n=10	n=20	n=10	n=20	n=10	n=20
1. Regular Taxes (no incentive)	11.0 10.0 9.0	13.0 12.5 12.0	10.25	11.1	10.25	11.5	15.0	16.5	11.25	13.25
2. Tax Holiday (min. no. of years allowed)	NA		16.5	15.0	NA		17.0	17.25	12.0	13.5
3. Tax Holiday (max. no. of years allowed)	NA		16.75	17.0	NA		20.0	19.0	14.0	15.0
4. Duty Exemption on Capital	15.0 14.25 13.5	16.5 15.75 15.25	12.25	12.25	10.8 c/ 11.3 c/	11.8 c/ 12.0 c/	NA		15.0	16.5
5. Tax Credit for Net Value Earned	NA		NA		12.5 d/ 13.8 d/	12.0 d/ 13.3 d/	NA		NA	
6. Export Allowance e/	NA		16.5	16.0	NA				11.5	13.5
7. Tax Credit on Net Local Content (for exporters only)	NA		NA		19.3	16.3	NA		NA	
8. Duty Exemption on Capital (additional for exporters over and above that in (4))	NA		NA		13.3 d/ 12.8 d/	13.8 d/ 13.5 d/	NA		NA	

Table 13 (cont'd)

	Indonesia b/		Malaysia		Philippines		Singapore		Thailand	
	n=10	n=20	n=10	n=20	n=10	n=20	n=10	n=20	n=10	n=20
9. All Incentives (for non-exporters - min. allowed)	15.0 14.25 13.5	16.5 15.75 15.25	19.35	17.35	14.0	13.3	17.0	17.25	16.5	17.0
10. All Incentives (for non-exporters max. allowed)	15.0 14.25 13.5	16.5 15.75 15.25	20.0	19.25	15.8	14.0	20.0	19.0	19.0	18.5
11. All Incentives (for exporters min. allowed)	15.0 14.25 13.5	16.5 15.75 15.25	20.0	19.5	26.0	20.3	17.0	17.25	17.0	17.5
12. All Incentives (for non-exporters max. allowed)	15.0 14.25 13.5	16.5 15.75 15.25	20.0	20.0	27.3	20.5	20.0	19.0	19.5	19.0
Memo Item tariff on capital equipment	0.25		0.12		0.2		0		0.2	
corporate tax rate	0.15/0.25/0.35		0.4+0.05		0.35		0.33		0.35	

a/ For the Philippines, we used BP 391 incentives to find out how it compares with those of other ASEAN countries. The assumed income stream used in these calculations is that which yields as before tax IRR of .20.

b/ For corporate tax rate of .15, 25, 35%, respectively.

c/ First figure refers to non exporting non pioneer firms while the second refers to non exporting pioneer firms.

d/ First figure refers to non pioneer firms while the second refers to pioneer firms.

e/ For 100% export firm.

between the ASEAN countries and major capital exporting countries like the United States, Japan and the OECD, that tax income on a global basis, negates the potential benefit to the individual investor of the income tax holiday. Second, for firms that incur losses in the early years of their operations, the income tax holiday may not be as valuable an incentive as our computations show since our hypothetical firm is assumed to be uniformly profitable over its life span. Thus, contrary to official pronouncements, the set of incentives granted by BP 391 is likely to be as generous as that of the other ASEAN countries.

On the other hand, assessing the impact of the more important provisions of BP 391 and EO 226 on the internal rate of return of hypothetical BOI-registered firms, it is observed that, in principle, the benefits made available under BP 391 are approximately equal to those granted under EO 226 (Tables 14 and 15). In principle, the benefits made available to BOI-registered firms, in terms of the increment to their after-tax internal rate of return under EO 226 are approximately equal to those granted under BP 391. Note that the increase in the after-tax IRR of pioneer firms arising from the EO 226 incentives is equal to the average increment in the IRR of pioneeer exporting and pioneer non-exporting firms registered under BP 391. A similar result is observed in the case of nonpioneer firms.

While the principal source of improvement in the IRR under EO 226 is the income tax holiday, under BP 391, it was tax credit on net value earned and net local content. Given the shortcomings of the income tax holiday that were outlined above, it is likely that BP 391 incentives are, in fact, more generous than EO 226 incentives.

Noting that the principal rationale for the use of investment incentives as an instrument of industrial policy is to compensate for the biases against certain sectors induced by the existing trade regime, it is alarming to find that the new investment incentive scheme has diminished the support provided to exports. Manasan (1989a) has shown that while BP 391 incentives are likely to increase the IRR of exporters substantially more than that of non-exporters, this was not enough to counteract the penalty on exports that is inherent in the prevailing protection structure. EO 226, on the other hand, has exacerbated this deficiency by reducing by half the potential inducements, in terms of increments in the after-tax IRR, given to exporters while it doubled the potential benefits granted to non-exporters. Thus, the major losers from the shift to the new investments incentive code are the exporters while the major gainers are the pioneer non-exporting enterprises.

Furthermore, EO 226 reverted to the use of capital cheapening incentives that was characteristic of the pre-1983 investment incentive scheme. By introducing additional distortions in relative factor prices, such a move tends to

Table 11
CHANGE IN THE INTERNAL RATE OF RETURN OF HYPOTHETICAL BOI REGISTERED FIRMS UNDER BP391 a/
(In Percentage Points)

	Exporting				Non-Exporting			
	Non-Pioneer		Pioneer		Non-Pioneer		Pioneer	
	n=10	n=20	n=10	n=20	n=10	n=20	n=10	n=20
1. Exemption/ Deferment of duties on capital b/	3.5	2.5	3.5	2.5	.5	.25	1.0	.5
2. Tax Credit on net value earned	2.25	.5	3.5	1.75	2.25	.5	3.5	1.75
3. Tax Credit on net local content	9.0	4.75	9.0	4.75	-	-	-	-
4. Total	15.75	8.75	17.0	10.0	3.75	1.75	5.5	3.25

a/ Change in IRR is computed relative to IRRo = 10%

b/ Computed based on t_k = .2 and VAT, where t_k is tariff on capital equipment.

Source: Manasan, 1989a (unpublished).

Table 15
CHANGE IN THE INTERNAL RATE OF RETURN OF HYPOTHETICAL BOI REGISTERED FIRMS UNDER EO 226 a/
(In Percentage Points)

		Non-Pioneer		Pioneer	
		n=10	n=20	n=10	n=20
1.	Tax holiday without extension	2.5	1.75	3.5	2.5
2.	Tax holiday with maximum extension	3.75	2.75	4.0	3.0
3.	Duty Exemption on Capital b/	3.5	2.5	3.5	2.5
4.	1+3	7.25	4.9	8.25	5.75
5.	2+3	8.75	6.0	9.0	6.5

a/ Change in IRR is computed relative to IRRo = 10%.

b/ Computed based on t_k = .2 and VAT, where t_k is tariff on capital equipment.

Source: Manasan, 1989a (unpublished).

result in a sub-optimal relative factor ratio in production. The impact of this change on relative factor prices and consequently, on relative factor use may be appraised by looking at its effect on the user cost of capital. Manasan (1986) showed that the user cost of capital is reduced by 7.8 to 23.7 percent under BP 391 incentives while the decline in the user cost of capital due to EO 226 incentive was estimated (Manasan 1988b) to vary from 26.2 to 35.5 percent. Thus, EO 226 incentives have resulted in a lower user cost of capital relative to BP 391 incentives implying that the former tends to be more bias in favor of capital use relative to the latter. Data on the capital-labor ratio of BOI-registered firms from 1981-1988 confirm this expectation (Table 16). The capital-labor ratio of firms registered with the BOI after the enactment of EO 226 is almost double that of firms registered under the previous incentive legislation.

8. Tax on Real Property

The real property tax is an ad valorem tax based on the assessed value of real property including land, buildings, machinery and other improvements. The assessed value is computed as the product of the market value and the assessment levels, i.e., the percentage applied to market value to determine the taxable value of the real property. The assessment levels vary from 30 to 40 percent for land, from 60 to 70 percent for machinery, and from 15 to 80 percent for buildings depending on the "actual use" of the property, e.g., for lands, residential, commercial, agricultural, etc. The tax rate is set by the provincial board or city council at a rate anywhere between 0.5 to 2.0 percent.

The 1986 Tax Reform Package called for the general revision in the taxable values of real property based on the 1981-1984 market value in 1986 but this provision was suspended until July 1987 due to political pressures. Note that while the Real Property Tax Code provides that such a general revision be undertaken once every three years, such a move was also suspended by the Marcos government in 1984.

The real property tax accounts for more than 50 percent of the total revenues collected by local governments. Noting the urgent need for finances by local governments under a real decentralization scheme it then becomes apparent that a thorough review of the real property tax is imperative. First, the tendency to postpone the general revision of property values mandated under the existing law should be avoided as it engenders the use of outdated taxable values. Second, the adherence to the "actual use" as the basis of the taxable values tends to retard the socially optimal shift to alternative uses (Paderanga 1984). Third, the differential rates that are currently imposed on various forms of real property and improvements also tend to be bias against buildings and machinery relative to land and may not be a desirable arrangement from the resource allocation point of

Table 16
SELECTED STATISTICS ON NEW AND EXPANSION PROJECTS
APPROVED BY THE BOI (WITH INCENTIVES)
(In Thousand Pesos)
(1981-1988)

Year	No. of Firms	Project Cost (nominal)	Employ-ment	a/ K/L (nominal)	Project b/ Cost (real)	c/ K/L (real)
	(1)	(2)	(3)	(4)	(5)	(6)
1981	193	11364366	53110	213.98	11364366	213.98
1982	143	14497342	28274	512.74	13371779	472.94
1983	143	7437044	27980	265.80	6142534	219.53
1984	121	7203588	37830	190.42	3970818	104.96
1985	136	2742089	23961	114.44	1278566	53.36
1986	114	2191961	26201	83.66	1005223	38.37
1987						
BP 391	230	5369942	48782	110.08	2283490	46.81
EO 226	161	4474199	33319	134.28	1902588	57.10
1988	616	28720161	128052	224.29	11187537	87.37

a/
col (20 : col (3).
b/
Deflated by GNP deflator (1981=100).
c/
col (5) / col (3).

Source: Department of Trade and Industry.

view. Fourth, a nationwide tax mapping activity should also provide more accurate information on the characteristics of individual properties and constitute a necessary input in the reform of the present property values (World Bank 1988). Fifth, the valuation system that is currently in place allows the individual assessor a great deal of discretion in determining the market value of real property for tax purposes and provides a lot of opportunity for graft and corruption. Sixth, the real property tax is subject to a high delinquency rate; hence, an improved tax administration would go a long way in increasing the revenue yields of the tax. Finally, given the uneven distribution of wealth in the country, a more efficient real property tax system would also greatly enhance the redistributional characteristics of the tax regime.

IV. GOVERNMENT EXPENDITURE POLICY

The Medium Term Development Plan states that the fiscal sector shall address, among others, the following objectives: "(1) to increase the flow of budgetary resources to activities supportive of employment generating rural-based activities and to social services; and (2) to improve the cost effectiveness of government operations." Against this backdrop, the distribution of government expenditures across sectors and across different economic categories is reviewed. The discussion that follows presents a macro view of the allocation of fiscal resources. No attempt is made to describe government expenditures at the program level, much less to evaluate the economic impact of the same.

Total government expenditures, on an obligation basis, has grown very rapidly during the Aquino years such that its average rate of growth in 1986-1988 is 29.1 percent compared to the 1975-1985 average of 16.6 percent (Table 17). Consequently, as a proportion of GNP, the government budget has increased from its 15.0 percent average in 1975-1985 to 21.5 percent in 1986-1988. In fact, programmed government expenditure in 1988 is equal to 23.193 percent of GNP, its highest level (in the last 20 years (Table 18).

These figures, however, are rather misleading indicators of the growth and size of the government during the period. This is because of the explosive growth of the debt service in the government budget. 19/ Debt service on account of both the national government and government-owned and/or -controlled corporations (via the net lending category) is equal to 3.5 percent of GNP in 1975-1985 as against almost three times that amount (or 9.7 percent of GNP) in 1986-1988. At present, debt

19/ More precisely, debt service started to balloon in 1982.

Table 17
NOMINAL GROWTH RATE OF NATIONAL GOVERNMENT EXPENDITURES BY SECTOR,
ON OBLIGATION BASIS, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
GRAND TOTAL	16.62	16.60	16.65	29.12	29.25	35.80	22.63
Total Economic Services	13.66	15.26	10.01	8.62	26.97	-19.39	25.21
Agriculture	8.55	8.92	7.69	37.04	-55.95	500.95	-2.00
Agrarian Reform	3.72	0.54	11.53	182.63	12.13	251.52	472.79
Natural Resources	37.10	14.73	170.79	-30.22	-85.67	26.56	30.07
Industry	13.20	30.29	-10.47	32.43	-63.41	890.92	-35.94
Trade	2.76	-13.66	54.20	-12.02	-92.10	160.79	230.51
Tourism	8.54	22.31	-17.85	31.49	-84.48	1064.08	25.87
Power & Energy	2.17	31.29	-43.09		-85.75	871.11	-110.59
Water Resources Development	23.99	53.32	-24.45	22.80	-97.86	9404.92	-8.90
Transportation & Communication	1.56	11.10	-17.78	44.19	64.47	46.76	24.21
Other Economic Services	38.81	22.40	86.16	-37.51	125.26	-93.54	67.70
Total Social Services	15.94	10.95	9.22	20.43	67.68	-4.37	32.11
Education	16.02	17.16	13.40	31.44	44.52	21.28	29.57
Health	15.21	17.81	9.37	29.16	19.28	22.94	46.94
Social Services, Labor & Employment	5.66	6.73	3.21	11.45	40.74	-28.75	38.05
Housing & Community Development	27.84	44.84	-4.47	15.75	289.99	-66.73	19.52
Other Social Services	35.36	53.75	0.55	21.06	-6.08	4.64	80.52
National Defense	5.81	7.82	1.25	20.91	23.39	13.21	26.52
Total Public Services	17.42	13.83	26.23	35.65	18.39	56.82	34.45
Public Administration	14.34	12.71	18.25	49.70	14.18	124.90	30.64
Peace and Order	30.73	27.21	39.31	28.36	37.88	3.42	40.31
Others	16.52	6.22	44.58		-1.75		
Debt Service	38.31	37.09	41.20	40.68	14.76	150.25	14.44
Grand Total - Debt Service	13.49	14.66	10.82	19.82	34.78	-1.35	29.37
Grand Total-Debt Service-Net Lending	13.10	13.49	12.22	18.79	15.20	8.77	33.78
Memo Item: Net Lending	156.17	306.41	-12.73	43.63	591.51	-49.28	-15.51

1/
Calculated based on data from the Department of Budget and Management (DBM). Agency level expenditures were classified according to function by using the COA Chart of Accounts.

Table 10
NATIONAL GOVERNMENT EXPENDITURES BY SECTOR, ON AN OBLIGATION BASIS
AS A PROPORTION OF GNP, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
GRAND TOTAL	15.92	15.61	16.27	21.50	18.63	22.11	23.13
Total Economic Services	6.43	7.12	5.64	5.44	6.73	4.74	5.06
Agriculture	0.74	0.82	0.65	0.89	0.24	1.27	1.86
Agrarian Reform	0.08	0.10	0.06	0.40	0.06	0.17	0.05
Natural Resources	0.64	0.29	1.03	0.21	0.19	0.21	0.23
Industry	0.25	0.34	0.15	0.22	0.05	0.39	0.22
Trade	0.04	0.05	0.03	0.01	0.00	0.00	0.01
Tourism	0.03	0.04	0.02	0.02	0.00	0.02	0.02
Power & Energy	0.81	1.13	0.44	0.06	0.02	0.19	-0.02
Water Resources Development	0.16	0.19	0.11	0.05	0.00	0.00	0.06
Transportation & Communication	2.71	3.64	1.66	2.05	1.67	2.14	2.27
Other Economic Services	0.97	0.53	1.48	1.51	4.50	0.25	0.36
Total Social Services	3.01	3.26	2.72	3.78	4.10	3.42	3.86
Education	1.76	1.90	1.60	2.47	2.27	2.41	2.66
Health	0.54	0.58	0.49	0.62	0.53	0.57	0.72
Social Services, Labor & Employment	0.20	0.24	0.15	0.13	0.16	0.10	0.12
Housing & Community Development	0.48	0.51	0.45	0.55	1.11	0.32	0.33
Other Social Services	0.03	0.03	0.03	0.03	0.02	0.02	0.03
National Defense	1.67	2.07	1.22	1.28	1.25	1.24	1.33
Total Public Services	1.81	1.85	1.75	2.67	1.99	2.72	3.12
Public Administration	1.11	1.18	1.02	1.93	1.09	2.14	2.30
Peace and Order	0.50	0.50	0.51	0.66	0.65	0.59	0.74
Others	0.20	0.18	0.22	0.07	0.25	0.00	0.08
Debt Service	3.01	1.30	4.94	8.34	4.56	9.98	9.75
Grand Total - Debt Service	12.91	14.31	11.33	13.16	14.06	12.12	13.38
Grand Total-Debt Service-Net Lending	12.42	14.05	10.57	11.80	11.61	11.04	12.60
Memo Item: Net Lending	0.50	0.26	0.76	1.36	2.45	1.09	0.78

Calculated based on data from the Department of Budget and Management (DBM) and National Statistical Coordination Board (NSCB). Agency level expenditures were classified according to function by using the COA Chart of Accounts.

service payments eat up close to one-half of the Aquino administration's budgets. In contrast, this item accounted for only 22.0 percent of total government outlays in 1975-1985 (Table 19). 20/ Debt service is so huge such that without it, the overall fiscal balance during the Aquino years would show a surplus rather than a deficit. Thus, despite the substantial growth in the government's programmed outlays in 1986-1988, the total budget net of debt service and net lending has actually shrunk to 11.8 percent of GNP from the 12.4 percent average in the earlier period. The problem was particularly acute in 1987 when this aggregate actually registered a decline in nominal terms although the overall budget grew by 35.8 percent. What is even more alarming is the extent to which the debt burden has hampered the government's capacity to provide much-needed services to the people. Thus, real per capita government expenditures adjusted for debt service and net lending stood at ₱217 in 1988, well below the pre-crisis peak level of ₱282 in 1981 (Table 20). 21/ This highlights the urgency of the need for the government to work out means by which the debt burden could be reduced.

A. Distribution of Government Expenditures Across Sectors

Abstracting from debt service, the social service sectors appear to be more favored than the other sectors during the Aquino years. This is consistent with the administration's policy pronouncements. Between 1986-1988, the annual growth of the budgetary allocations to the social service sectors was 28.4 percent (36.3 percent if agrarian reform is included under social services) as against the other sectors' growth of 19.2 percent. While government expenditures on social services also grew faster than those on the economic sectors in 1975-1985, the difference was not as pronounced as that in the subsequent period (Table 17). As a consequence, there has been a general reallocation of fiscal resources with the social sectors increasing their share in the total budget net of debt service from 23.3 percent (23.9 percent with agrarian reform) in 1975-1985 to 28.8 percent (35.2 percent with agrarian reform) in 1988 and the economic sectors' share declining from 49.8 percent (49.1 percent net of agrarian reform) to 37.8 percent (31.5 percent net of agrarian reform) in the same period (Annex Table 11). Note

20/ It should be emphasized that the Aquino government inherited this debt burden from the old regime. The comparative figures cited above are not meant to connote any normative judgment but rather intended to highlight the severe constraints faced by the present government in this regard.

21/ To be fair, this represents some improvement over the very low levels of less than ₱170 during the tough years of the 1983-1985 crisis.

Table 19
PERCENTAGE DISTRIBUTION OF TOTAL NATIONAL GOVERNMENT EXPENDITURES BY SECTOR, ON AN OBLIGATION BASIS, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
GRAND TOTAL	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Total Economic Services	40.37	45.63	34.64	25.20	36.12	21.44	21.89
Agriculture	4.64	5.22	4.00	4.15	1.30	5.76	4.56
Agrarian Reform	0.50	0.65	0.34	1.86	0.30	0.70	3.67
Natural Resources	4.00	1.85	6.33	0.99	1.02	0.95	1.00
Industry	1.57	2.17	0.93	1.05	0.24	1.70	0.93
Trade	0.27	0.32	0.21	0.03	0.01	0.02	0.06
Tourism	0.19	0.27	0.10	0.08	0.01	0.10	0.10
Power & Energy	5.07	7.22	2.73	0.29	0.12	0.86	-0.07
Water Resources Development	0.90	1.24	0.69	0.23	0.01	0.36	0.27
Transportation & Communication	17.04	23.31	10.21	9.55	8.96	9.68	9.81
Other Economic Services	6.11	3.37	9.10	7.04	24.15	1.15	1.57
Total Social Services	18.90	20.91	16.71	17.60	22.00	15.49	16.69
Education	11.07	12.20	9.85	11.46	12.19	10.80	11.50
Health	3.39	3.72	3.03	2.86	2.86	2.58	3.10
Social Services, Labor & Employment	1.24	1.52	0.93	0.59	0.88	0.46	0.52
Housing & Community Development	3.03	3.29	2.74	2.55	5.94	1.45	1.42
Other Social Services	0.17	0.18	0.16	0.13	0.13	0.10	0.15
National Defense	10.51	13.26	7.52	5.94	6.71	5.59	5.77
Total Public Services	11.35	11.87	10.70	12.40	10.67	12.32	13.51
Public Administration	6.95	7.56	6.29	8.98	5.84	9.67	10.30
Peace and Order	3.17	3.19	3.15	3.09	3.48	2.65	3.21
Others	1.23	1.12	1.35	0.34	1.35		
Debt Service	18.88	8.34	30.34	38.78	24.51	45.16	42.14
Grand Total - Debt Service	81.12	91.66	69.66	61.22	75.49	54.84	57.86
Grand Total-Debt Service-Net Lending	78.01	89.97	64.99	54.89	62.34	49.93	54.47
Memo Item: Net Lending	3.11	1.69	4.67	6.33	13.16	4.91	3.39

1/ Calculated based on data from the Department of Budget and Management (DBM) and National Statistical Coordination Board (NSCB). Agency level expenditures were classified according to function by using the COA Chart of Accounts.

Table 20
LEVELS OF NATIONAL GOVERNMENT EXPENDITURES BY SECTOR
ON AN OBLIGATION AND REAL PER CAPITA BASIS, 1975-1988 1/

	1975	1979	1981	1985	1986	1987	1988
GRAND TOTAL	268.86	282.68	306.84	239.23	297.70	365.40	390.80
Total Economic Services	127.83	128.64	148.58	87.97	107.54	78.35	87.31
Agriculture	21.02	7.05	14.52	9.13	3.87	21.03	18.19
Agrarian Reform	3.03	2.05	1.36	0.84	0.90	2.87	14.62
Natural Resources	4.88	5.44	5.46	21.92	3.02	3.46	4.00
Industry	3.12	2.38	15.01	2.06	0.73	6.50	3.71
Trade	1.73	1.52	0.28	0.43	0.03	0.08	0.23
Tourism	0.54	1.33	0.69	0.23	0.03	0.37	0.41
Power & Energy	11.06	25.32	19.79	2.62	0.36	3.15	-0.30
Water Resources Development	0.45	3.57	5.57	0.74	0.02	1.31	1.06
Transportation & Communication	75.47	74.42	69.26	16.84	26.67	35.38	39.11
Other Economic Services	6.53	5.57	16.65	33.15	71.90	4.20	6.27
Total Social Services	48.32	63.26	67.06	40.56	65.48	56.60	66.55
Education	30.87	34.38	37.87	26.08	36.28	39.77	45.87
Health	9.39	10.43	11.11	7.40	8.50	9.45	12.35
Social Services, Labor & Employment	5.83	4.20	4.47	1.94	2.62	1.69	2.08
Housing & Community Development	2.11	13.90	12.84	4.71	17.68	5.32	5.65
Other Social Services	0.11	0.35	0.77	0.44	0.39	0.37	0.60
National Defense	49.97	36.76	29.71	16.80	19.96	20.43	23.00
Total Public Services	29.26	37.05	40.62	27.87	31.76	45.02	53.87
Public Administration	21.64	22.68	27.20	15.81	17.38	35.34	41.09
Peace and Order	2.80	11.68	11.43	7.81	10.36	9.69	12.79
Others	4.81	2.69	1.98	4.25	4.02	0.00	0.00
Debt Service	13.48	16.97	20.88	66.03	72.96	165.01	160.07
Grand Total-Debt Service-Net Lending	255.38	261.92	281.70	167.32	185.50	182.44	217.23

1/
Calculated based on data from the Department of Budget and Management (DBM) and National Statistical Coordination Board (NSCB). Agency level expenditures were classified according to function by using the COA Chart of Accounts.

that if one looks at the total budget inclusive of debt service, the proportional share of all sectors except debt service and general public administration contracted, with the economic sectors suffering deeper cuts than the social sectors (Table 19). When expressed in terms of GNP, similar trends are observed with regards to government expenditures on the social sectors vis-à-vis the economic sectors. Government outlays on the social sectors rose to 3.8 percent of GNP (4.2 percent with agrarian reform) in 1986-1988, up from the 1975-1985 average of 3.0 percent (3.1 percent with agrarian reform). On the other hand, expenditures on the economic sectors dropped from 6.4 percent of GNP (6.3 percent net of agrarian reform) in 1975-1985 to 5.4 percent (5.0 percent net of agrarian reform) in 1986-1988 (Table 18).

Education expenditures, in nominal, real and real per capita terms, exhibited a well defined upward trend during the Aquino years. During these years, its average annual nominal rate of growth is almost twice that in 1975-1985. In real per capita terms, it has grown by 20.7 percent annually in the later period. Compare this with the 2.9 percent average rate of increase in 1975-1983 and the -11.7 percent growth in 1983-1985. As a result, by 1987, per capita government expenditures in education has recovered from the sharp decline during the crisis years to yield the highest level attained in the last 15 years (Table 20).

Furthermore, education's share in the total budget has increased to 11.5 percent in 1988 from the 9.9 percent average in 1983-1985 making it the single most important sector outside of debt service in terms of budgetary allocation (Table 19). Needless to say, if one looks at the sector's share relative to the total budget net of debt service, then the picture looks even better with education's share in 1988 reaching 19.9 percent from the 13.7 percent average in 1975-1985 (Annex Table 11).

Expressed as a proportion of GNP, government expenditures on education amounted to 2.7 percent in 1988 as against the 1.8 percent average in the Marcos years. Thus, this is one example where the government has put its money where its mouth is. This development is definitely in line with official policy statements and the constitutional provision. On the other hand, this share is still slightly smaller than the allocation received by the education sector in the other Asian countries. For instance, government education outlays in Thailand was 4.0 percent of GNP in 1975-1985.

The health sector is one of the professed priority areas of the present administration. In 1986-1988, the growth rate of expenditures on the health sector was 29.2 percent, just about equal to that of the average sector. Thus, there is an almost imperceptible upward movement in health expenditures in terms of GNP (0.6 percent in 1986-1988 versus 0.5 percent in 1975-1985) or in terms of real per capita levels (₱12.35 in 1988 against ₱12.00 in 1982 (Tables 18 and 20).

Both the social welfare and the housing sectors suffered severe reductions in budgetary allocations during the crisis years. Although some improvement is registered in 1986, it was almost wiped out by 1987. This is true whether one looks at nominal, real, real per capita or GNP terms. The positive nominal growth posted in 1988 in these sectors was not enough to bring the real per capita levels at par with the pre-crisis levels.

In terms of the share in the total budget and as a percentage of GNP, agriculture is the most important sector in the agriculture/agrarian reform/natural resource group in the Aquino as well as in the Marcos years. On the other hand, the agrarian reform sector garnered the biggest increments in 1986-1988 (with an average annual growth rate of 182.6 percent) such that government expenditures in agrarian reform as a proportion of GNP increased by almost tenfold from 0.1 percent in 1975-1985 to 0.9 percent in 1988 (Table 18). Despite considerable adjustments in government expenditures on the natural resource sector in 1987 and 1988, it has not reached the pre-crisis levels.

The infrastructure/utilities sector was the hardest hit sector during the 1983-1985 crisis. Although some increase in government outlays on this sector was posted in 1986-1988, it has yet to fully recover from earlier expenditure cuts. Expressed as a proportion of GNP, government expenditures in the infrastructure/utilities sector stood at a low 2.3 percent in 1988 as against the 5.0 percent average in the pre-crisis years (Table 18).

Viewed any which way, defense expenditures exhibited a definite downtrend in 1975-1985. Between 1985 and 1988, however, it grew faster than the average sector so that the reverse is evident in the trend for this period. This observation holds whether one includes outlays for peace and order under the defense category or not. In spite of this marked increase in defense/peace and order expenditures in recent years, the Philippines' expenditures in this sector (equal to 2.1 percent of GNP in 1988) is lower than that of its Asian neighbors. For instance, Thailand spent 4.0 percent of its GNP on defense in the last decade.

Public administration expenditure was the second fastest growing item in the government's budget in 1986-1988. Coupled with the fact that it was practically spared the belt-tightening measures imposed in 1983-1985, it rose consistently from 1.1 percent of GNP in 1975-1985 to 1.9 percent in 1986-1988. It reached 2.4 percent of GNP in 1988, the highest level attained in the last 15 years. This is rather surprising considering the present government's vow to trim the bureaucracy (Table 18).

B. Distribution of Government Expenditures Across Economic Categories

Government expenditures on personal services grew by 32.8 percent nominally in 1986-1988. This is almost twice as fast as that in 1975-1985 (Annex Table 12). Even after adjusting for inflation, personal services expenses rose by 24.9 percent during the Aquino years compared to 1.4 percent in the earlier period. Thus, the ratio of personal service expenditures to GNP was 5.1 percent in 1986-1988 in contrast to 3.8 percent in the previous decade (Annex Table 13).

If one considers or takes in the salary adjustments to government workers actually granted by the Aquino administration, one would not be able to fully account for the hefty growth in this abovementioned expense item. This implies that there has been an increase in the bureaucracy in terms of number of personnel during the present government.

The findings of earlier studies show that there is a wide disparity in the compensation scales of employees in the public and private sectors. The possibility that this may adversely affect the quality of public services has also been raised. Thus, a pay hike for government workers appears to be justified. Significant increases in the salaries of government workers in the education and the defense/peace and order sectors are highly publicized and are generally perceived to be well deserved. However, the incidence of salary adjustments is highly uneven across sectors, with some sectors being able to negotiate to be covered by the "Office of the President" pay plan while others are not. Thus, a salary standardization scheme is urgently needed to rationalize the government pay scale and to take the place of the piece-meal approach that has been implemented so far.

In relation to the second point, there are some anecdotal stories of certain agencies increasing their personnel complement for turf-building reasons. The circumstantial evidence that has been presented here tends to validate these stories. This stands in sharp contrast to official pronouncements of trimming the fat off the government.

Maintenance and other operating expenditures exclusive of interest payments, transfers and loan repayments suffered severe cuts in the crisis years. It has been pointed out that these reductions may result in the premature deterioration of the existing stock of government capital assets. The 1988 level of maintenance and operating expenditures indicates that this problem has not been adequately addressed by the present administration. In nominal as well as in real terms, this expense item has not quite caught up yet in the Aquino years such that as a proportion of GNP, its 1988 level is equal to only 2.5 percent, still below the 3.2 percent average in the pre-crisis years (Table 21).

Capital outlays exclusive of net lending likewise experienced the brunt of the cost cutting measures instituted during the crisis years and as a consequence of the heavy debt burden that is particularly severe in the Aquino years. Thus, this expenditure category has contracted significantly in real terms since 1983. In fact, it declined nominally even in 1987 and 1988. As a proportion of GNP, it decreased from an average of 5.2 percent in 1975-1982 to a low of 2.9 percent in 1988 (Table 21). Its share in total government expenditures also declined from an average of 34 percent in the period before 1982 to less than nine percent in 1988. This contraction in public investments is worrisome given the well established theoretical and empirical link between investment and economic growth.

Transfers from the national government to GOCCs in the form of subsidies, equity and net lending used to be rather high in the Marcos years when it averaged 3.4 percent of GNP. In fact, earlier studies (Amatong 1986) have shown that this was a serious cause of the leakage in the government budget in 1975-1985. The present government has been successful in trimming down this item to 1.0 percent of GNP in 1988 reflective of its efforts to rationalize the government corporate sector (Table 21).

Finally, it is noted that the national government budget, given present accounting conventions, does not account for tax expenditures granted by such agencies like the Board of Investments in the form of tax exemptions/deductions/credits to specific private and government corporations. Annex Table 14 reveals that these tax expenditures are not insignificant. These figures reflect the revenues foregone and by implication, expended by the government. The question is: should these expenditures be allowed to bypass the budgetary allocation process?

V. THE GOVERNMENT CORPORATE SECTOR AND THE PRIVATIZATION PROGRAM

The government corporate sector expanded very rapidly in the seventies and the early eighties. GOCCs numbered only 70 in 1973. In just over a decade, this figure has more than tripled. In 1985, the Presidential Commission on Reorganization (PCR) made an inventory of government corporations and counted 303 such entities: 93 parent corporations, 153 subsidiaries and 57 acquired assets.

As a result of this unrivaled surge in the number of public sector enterprises (PSEs), the public sector began to play a major role in activities previously dominated by the private sector like petroleum refining and trading, sugar trading, land transportation, hotel operation, rubber and coffee plantation, etc. It has also led to the duplication of functions of some government corporations. Furthermore, certain anomalous

Table 21
NATIONAL GOVERNMENT EXPENDITURES BY ECONOMIC CLASSIFICATION,
ON AN OBLIGATION BASIS AS PROPORTION OF GNP, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
TOTAL	15.92	15.61	16.27	21.51	18.63	22.11	23.15
I. Current Operating Expenditures	10.8	10.14	11.75	17.07	12.59	18.14	19.50
A. Personal Services	3.8	4.06	3.59	5.12	4.64	4.48	6.01
B. Maintenance & Other Operating Expenditures	7.0	6.08	8.16	11.95	7.95	13.66	13.49
a. Interests	1.22	0.85	1.64	8.04	3.52	9.98	9.76
b. Transfers	1.13	1.32	0.92	1.02	1.00	0.84	1.19
1. to local government	0.63	0.63	0.64	0.46	0.59	0.26	0.54
2. to all government corporations	0.18	0.22	0.12	0.18	0.00	0.21	0.28
3. to others	0.33	0.47	0.16	0.38	0.41	0.37	0.37
c. Loan Repayment & Sinking Fund Contribution	1.92	0.68	3.32	0.30	1.05	0.00	0.00
d. Other MOE	2.78	3.23	2.28	2.59	2.38	2.83	2.54
II. Capital Outlay	5.03	5.47	4.52	4.44	6.04	3.97	3.65
A. Land, Land Improvements & Structure Outlays	1.51	1.98	0.98	0.86	0.49	1.07	0.97
B. Buildings & Structures	0.57	0.72	0.40	0.67	0.97	0.53	0.57
C. Equipment	0.26	0.25	0.28	0.16	0.10	0.17	0.20
D. Investment Outlay	2.14	2.21	2.05	0.91	2.03	0.67	0.28
a. to local government	0.00	0.00	0.00	0.00	0.00	0.00	0.00
b. to all government corporations	2.05	2.17	1.92	0.89	2.00	0.66	0.27
c. to others	0.08	0.05	0.12	0.01	0.02	0.01	0.00
E. Loans Outlay	0.54	0.31	0.81	1.83	2.46	1.52	1.63
a. to local government	0.00	0.00	0.00	0.02	0.00	0.03	0.03
b. to all government corporations	0.50	0.26	0.76	1.36	2.45	1.09	0.78
c. to others	0.05	0.04	0.05	0.45	0.00	0.40	0.82

1/ Calculated based on data from the Department of Budget and Management (DBM) and National Statistical Coordination Board (NSCB).

practices arose, signals perhaps of the government's inability to cope with the unprecedented growth of the government corporate sector. It was observed that some government corporations are regulating their competitors from the private sector while some government nonfinancial corporations are behaving like financial corporations. At the same time, other PSEs collected taxes like regular government bureaus (Manasan, Amatong and Beltran 1988). Moreover, interlocking directorates became prevalent as government Ministers assumed multiple directorships in various GOCCs. In 1984, for example, the Commission on Audit (COA) observed that one Minister was in the Board of Directors of 43 government corporations while another was in 40.

Despite the tremendous growth in the number of PSEs in the last decade, gross value added of the sector lagged behind that of the total economy. Their share in Gross Domestic Product is also low relative to that in other countries (Short 1984). At its peak in 1983, gross value added of public enterprises accounted for 3.3 percent of GDP but averaged a low 2.0 percent of GDP for the rest of the period between 1975-1984 (Manasan and Buenaventura 1986).

At the same time, estimates of the factor productivity ratios as well as the financial profitability ratios confirm the widespread perception that public enterprises are, in general, less efficient than their private sector counterpart. Total factor productivity of the whole economy was 5.5 times that of government corporations in the last half of the seventies and roughly nine times in the first two years of the eighties (Manasan, Amatong and Beltran 1988).

Poor financial performance coupled with the unsustainably high levels of capital expenditures has led PSEs to eat up a disproportionately huge chunk (about 29 percent) of the national government's budgetary resources. They also account for a significant portion (over 50 percent) of the external debt of the consolidated public sector (Manasan and Buenaventura 1986). Consequently, the failure of the public enterprise sector is generally seen as having been a major contributory factor in the economic crisis of 1983-1985.

Against this backdrop, Letter of Instructions 1454 was issued in April 1985 directing the Special Presidential Reorganization Committee (SPRC) to conduct studies aimed at rationalizing the government corporate sector. Among other things, this Committee recommended the limiting of the use of the government corporate form to certain areas/activities, the institutionalization of effective supervision, the coordination and control of government corporations hand in hand with the provision of adequate operational flexibility to the said enterprises, and the abolition, merger, retention or privatization of specific corporations. These efforts, however, were overtaken by the change in administration in February 1986.

The change in government in 1986 ushered in reforms that assign the pivotal role in economic development to the private sector. These reforms which were succintly enunciated in the 1987-1992 Medium Term Development Plan call for a program that will: (1) limit the use of the government corporate form to those activities that are usually considered to be natural monopolies, those that require large and physically indivisible capital investments, those that are characterized by long and uncertain gestation periods, and/or those that are deemed essential from the point of view of national welfare, security or defense; 22/ (2) dispose of existing government corporations that do not meet the criteria outlined in (1) above; (3) establish an integrated system of performance evaluation for the remaining government corporations; and (4) improve the system of supervision and control of government corporations. These general statements of policies are very much in line with the pre-Aquino government pronouncements of the SPRC.

A. Rationalization of the Government Corporate Sector

With regard to the first and second objectives of the government corporate sector rationalization program in the Medium Term Development Plan, it should be pointed out that possible government action on this may come at two levels.

First, the government may promulgate an issuance (perhaps in the form of a Government Corporate Code) that would provide the framework for the operation and administration of GOCCs. The Plan suggests that such an issuance should "among others, define the role of the government corporate sector in the development process; identify the areas where the corporate form of organization may be utilized by the government, including the criteria and the guidelines on the use of the corporate form in government; determine the manner by which the government corporations may be created; and establish a uniform set of guidelines to delineate more clearly the relationships at the different levels of corporate supervision and control." Note that such a code would have been a useful instrument in the long protracted policy discussions on the disposition of existing GOCCs. Furthermore, it would have ensured, if steadfastly implemented, a more rational government corporate sector in the future. Thus, it is unfortunate that no such issuance was made by the President before Congress was convened or by the legislative branch of government afterwards despite the existence of various versions of a draft Government Corporate Code as formulated by different agencies like the Government Corporate

22/ The Plan proposes the following criteria to govern the use of the government corporate form: (i) flexibility and autonomy in operations; (ii) financial viability; (iii) limited liability of the national government; and (iv) possibility of private sector participation.

Monitoring and Coordinating Committee (GCMCC) and the Commission on Audit (COA) as early as late 1986 and the introduction of a number of bills in Congress (sponsored by Senators Guingona and Romulo in the Senate, and Congressman Amatong, among others, in the House).

Second, the government, even in the absence of such a code, could undertake a review of the existing GOCCs with the end in view of formulating policy actions on their disposition. This is, in fact, what the government did. After reviewing the proposals of the Presidential Commission on Reorganization and the Government Corporate Monitoring and Coordinating Committee (GCMCC), the Department of Budget and Management (DBM) recommended the privatization of 121 GOCCs, 23/ the retention of 33 in their present form, the abolition of 58, and the conversion/regularization or consolidation with other GOCCs of the remaining 88. Since then, numerous reshufflings have occurred as to the disposition of these GOCCs. For some time, it was difficult to have a sense of what the government dispositive action is with regard to specific GOCCs because the fate of a great number of the GOCCs was classified under "pending with the President (of the Philippines)" for quite a while. For instance, decision on the dispositive action on 35 of the 121 corporations originally recommended for privatization was still uncertain as of December 1987. No decision on 25 of these GOCCs has been reached as of February 1988. It was only on July 28, 1989 that all 121 GOCCs finally got the Presidential seal of approval for privatization. Similarly, as late as June 30, 1989, the decision on the disposition of 30 other corporations which were recommended for conversion, regularization and abolition by the DBM was still pending with the President. Table 22 presents the status of government disposition action on the GOCCs as of July 30, 1989. Despite the length of time it took to arrive at some firm decision on the disposition of most GOCCs, a cursory review of the list of retained government corporations indicates that quite a number of them would not satisfy the criteria outlined in the official policy pronouncements, e.g., Marcos Golf Foundation, Gintong Alay Foundation, Sugar Regulatory Administration, etc. Furthermore, the necessary legislative action with regard to the charters governing the GOCCs that are up for abolition, regularization and consolidation has not been undertaken to date. 24/

23/ Four of these were already privatized even before the issuance of Proclamation 50.

24/ The privatization program will be reviewed in a separate sub-section in this paper.

Table 22
STATUS OF DISPOSITION ACTION ON GOCCs
(July 3

	Approved the President	Pending w/ the President	No need for Presidential approval	For further Review	TOTAL
Privatization	121	-	-	6	127
Conversion	5		-	-	5
Regularization	17	-	-	3	20
Retention	38	-	34	-	72
Consolidation	18	-	-	-	18
Abolition	0	8	-	-	58
Total	249	8	34	9	300

Source: Department of Budget and Management (DBM).

The rationale for items (3) and (4) of the Medium Term Development Plan objectives for the government corporate sector is to instill fiscal discipline and to strengthen the accountability of public enterprise managers through the effective monitoring and supervision of the retained corporations. The progress of government efforts in this area has also been painfully slow as evidenced by failure to comply with the timetable set in the Medium Term Development Plan.

Contrary to earlier recommendations and the spirit of the public enterprise sector reform program, the membership of Department Secretaries/Undersecretaries in the Board of Directors of various GOCCs has not been limited to two. 25/ This has been detrimental to the quality of decisionmaking since many "Board meetings are attended not by official members but by minor functionaries."

Moreover, in 1988, the GCMCC had oversight responsibility over 14 nonfinancial government corporations only. This number was increased to 18 in 1989 and will reach 25 in 1990. Furthermore, the inclusion of the Departments of Agriculture, Environment and Natural Resources, Public Works and Highways, Trade and Industry, and Transportation and Communication, (agencies which are heavily involved in the operation of the big GOCCs) in the GCMCC in lieu of the DBM and CB has further exacerbated the incentive incompatibility problem that is inherent when the heads of the various line agencies sit in the Board of Directors of the GOCCs that they are supposed to supervise. 26/ Thus, the move may be viewed as a weakening of the system of supra-ministerial supervision of government corporations.

Also, a performance evaluation system consisting of the formulation of quantifiable performance criteria, the determination of sectoral and firm level norms or target values against which the corporations' actual performance will be appraised, and the institution of an incentive mechanism that will ensure reinforced "good" behavior and sanction "poor" performance, has yet to be put in place for the retained government corporations. The experience of other countries in this area suggest that the benefits that can be derived from the institutionalization of a performance evaluation system for public enterprises can be maximized if these firms are given operational autonomy as well (World Development Report 1988). In

25/ At present, the ceiling of two is applied to memberships in the Board of Directors on non-ex-officio basis.

26/ The GCMCC was originally composed of the Executive Secretary and the heads of the following service agencies: CB, Department of Finance (DOF), DBM, and NEDA.

this regard, it should be noted that there are some bills pending in Congress that would tend to emasculate public enterprise managers in the name of ensuring central government control over their actions.

To be fair, as of the end of 1988, the GCMCC has piloted corporate planning programs, including the development of performance criteria and the setting of targets, in five corporations, namely, the National Power Corporation, the National Irrigation Administration, the Philippine Ports Authority, the National Housing Authority, and the National Electrification Administration. Together with the Government Corporate Affairs Office of the Department of Finance, it has worked on the improvement of the monitoring system of the GOCCs under its wing. Consequently, as pointed out earlier in Section 4, the budgetary burden of GOCCs has been put under control under the present administration. For instance, the sum of national government subsidy, equity and net lending contributions has declined to 1.6 percent of GNP in 1987-1988 from its 3.1 percent average in 1981-1985. The self-financing ratio (i.e., the ratio of savings to investments) of the major nonfinancial GOCCs averaged 100 percent for 1986-1987 27/ compared to a low 13.4 percent average for some 60 GOCCs in 1975-1984 (Manasan, Amatong and Beltran 1988). This development is partly due to an improvement in the economic performance of the GOCCs and partly to the scaling down of the planned investments of these corporations. Note that the ratio of actual to planned GOCC investment is .52 and .65 in 1987 and 1988, respectively. On the other hand, the ratio of actual receipts to actual current expenditures is 1.16 and 1.25 compared to the planned ratios of 1.13 and 1.07 in 1987 and 1988, respectively (Table 23).

B. The Privatization Program

In December 1986, President Aquino issued Proclamation 50 creating the Committee on Privatization (COP) and the Asset Privatization Trust (APT) as the implementing arm of the COP. The COP is vested with comprehensive policymaking functions relating to the rehabilitation, conservation, take-over and the disposition of government corporations and acquired assets of government financial institutions. It is headed by the Secretary of Finance and is composed of the Secretaries of Budget and Management, Trade and Industry, Justice, and Economic Planning.

On the other hand, the APT was initially tasked with the divestiture of the nonperforming assets (NPAs) earlier transferred to the national government by the Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP) as part of the rehabilitation programs of said government financial

27/ This is based on data furnished by the GCMCC.

Table 23
FINANCIAL OPERATIONS OF THE
MAJOR NONFINANCIAL CORPORATIONS, 1987-1988
(In ₱B)

	1985	1986	1987		1988	
	Actual		Target	Actual	Target	Actual
Total Receipts	56.5	38.7	47.7	49.8	59.5	59.8
Current Expenditures	52.0	38.4	42.2	43.1	55.4	47.8
Capital Expenditures	12.5	5.9	15.1	7.8	13.8	9.0
Capital Transfers	0.0	1.2	0.0	-1.4	0.0	0.0
Internal Cash Generation	4.4	0.3	5.5	6.7	4.2	12.0
Overall Surplus (Deficit)	-8.0	-6.8	-9.6	0.2	-9.7	2.9
Total Receipts ÷ Current Expenditures	1.087	1.008	1.130	1.155	1.074	1.251
ICG ÷ Capital Expenditures	0.352	0.051	0.364	0.859	0.304	1.333

Source: Actual data from GCMCC; Plan Targets from NEDA Medium-Term Development Plan, 1987-1992.

institutions. Ten out of the 86 GOCCs that were originally approved by the President for privatization were also assigned to the APT. The disposition of the remaining GOCCs was given to 11 government agencies to which these corporations are attached. 28/

The COP privatization guidelines call for the disposition entities to prepare a privatization plan within 60 days from date of designation. Such plans should include the following aspects: extent of privatization (whether total or partial); mode of privatization (whether it will involve sale of assets or sale of shares); method of privatization (whether it will take the form of public offering stocks, sealed bidding of stocks or assets or negotiated sale of stocks or assets); identification of potential investors; valuation of assets or stocks; and timing. With regard to the method of privatization, the COP has a stated preference for public offering of shares with the end in view of widening the ownership base of enterprises. On the other hand, negotiated sale is viewed as a last resort that should be approached with the outmost transparency. Furthermore, cash offers are preferred over sale on installment basis. Other things being equal, Filipino investors are preferred over others.

The nonperforming assets of the PNB and the DBP that were put on the block represent a total of 399 accounts, with total booked exposure amounting to ₱108 billion plus contingent exposure of ₱33.8 billion. As of the end of 1988, some 104 NPAs had been liquidated in full while 48 accounts had been the subject of partial sale. The gross recovery on the full sale using various modes of disposal was ₱6,992.6 million as against a total exposure of ₱16,149.6 million, reflecting a gross recovery factor of 43 percent. Note that the PNB and the DBP had estimated the gross recovery factor for the 399 accounts to be in the vicinity of 17 percent only. The difference between this estimate and the actual APT figures as of December 1988 might be due to the fact that the more attractive assets tend to be sold earlier because of demand considerations. In fact, the gross recovery rate for 1987 is 49.1 percent compared to 38.0 percent in 1988 (Table 24). If this hypothesis is correct, then a considerably lower recovery rate relative to that achieved in 1987-1988 should be expected in the future.

In general, the divestment via the APT yielded a higher recovery rate than through non-APT means. The direct-debt-buy-out scheme of the "transfer price" variety posted the highest recovery rate of all the disposition modes used. Contrary to a

28/ These agencies are the Department of Agriculture, Department of Transportation and Communication, Department of Tourism, Government Service Insurance System, Home Insurance and Guaranty Corporation, National Development Company, Philippine National Bank, Philippine National Oil Company, Philippine Management Staff and the Development Bank of the Philippines.

Table 24
DISPOSITION OF TRANSFERRED ASSETS

	Number	Gross Recovery (PM)			Total Exposure (PM)			Recovery Rate (%)		
	Total	1987	1988	Total	1987	1988	Total	1987	1988	Total
FULLY DISPOSED	104	3795.4	3197.1	6992.6	7730.9	8418.7	16149.6	49.1	38.0	43.3
A. Thru APT	90	3188.1	2944.3	6132.2	4952.5	7151.2	12103.7	64.4	41.2	50.7
1. Bidding	36	1905.1	956.5	2861.6	3553.3	4489.6	8042.9	53.6	21.3	35.6
2. DDBO-AV	12	50.8	120.5	171.4	154.6	198.2	352.8	32.9	60.8	48.6
3. DDBO-TP	23	1021.3	956.2	1977.5	958.0	7917.6	1875.5	106.6	104.2	105.4
4. Retrieved	12	210.9	723.8	934.7	286.6	958.1	1244.7	73.6	75.6	75.1
5. Other Modes	7	0	187.0	187.0	0	587.7	587.7	-	31.8	31.8
B. Thru Non-APT	29	607.3	253.1	860.4	2778.4	1267.5	4045.8	21.9	20.0	21.3
6. GFI Sales	24	607.3	122.6	729.9	2778.4	494.2	3272.6	21.9	24.8	22.3
7. Other Modes	5	0	130.5	130.5	0	773.3	773.3	-	16.9	16.9
PARTIALLY DISPOSED	48	181.4	959.3	1140.7	9191.0	10322.9	19513.9			
A. Thru APT	48	52.9		882.6	5324.3	9634.6	14958.9			
1. Bidding	33	52.9	474.4	527.3	5324.3	7823.8	13148.1			
2. DDBO-AV	7	0	41.4	41.4	0	255.0	255.0			
3. DDBO-TP	2	0	232.5	232.5	0	1115.8	1115.8			
4. Retrieved	1	0	50.4	50.4	0	107.0	107.0			
5. Other Modes	5	0	31.0	31.0	0	333.0	333.0			
B. Thru Non APT	15	128.5	1	258.1	3866.8	688.4	4555.2			
6. GFI Sales	12	20.6	0.2	20.8	3438.6	60.7	3499.3			
7. Other Modes	3	107.9	129.5	237.3	428.2	627.7	1055.4			
GRAND TOTAL	152 1/	3976.8	4156.4	8133.3	16921.9	18741.6	35663.5			

1/
Asset counts total do not tally because some assets were disposed through more than one mode.

Source: Asset Privatization Trust (APT).

priori expectation, sealed bidding scored the lowest recovery rate (35.6 percent) of all the APT modes (Table 24).

Contrary to COP pronouncements, public offering of shares has not been utilized at all as a divestment instrument prior to the offering of PNB shares in early 1989. This has serious distributional implications on the government's privatization program. Forty-one percent of total sales were made through sealed bids, making it the most favored mode of disposition. An inconsistency of sorts arises here as this implies that a significant proportion of government assets was sold via the mode that has registered the lowest recovery date.

On the other hand, a total of 12 GOCCs were sold in full in 1987-1988 while seven were the subject of partial sales. The government grossed a total of ₱4352.2 million from these transactions (Table 25).

The divestiture of the NPAs assigned to the APT has suffered considerable delays because about 300 of such assets are not in physical form assets, i.e., they are financial form assets, and therefore, not conveyable. In fact, even some of the physical form assets are not conveyable because they are still under litigation. This problem might be approached from three directions: legislative action that will facilitate the conversion of the financial claims against debtors to foreclosed assets; judicial reform that will involve the designation of a special Court to try collection cases with the end in view of speeding up the foreclosure proceedings; and the pragmatic approach that is currently being pursued by the APT whereby it essentially tries to come up with compromise foreclosures outside of the judicial system via such measures as direct-debt-buy-out, bid-out of financial form assets with escrow provisions, etc. Note that normal judicial foreclosure proceedings are very costly in terms of both time and money. On the other hand, the legal issues that have to be considered are: constitutional non-impairment of contracts, pre-emptive rights of stockholders, rights of debtors under the Civil Code and other laws relating to foreclosures, nationality laws and related policies and accounting and auditing laws related to valuation and pricing of assets. Given that the APT is operating on a five year timeframe (which implies that it has more than two years to go), the other two approaches cited above might still post significant returns if explored.

VI. CONCLUSION

This part of the paper highlights the major findings discussed in greater detail in the preceding sections. In addition, it spells out the policy directions that emerge.

Table 25
SALES/DISPOSITION OF GOCCs
(Gross Recovery in ₱M)

		1987	1988	Total
	FULL SALE	617.7	2,436.7	3,054.4
1.	Asia Industries, Inc.)		130.5	130.5
2.	Beta Electric Corp.)			
3.	Commercial Bank of Manila	510.0		510.0
4.	Hotel Ent. of the Phil., Inc.		325.0	325.0
5.	Marina Properties		1,777.8	1,777.8
6.	Maunlad Savings & Loan Asso.		14.1	14.1
7.	Mindanao Textile Corp.	23.6		23.6
8.	National Marine Corp.		168.0	168.0
9.	Nat'l Precision Cutting Tools		21.3	21.3
10.	Pilipinas Bank	38.6		38.6
11.	Tacoma Bay Shipping Co.	10.0		10.0
12.	Usiphil, Inc.	35.5		35.5
	PARTIAL SALE	579.2	718.6	1,297.8
1.	International Corporate Bank	297.6 *		297.6
2.	Nat'l Shipping Corp. of the Philippines	141.4	132.2	273.6
3.	National Stevedoring	36.0		36.0
4.	Negros Occidental Copperfields	101.9	60.2	162.1
5.	The Energy Corp.	2.3		2.3
6.	Union Bank of the Phils.		518.6	518.6
7.	Woodwaste Utilization & Dev. Corp.		7.6	7.6
	GRAND TOTAL	1,196.9	3,155.3	4,352.2

*Includes sale of shares made by National Development Company (NDC) in July 1986.

Source: Committee on Privatization (COP).

First, there has been a deterioration in the overall fiscal position of the national government in 1986-1988 relative to 1983-1985. In fact, the fiscal deficit in the first three years of the Aquino administration is comparable in size to that in 1980-1982 when the Marcos government embarked on an expansionary countercyclical expenditure program. However, if one looks at the primary fiscal balance (a measure of how fiscal actions in the current period contribute to the government's net indebtedness) rather than the overall fiscal deficit, the shift to a more conservative fiscal stance in 1986-1988 can be observed. In particular, there has been a dramatic improvement in the primary balance in 1987 and 1988.

What appears to be worrisome, though, is the downward trend in government savings. While total revenues have increased somewhat in the last three years, it has not kept pace with the growth in current expenditures of the national government so that the current balance has consistently declined. In 1988, the national government registered a deficit in its current account for the first time in the last 15 years. For the most part, the increase in current expenditures may be attributed to the ballooning of interest payments as a result of the unprecedented accretion in the outstanding stock of government debt under the previous regime. To some extent, however, this development may be traced to the increase in non-interest current expenditures, particularly personal services expenditures. In turn, this is partly due to the government's failure to trim the fat from the bureaucracy. These developments point to the government's increasing inability to finance the already depressed level of maintenance and operating as well as capital expenditures that characterized most of the crisis years. It is expected that these shortcomings will pose severe constraints on the country's growth prospects in the near future.

In this regard, it is noted that there is a need (i) to increase the public sector's revenue effort, (ii) to exercise greater control over government expenditures, and (iii) to explore more innovative ways by which to relieve the debt service burden on the government budget. The Philippine revenue effort ratio (tax as well as nontax) is the lowest in the ASEAN region (Manasan 1989b) and is lower than the average ratio of middle-income countries (World Bank 1988). Thus, the expected rewards from a more vigorous revenue collection effort appear to be high. At the same time, the analysis in this study indicates that there still exist some potential gains from cost cutting measures in the government. In the final analysis, though, the magnitude of the debt service and its impact on the government budget is simply too enormous to be ignored and is almost impossible to be overemphasized as it effectively strangulates the government's capability to provide basic public services.

Second, the period witnessed the increasing reliance on domestic borrowings to finance the government deficit. Without doubt, this is a direct consequence of the dimunition of foreign sourced finance since the Philippines joined the ranks of highly indebted countries in 1984. But what is unexpected is the paradoxical observation that if one looks at the combined accounts of the national government and the government corporate sector alone, the government seemed to have "overborrowed" from the domestic private sector. This arose because the national government, on its own account, has consistently built up its cash balances with the Central Bank in 1986-1988 as it simultaneously resorted to the new issue of domestic debt instruments to cover the same. Thus, while economic theory suggests that there is some room for non-inflationary money financing of the fiscal deficit, it can be observed that the national government and the government corporate sector had, in fact, detracted from the growth of reserve money during the three year period under review even as the inflation rate started to rise in the second quarter of 1987 and the Plan target exceeded in 1988.

Concomitantly, there has been a substantial increase in the amount of new issue of government securities left in private sector hands. Earlier studies point to the significant crowding out effects of increases in privately-held domestic government debt and suggest that such a practice tends to exert undue pressure on the interest rate with the concomitant adverse impact on the level of private investment and economic growth. On the other hand, a closer examination of the data reveals the fact that the excess of national government domestic borrowing over the conventionally measured fiscal deficit is linked to the massive deficits of the Central Bank that may have resulted from its quasi-fiscal activities. Given the amount of external financing available, the size of the combined fiscal and quasi-fiscal deficit, i.e., the consolidated public sector deficit, in 1987-1988 appears to be inconsistent with other macroeconomic targets as reflected in the upward pressure on both the inflation rate and the interest rate. This is contrary to the precepts of a truly prudent fiscal policy. What is manifested, therefore, is a need for (i) a closer examination and firmer control of the consolidated public sector deficit over and above the concern for the conventionally defined fiscal deficit, and (ii) a review and a re-delineation of the appropriate role of the Central Bank in carrying out so-called quasi-fiscal activities.

Third, the government's record with ~~regards~~ to fiscal marksmanship in its demand management program in 1986-1988 is not very encouraging since it has exhibited a marked tendency to overestimate the expansion or contraction in the fiscal impulse necessary to achieve its growth targets. This experience shows that the government should exercise greater circumspection in the use of fiscal policy to actively influence aggregate demand and overall economic growth.

Fourth, this review reiterates its earlier observation that there is a need to improve the revenue performance of the government. While the elasticity of the tax system has recovered from the slump it suffered in 1980-1985, it has not improved enough to surpass its pre-1980 level which is low by international standards. At the same time, other studies (NTRC 1986, Manasan 1988a) indicate that the amount of potential government revenue foregone because of tax evasion is substantial. Furthermore, the present paper also stressed that tax evasion weakens the tax system in terms of both horizontal equity and economic efficiency considerations. Thus, at this point, improvements in tax compliance and tax administration hold greater promise than increasing tax rates or introducing new taxes.

Fifth, in principle, the 1986 tax reform package scores high with regards to both resource allocation and equity goals. The efficiency gains are large specifically in the shift towards a more global approach to individual income taxation, the separate taxation of married couples, the elimination of the double taxation of dividend income, the application of a single rate on corporate income, the introduction of the VAT, the elimination of the export tax, and the abolition of the excise tax on fuel oil. Similarly, the potential impact on the redistributional characteristic of the tax system of the new tax measures like the modifications in the individual income tax, the excise tax on fuel oil, and the VAT, is positive.

Some problem areas still exist in the tax arena.

(i) It is unfortunate that the proposal to impose ceilings on allowable income tax deductions was not implemented. The failure to plug what could be one of the principal sources of leakage in the tax collection machinery jeopardized the potential gains from the modifications in the structure of individual income tax under the 1986 tax package. At present, a bill regarding this matter is pending in Congress. The enactment of legislation or the issuance of an administrative order that will effectively deter excessive claims for business expense for tax purposes will not only yield positive results in revenue mobilization but will also enhance the realization of the envisioned improvements in equity and economic efficiency of the tax package.

(ii) Because the Philippine version of the VAT exempts more transactions, it has a narrower base than that of other countries like Indonesia and New Zealand. This has resulted in the incomplete elimination of the distortionary effects of input taxation, contrary to the underlying philosophy of the VAT, and the lower than projected revenue yield of the VAT in its first year of implementation. 29/

(iii) The present system of taxes on passive income and capital income yields highly unequal effective tax rates and is, thus, nonneutral with respect to the allocation of savings into alternative forms. This is a rather complex area with no straightforward solutions. Further study is, therefore, recommended.

(iv) Historically and prospectively, the government has shown a tendency to rely heavily on excise taxes. 30/ While said taxes are easy to collect, they are highly regressive. In this light, it would perhaps be wiser to concentrate on improving the revenue yield of the VAT, a confirmed money maker in other countries, than to continue this dependence on excise taxes.

(v) The shift to pre-1983 type investment incentives and the introduction of the tax holiday is seen as a retrogression in the industrial promotion strategy. This is because of the capital bias of the 1987 Omnibus Investment Code, its perverse effect of benefiting the national coffers of the capital exporting countries rather than the foreign investors it seeks to attract, and the deterioration in its ability to counteract the bias against exports that is inherent in the prevailing structure of protection. It is recognized that, at this point, it is not possible to simply revert back to the 1983 incentives because of the Philippine accession to the GATT. The new challenge is the design of innovative performance-based incentives that do not invite countervailing measures from our trading partners.

(vi) Given the limited financial resources available to local governments units, it is imperative that they harness the full potential of the real property tax as a revenue source. This can be achieved through the regular updating of assessed values of real properties to reflect changes in the current market value and increased efforts in the area of tax mapping. While existing legislation provides that a general revision of property values be undertaken once in three years, it is truly unfortunate that the political will to implement this has not

29/ Undoubtedly, inadequate prior preparation for the implementation of the VAT also contributed significantly to the VAT's underperformance with respect to revenue generation.

30/ There is a pending legislative proposal to increase excise taxes on certain alcoholic and tobacco products in 1990.

been evident in the last decade. 31/ Furthermore, the present practice of using "actual use" as the basis of the assessed value, the imposition of differential rates on different forms of real property, the highly discretionary system of establishing property values for tax purposes and the roots of the poor compliance should be re-examined to improve the resource allocation effects and the revenue yield of the real property tax.

Sixth, the years 1986-1988 witnessed an unprecedented growth in the size of the national government budget in nominal terms and relative to GNP. In fact, in 1988, total government expenditures, on an obligation basis, reached 23.1 percent of GNP, its highest level in the last twenty years or so. These are rather misleading indicators of the size and growth of the government in the period and illustrates very well the observation that it is not only the size but also the composition of government expenditures that is important in defining its overall economic impact. In this light, several observations deserve special interest.

(i) An analysis of the sectoral distribution of the national government budget further highlights an earlier point made in this study that debt service accounts for a disproportionate share of total government outlay in the last three years. It is beyond doubt that this huge debt burden has hampered the government's capacity to provide adequate service to the people. In 1987-1988, interest payments and principal amortization combined accounted for close to 50 percent of the national budget. Thus, relative to GNP, aggregate government expenditures net of debt service and net lending in 1986-1988 contracted relative to that in previous decade.

(ii) Abstracting from the constraints posed by the government's debt burden, the Aquino administration has favored, in terms of budget allocation, the social service sectors relative to the other sectors in contrast to the previous regime's tendency to pour more resources into the economic sectors. This tendency is particularly pronounced in education which received substantial increments in its budget share in the last three years.

(iii) The government expenditures on defense and peace and order was on an uptrend in 1986-1988 following a persistent decline in the Marcos years. Despite this development, the

31/ The Marcos government suspended the revision scheduled in 1984 while the Aquino administration likewise suspended the implementation of EO 73 (issued in 1986) which provides for what could have been the first general revision of assessed values of real properties since 1979.

Philippine defense budget, in GNP terms, is one of the lowest in Asia.

(iv) Expenditures on public administration proved to be the most resilient item in the government budget. It was practically spared the belt-tightening measures imposed during the crisis years. Furthermore, expressed as a proportion of GNP, public administration expenditures rose in an unabated fashion in the last three years such that in 1988, its level reached its highest in the last 15 years. At the same time, it is noted that the record-breaking rate of growth in government expenditures on personal services in the last three years is attributable not only to the salary adjustment granted government workers but also to an increase in the number of personnel. This is rather surprising given the government's promise to come up with a leaner bureauracy.

(v) Government expenditures on the infrastructure utilities sectors in 1986-1988 has hardly risen above the levels set by the cost-cutting measures of the crisis years. In a related development, capital outlays exclusive of net lending have continuously declined since 1983, relative to GNP and in real terms. This protracted contraction in public investments particularly in infrastructure and utilities is alarming given the well-established theoretical and empirical link between investment and economic growth. Furthermore, outlays on maintenance and other operating expenditures in 1986-1988 do not appear to have recovered from the expenditure cuts imposed during the crisis years. This would have an adverse effect on the government's ability to prevent the premature deterioration of its existing stock of capital assets and may exert additional pressure on the future demand for public capital formation.

(vi) The remarkable reduction in national government transfers to GOCCs under the Aquino government is commendable. While this development may partly be explained by the scaling down of the investment programs of most government corporations, it may also be attributed to some improvement in the financial performance of the same and may be reflective of some success in the government's efforts to rationalize the government corporate sector.

Seventh, under present accounting conventions, tax expenditures like tax exemptions/deductions/credits granted by agencies like the Board of Investments to specific private and government corporations are not included in the national government budget. There is some evidence that the amount involved here is sizeable. Since the revenues foregone in this manner are in essence spent by the government, it is but proper that tax expenditures be included in both the revenue and the expenditure side of the government budget and thus, should not be spared of the budgetary allocation process. It is hoped that in enhancing the transparency of the government accounting system, fiscal discipline will also be promoted.

Eighth, in the first half of the eighties, the government corporate sector experienced an unprecedented growth in terms of both number and assets that was accompanied by a great deal of inefficiency that has resulted in a huge outflow of resources from the national treasury. The first three years of the Aquino administration saw the fruition of earlier efforts to rationalize the public enterprise sector. The Medium Term Development Plan enunciates a four-point program that seeks to limit the use of the government corporate form, dispose existing government corporations which do not meet certain criteria, establish an integrated system of performance evaluation, and improve the system of supervision and control of government corporations.

Soon after it assumed power, the Aquino government, under the aegis of the Presidential Commission and Reorganization, embarked on a review of existing GOCCs for the purpose of recommending government dispositive action on said corporations. After its creation, the Committee on Privatization, together with the Department of Budget and Management, subjected the above-mentioned recommendations to further study. The slowness of the decisionmaking process regarding the disposition of some 249 GOCCs bordered on feet-dragging (as of the end of July 1989, no final decision has yet been reached on the fate of eight GOCCs facing abolition). What is even more disappointing, however, is that the final list of retained corporations included a number of corporations that do not satisfy the requirements outlined in official policy statements. Also, the requisite legislative action with regards to the charters of the GOCCs that are up for abolition, regularization or consolidation is still sorely missing to date.

While the GCMCC has improved the monitoring of GOCCs under its wing, thereby promoting some fiscal discipline in the conduct of these GOCCs, the oversight responsibility of the GCMCC is limited to only 14 corporations. Furthermore, no incentive-based performance evaluation system that defines the quantifiable performance criteria and sectoral norms or standards has been put in place to date. It is also noteworthy that Department Secretaries and Undersecretaries continue to hold seats on the Board of numerous government corporations. In this regard, this paper concurs with the recommendation made earlier by some groups that a Government Corporate Code that embodies the framework for the operation and administration of GOCCs be enacted. Care should be exercised that said code should promote accountability in the context of greater operational autonomy. Such a code should be a useful instrument in the further rationalization of the government corporate sector and should help prevent the undeterred growth of GOCCS in the future.

Ninth, the government's privatization program that covers the divestment of government ownership of some GOCCs and of the nonperforming assets of government financial institutions, has been hampered by legal impediments in the disposition of these assets. Possible solutions to this problem include: (1) legislative action that will facilitate the conversion of financial claims to physical form assets, (2) the creation of a special Court to try collection cases with the end in view of speeding up foreclosure proceedings, and (3) the use of compromise foreclosures, e.g., via the direct-debt-buy-out, bid-out with escrow provisions, etc., outside the existing judicial system. Although the evidence to date indicates that the direct-debt-buy-out does not suffer from lower the average recovery rates, the other alternatives are still worth exploring in the interest of greater transparency in the disposition of government assets. Finally, the government seems to have given very little consideration to the distributional implications of the various methods of privatization that are available. Thus, public offering of shares has been utilized to a rather limited extent. In this regard, the government should study the different modes in countries like Jamaica and South Korea that seeks to allocate more shares to small buyers.

Annex Table 1
SOURCES OF CHANGE IN RESERVE MONEY, 1984-1988 1/
(In ₱M)

CHANGE IN LEVELS	1983-84	1984-85	1985-86	1986-87	1987-88
Reserve Money	5722	4541	11997	6880	9682
Net Foreign Assets	-16838	-32880	-14516	-7075	9761
Net Domestic Assets	22560	37421	26513	13949	-73
Net Claims on Deposit Money Banks (DMB)	-7596	-10220	1924	18225	2585
Net Claims on Public Sector (PS)	-5086	9195	-8314	-31939	-66023
Net Claims on National Government (NG)	-4235	4268	-7830	-32228	-18243
Net Claims on Other Government	-851	4927	-484	289	-47780
Net Claims on Other Financial	3128	-374	-7722	-754	2253
Net Other Items	32114	38820	40625	28413	12671

PERCENT DISTRIBUTION OF CHANGE	1983-84	1984-85	1985-86	1986-87	1987-88
Reserve Money	100.00	100.00	100.00	100.00	100.00
Net Foreign Assets	-294.27	-724.07	-121.00	-102.83	100.82
Net Domestic Assets	394.27	824.07	221.00	202.75	-0.75
Net Claims on DMB	-132.75	-225.06	16.04	264.90	26.70
Net Claims on PS	-88.89	202.49	-69.30	-464.23	-681.91
Net Claims on NG	-74.01	93.99	-65.27	-468.43	-188.42
Net Claims on Other Government	-14.87	108.50	-4.03	4.20	-493.49
Net Claims on Other Financial	54.67	-8.24	-64.37	-10.96	23.27
Net Other Items	561.24	854.88	338.63	412.98	130.87

1/
Calculated based on data from the Central Bank of the Philippines.

Annex Table 2
BALANCES OF THE NATIONAL GOVERNMENT BY DEPOSITORY, 1984-1988
(Levels: ₱M)

Year	End of Period Levels				Percent Distribution			
	Grand Total	Central Bank	Treasury	Others	Grand Total	Central Bank	Treasury	Others
1978	9301	2164	7	7130	100.00	23.27	0.08	76.66
1979	12557	2204	40	10313	100.00	17.55	0.32	82.13
1980	13994	1642	10	12342	100.00	11.73	0.07	88.19
1981	17315	2644	29	14642	100.00	15.27	0.17	84.56
1982	15423	2203	117	13103	100.00	14.28	0.76	84.96
1983	18061	3214	101	14746	100.00	17.80	0.56	81.65
1984	27382	10652	930	15800	100.00	38.90	3.40	57.70
1985	28196	7616	572	20008	100.00	27.01	2.03	70.96
1986	27731	14403	318	13010	100.00	51.94	1.15	46.92
1987	53052	43636	281	9135	100.00	82.25	0.53	17.22
1988	70432	61687	270	8475	100.00	87.58	0.38	12.03

Source of Basic Data: Bureau of Treasury.

Annex Table 3
91-DAY TREASURY BILL RATES, 1985-1989
(In %)

	Nominal	Real
1985	26.7	5.6
Q1	33.9	-6.5
Q2	34.7	1.6
Q3	21.5	5.8
Q4	16.6	16.6
1986	15.8	13.2
Q1	22.0	18.3
Q2	17.0	15.9
Q3	13.0	14.4
Q4	10.7	3.3
1987	11.5	7.7
Q1	9.5	10.1
Q2	11.5	8.8
Q3	11.7	5.4
Q4	13.2	6.3
1988	14.7	5.9
Q1	13.0	4.1
Q2	14.8	5.5
Q3	14.6	6.4
Q4	16.2	7.6

Source: Central Bank of the Philippines.

Annex Table 4
SOURCES OF CHANGE IN NET DOMESTIC CREDITS, 1984-1988 1/

CHANGE IN LEVELS (₱M)	1983-84	1984-85	1985-86	1986-87	1987-88
TOTAL	-4390.7	-10260.5	-32017	-16347.6	13601.3
National Government	-2398.3	1318.1	-2345.7	-32659.4	-8846
Other Government	45857	18108.6	34156	41313	16791.3
Public Sector	43458.7	19426.7	31810.3	8653.6	7945.3
Private Sector	-47849.4	-29687.2	-63827.3	-25001.2	5656

PERCENT DISTRIBUTION OF CHANGE	1983-84	1984-85	1985-86	1986-87	1987-88
TOTAL	100.00	100.00	100.00	100.00	100.00
National Government	-54.62	12.85	-7.33	-199.78	65.04
Other Government	1044.41	176.49	106.68	252.72	-123.45
Public Sector	989.79	189.33	99.35	52.93	-58.42
Private Sector	-1089.79	-289.33	-199.35	-152.93	-41.58

1/
Calculated based on data from the Central Bank of the Philippines.

Annex Table 5
GROWTH RATE OF GOVERNMENT REVENUES, 1975-1988 1/
(In %)

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987
I. TOTAL REVENUES	15.17	12.44	21.00	17.71	14.51	30.25
TAX REVENUES	16.16	13.75	21.97	13.60	6.50	31.20
Bureau of Internal Revenue	21.36	18.22	29.01	14.83	9.41	25.20
Domestic Based	20.88	18.18	27.44	16.35	12.97	25.55
Income & Profits	19.77	15.47	30.44	13.68	2.64	13.04
Excise	22.30	18.03	32.09	13.27	21.50	38.20
Sales Tax and Licenses	19.38	20.94	15.01	19.51	20.96	31.23
Tax on Property						
Other Domestic Taxes			19.03	47.93	25.32	4.29
International Trade			207.60		-78.90	-20.57
Bureau of Customs	9.51	8.55	11.79	13.69	2.78	48.56
Import Duties and Taxes	11.51	11.97	10.45	15.99	5.20	54.08
Export Taxes	-3.81	-20.74	51.10	-85.56	-36.11	-97.65
Other Offices	8.93	13.83	-1.70	-30.57	-29.57	11.75
NON-TAX REVENUES	9.53	5.14	20.49	42.93	78.44	25.72
Memo Item: GNP	17.91	16.61	21.02	11.48	3.40	14.42

1/
Calculated based on data from the Bureau of Treasury (BT).

Annex Table 6
GOVERNMENT REVENUES AS A PROPORTION OF GNP 1/

	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988
I. TOTAL REVENUES	14.729	13.479	13.023	13.599	13.516	13.129	11.635	11.390	12.048	10.804	11.599	12.892	14.674	13.701
TAX REVENUES	12.018	11.421	11.063	11.547	11.905	11.542	10.349	10.076	10.521	9.523	10.303	10.654	12.216	10.968
Bureau of Internal Revenue	11.390	6.500	6.584	6.737	6.733	6.566	6.048	5.940	5.621	5.873	7.196	7.614	8.331	10.968
Domestic Based	5.393	6.500	6.584	6.737	6.733	6.550	6.034	5.923	5.612	5.764	6.917	7.557	8.292	7.863
Income & Profits	2.684	2.718	2.668	3.092	2.841	2.748	2.555	2.506	2.391	2.306	3.138	3.115	3.099	3.327
Excise	1.574	1.887	1.918	2.015	1.923	1.829	1.676	1.713	1.676	1.975	2.268	2.665	3.219	2.379
Sales Tax and Licenses	1.136	1.177	1.473	1.307	1.747	1.770	1.561	1.467	1.301	1.249	1.286	1.504	1.725	1.584
Tax on Property	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.046
Other Domestic Taxes	0.000	0.718	0.525	0.323	0.223	0.204	0.241	0.237	0.244	0.233	0.225	0.273	0.249	0.526
International Trade	5.996	0.000	0.000	0.000	0.000	0.015	0.014	0.017	0.009	0.108	0.279	0.057	0.040	3.105
Travel Tax	4.711	0.000	0.000	0.000	0.000	0.015	0.014	0.017	0.009	0.037	0.243	0.053	0.040	0.000
Foreign Exchange Tax	1.285	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.071	0.036	0.004	0.000	0.000
Bureau of Customs	0.000	4.598	4.100	4.424	4.348	4.382	3.666	3.606	4.353	3.265	2.823	2.846	3.695	0.000
Import Duties and Taxes	0.000	4.179	3.710	4.176	4.010	4.221	3.562	3.521	4.284	2.935	2.655	2.743	3.693	0.000
Export Taxes	0.000	0.420	0.390	0.248	0.338	0.161	0.104	0.086	0.069	0.330	0.168	0.104	0.002	0.000
Other Offices	0.628	0.323	0.379	0.386	0.824	0.595	0.636	0.531	0.547	0.385	0.284	0.194	0.189	0.000
NONTAX REVENUES	2.712	2.058	1.960	2.052	1.612	1.587	1.485	1.314	1.527	1.281	1.297	2.238	2.458	2.732

1/Calculated based on data from the Bureau of Treasury (BT) and National Statistical Coordination Board (NSCB).

Annex Table 7
CUMULATIVE DISTRIBUTION OF INCOME AND INDIVIDUAL INCOME TAX BURDEN BEFORE AND AFTER TAX REFORM
(%)

Decile	Cumulative Distribution of Income	Cumulative Distribution of Tax Burden	
		Before Reform	After Reform
1	2.02	0.03	0.00
2	5.23	0.06	0.00
3	9.32	0.16	0.01
4	14.31	0.31	0.02
5	20.33	0.70	0.05
6	27.59	1.57	0.21
7	36.53	3.91	0.87
8	47.91	9.16	3.68
9	63.56	22.24	15.58
10	100.00	100.00	100.00
Suit's Index		0.483	0.5423

Note : Suit's Index of Progressivity varies from -1 (for extreme regressivity) and +1 (for extreme progressivity).

Source: Manasan 1990a (forthcoming).

Annex Table 8
NOMINAL TAX RATES, EFFECTIVE TAX RATES AND TAXATION OF INPUTS IMPLIED
BY THE SALES TAX SYSTEM OF 1987 AND VAT OF 1988

Code	DESCRIPTION	1988 E	1988 T	1988 E-T	1987 E	1987 T	1987 E-T
1	Palay	0.012206440	0.001038905	0.011167535	0.046247775	0.014114878	0.032132896
2	Corn	0.008582591	0.000445806	0.008136785	0.033075882	0.009972651	0.023103231
3	Coconut	0.003847476	0.000279268	0.003568208	0.011707225	0.002569857	0.009137367
4	Sugarcane	0.010447426	0.000346411	0.010101014	0.039875662	0.011169670	0.028705992
5	Banana	0.013561164	0.002457445	0.011103719	0.043146775	0.012491813	0.030654962
6	Other crops incl. agric. services	0.004101390	0.000528914	0.003572476	0.013143112	0.003664230	0.009478881
7	Livestock and its products	0.013263549	0.000937704	0.012325844	0.129356417	0.044499730	0.084856687
8	Poultry and its products	0.014445973	0.001494834	0.012951139	0.115877619	0.040369649	0.075507970
9	Fishery	0.016873360	0.002866867	0.014006492	0.036363590	0.007185093	0.029178497
10	Forestry and logging	0.010080670	0.000966391	0.009114278	0.020449509	0.002153760	0.018295749
11	Metallic mining	0.104652478	0.081511347	0.023141131	0.201155546	0.154212011	0.046943535
12	Nonmetallic mining and quarrying	0.103973213	0.084406534	0.019566679	0.190515267	0.159650564	0.030864702
13	Rice and corn milling	0.012173114	0.000005681	0.012167432	0.037713998	0.000010930	0.037703067
14	Sugar milling and refining	0.013707193	0.000218326	0.013488867	0.069463813	0.030587217	0.038876596
15	Milk and other dairy products	0.072417987	0.033286200	0.039131787	0.195108289	0.085134504	0.109973704
16	Coconut oil, cake and meal	0.103457377	0.076820054	0.026637322	0.093691949	0.044567990	0.049123959
17	Refined cooking oil and margarine	0.105158496	0.039863137	0.065295359	0.244780395	0.164696205	0.080084190
18	Meat and meat products	0.057648866	0.044884851	0.012764015	0.173540549	0.083677600	0.089862949
19	Flour and other grain mill products	0.099623161	0.072319795	0.027303365	0.206692206	0.146796326	0.059895880
20	Animal feeds	0.021371703	0.004098375	0.017273327	0.209918771	0.155097855	0.054820915
21	Other processed food	0.102948459	0.068198835	0.034749624	0.227599923	0.146443788	0.081156135
22	Beverage industries	0.100761652	0.061894866	0.038866786	0.228380511	0.141423395	0.086957116
23	Tobacco manufactures	0.099115323	0.056200098	0.042915224	0.067222163	0.019148579	0.048073584
24	Textiles and textile goods	0.105594872	0.058813327	0.046781545	0.206576229	0.112047536	0.094528693
25	Wearing apparel and footwear	0.099771406	0.052189166	0.047582239	0.192390705	0.094330881	0.098059823
26	Lumber, plywood and veneer	0.108350278	0.085992520	0.022357758	0.206816834	0.161713132	0.045103701
27	Other wood, cork and cane products	0.101899713	0.068165444	0.033734268	0.206917514	0.141305980	0.065611534
28	Furniture and fixtures	0.103126777	0.044525409	0.058601368	0.224465150	0.110484404	0.113980745
29	Paper and paper products	0.110111855	0.054525236	0.055586618	0.346293716	0.195664298	0.150629417
30	Publishing and printing	0.077784271	0.025322564	0.052461706	0.243349638	0.093824917	0.149524721
31	Leather and leather products	0.099773472	0.059893330	0.039880141	0.275827359	0.165145338	0.110682021
32	Rubber and plastic products	0.102928431	0.051367416	0.051561015	0.212176203	0.103270117	0.108906086
33	Drugs and medicines	0.104496068	0.055010705	0.049485363	0.286450999	0.164414499	0.122309500
34	Basic industrial chemicals	0.106742453	0.054362506	0.052379947	0.240820156	0.150635722	0.090184433
35	Fertilizer	0.080175177	0.021455381	0.058719795	0.255854178	0.129225158	0.126629020
36	Other chemical products	0.102806194	0.048372700	0.054433494	0.236922719	0.149936915	0.086985804
37	Petroleum products	0.099995666	0.042875193	0.057120473	0.192047211	0.081676844	0.110370367
38	Cement manufacture	0.133266767	0.076586567	0.056680199	0.262704609	0.149890357	0.112814251
39	Other nonmetallic mineral products	0.109500939	0.060487660	0.049013278	0.240557495	0.142119812	0.098437683
40	Basic metal industries	0.110289188	0.042473970	0.067815217	0.211665198	0.080128572	0.131536625

nnex Table B (cont'd)

DESCRIPTION	1988 E	1988 T	1988 E-T	1987 E	1987 T	1987 E-T
Metal products	0.107150686	0.045578061	0.061572624	0.205961550	0.086026006	0.119935544
Machinery except electrical	0.104144780	0.052759315	0.051385464	0.220429829	0.117067689	0.103362139
Electrical machinery	0.103967848	0.050613872	0.053353976	0.272886579	0.146442250	0.126444329
Transport equipment	0.102718636	0.050779305	0.051939331	0.248432484	0.133787591	0.114644892
Miscellaneous manufactures incl. scrap	0.103143542	0.064034393	0.039109149	0.207494809	0.125102935	0.082391874
Construction	0.102125077	0.058438532	0.043686545	0.174507211	0.086020679	0.088486531
Electricity	0.059168414	0.001386567	0.057781847	0.116366090	0.003532858	0.112833231
Gas and steam	0.059569247	0.004047136	0.055522110	0.120258125	0.010580508	0.109677617
Water works	0.049317170	0.012189124	0.037128045	0.112932444	0.032404563	0.080527880
Busline operation	0.088403621	0.039305272	0.049098349	0.155514427	0.052828228	0.102686198
Other passenger land transport	0.083120612	0.039625271	0.043495341	0.143688303	0.052779962	0.090908340
Road freight transport	0.043832980	0.006795215	0.037037765	0.095717915	0.017508318	0.078209597
Water transport	0.033972256	0.004623730	0.029348526	0.073631489	0.009584375	0.064047114
Air transport	0.030979348	0.004577754	0.026401594	0.067023934	0.010400575	0.056623359
Supporting & allied services to transport	0.016626864	0.001700004	0.014926860	0.036960729	0.004221556	0.032739173
Communications	0.021935079	0.004877811	0.017057268	0.055269461	0.013538693	0.041730767
Storage and warehousing	0.107597580	0.086662395	0.020935185	0.046665160	0.004532188	0.042132972
Wholesale and retail trade	0.011474089	0.001976107	0.009497982	0.025360137	0.004448608	0.020911529
Banks, nonbanks and insurance	0.011692488	0.002225414	0.009467073	0.029144647	0.005686254	0.023458393
Real estate and ownership of a dwelling	0.010585999	0.003069315	0.007516684	0.020434170	0.005608018	0.014826151
Government services	0	0	0	0	0	0
Private education services	0.013351522	0.002022631	0.011328890	0.030359021	0.004854537	0.025504483
Private health services	0.023727045	0.006804925	0.016922119	0.060264105	0.016502185	0.043761919
Hotels and restaurants	0.040820557	0.011012475	0.029808082	0.098897491	0.024650785	0.074246705
Other private services	0.022497091	0.004644128	0.017852962	0.049761016	0.010725930	0.039035085
Average	0.064814694	0.032265208	0.032549486	0.143889600	0.072074079	0.071815520

Manasan, 1990b

Annex Table 9
TAX ON PETROLEUM PRODUCTS, 1986-1988

Date	Product	TOTAL	Specific Tax	Ad Valorem Tax	Whole-Sale Posted Price (WPP)	Percent of Tax to WPP TOTAL	Specific Tax	Ad Valorem Tax
Jan. 25, 1986	AVERAGE	1.4250	0.6490	0.7760	5.4190	26.2964	11.9764	14.3200
	Premium	2.6170	1.4900	1.1270	7.1260	36.7247	20.9093	15.8153
	Diesel	1.2040	0.2690	0.9350	5.4540	22.0755	4.9322	17.1434
	Fuel Oil	0.6840	0.4430	0.2410	4.1220	16.5939	10.7472	5.8467
Mar. 20, 1986	AVERAGE	1.3610	0.6490	0.7120	4.9190	27.6682	13.1937	14.4745
	Premium	2.5670	1.4900	1.0770	6.8760	37.3328	21.6696	15.6632
	Diesel	1.1210	0.2690	0.8520	4.9940	22.4469	5.3865	17.0605
	Fuel Oil	0.6410	0.4430	0.1980	3.4720	18.4620	12.7592	5.7028
May 22, 1986	AVERAGE	1.5360	1.0360	0.5000	4.3750	35.1086	23.6800	11.4286
	Premium	3.2760	2.4890	0.7870	6.6060	49.5913	37.6779	11.9134
	Diesel	1.1210	0.5230	0.5980	4.4740	25.0559	11.6898	13.3661
	Fuel Oil	0.6410	0.5110	0.1300	2.8150	22.7709	18.1528	4.6181
Aug. 1, 1986	AVERAGE	1.3150	0.9190	0.3960	4.0400	32.5495	22.7475	9.8020
	Premium	3.2390	2.4890	0.7500	6.6060	49.0312	37.6779	11.3533
	Diesel	1.0860	0.5230	0.5630	4.4740	24.2736	11.6898	12.5838
	Fuel Oil	0.6410	0.5110	0.1300	2.5030	25.6093	20.4155	5.1938
Oct. 15, 1986	AVERAGE	1.2550	0.9190	0.3360	4.0400	31.0644	22.7475	8.3168
	Premium	3.2110	2.4890	0.7220	6.6158	48.5353	37.6221	10.9133
	Diesel	0.9720	0.5230	0.4490	4.4830	21.6780	11.6642	10.0138
	Fuel Oil	0.6140	0.5110	0.1030	2.5045	24.5159	20.4033	4.1126
Nov. 1, 1986	AVERAGE	1.3070	0.9700	0.3370	4.0530	32.2477	23.9329	8.3148
	Premium	3.2110	2.4890	0.7220	6.6158	48.5353	37.6221	10.9133
	Diesel	0.9720	0.5230	0.4490	4.4830	21.6780	11.6642	10.0138
	Fuel Oil	0.6140	0.5110	0.1030	2.5045	24.5159	20.4033	4.1126

Annex Table 9 (cont'd)

Date	Product	TOTAL	Specific Tax	Ad Valorem Tax	Whole-Sale Posted Price (WPP)	Percent of Tax to WPP: TOTAL	Percent of Tax to WPP: Specific Tax	Percent of Tax to WPP: Ad Valorem Tax
Jan. 1, 1987	AVERAGE	1.3930	0.9270	0.4660	4.0530	34.3696	22.8719	11.4977
	Premium	3.4200	2.4890	0.9310	6.6158	51.6944	37.6221	14.0724
	Diesel	1.1550	0.5230	0.6320	4.4838	25.7594	11.6642	14.0952
	Fuel Oil	0.6650	0.5110	0.1540	2.5045	26.5522	20.4033	6.1489
Mar. 1, 1987	AVERAGE	1.6730	1.0280	0.6450	4.2910	38.9886	23.9571	15.0315
	Premium	3.4560	2.4890	0.9670	6.6158	52.2386	37.6221	14.6165
	Diesel	1.3100	0.5230	0.7870	4.4838	29.2163	11.6642	17.5521
	Fuel Oil	0.7130	0.5110	0.2020	2.5045	28.4688	20.4033	8.0655
Jul. 14, 1987	AVERAGE	1.4390		1.4390	4.2910	33.5353	0.0000	33.5353
	Premium	3.5712		3.5712	6.6158	53.9799	0.0000	53.9799
	Diesel	1.1298		1.1298	4.4838	25.1974	0.0000	25.1974
	Fuel Oil	0.0000			2.5045	0.0000	0.0000	0.0000
Aug. 15, 1987	AVERAGE	1.4450		1.4450	5.0830	28.4281	0.0000	28.4281
	Premium	3.5897		3.5897	7.9158	45.3485	0.0000	45.3485
	Diesel	1.1551		1.1551	5.3628	21.5391	0.0000	21.5391
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Aug. 26, 1987	AVERAGE	1.1758		1.1758	4.6210	25.4447	0.0000	25.4447
	Premium	3.4636		3.4636	7.2158	48.0002	0.0000	48.0002
	Diesel	1.0919		1.0919	4.9728	21.9574	0.0000	21.9574
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Sept. 1, 1987	AVERAGE	1.2207		1.2207	4.6214	26.4141	0.0000	26.4141
	Premium	3.5374		3.5374	7.2158	49.0230	0.0000	49.0230
	Diesel	1.1171		1.1171	4.9728	22.4642	0.0000	22.4642
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Sept. 18, 1987	AVERAGE	1.2207		1.2207	4.5992	26.5416	0.0000	26.5416
	Premium	3.5374		3.5374	7.1846	49.2359	0.0000	49.2359
	Diesel	1.1171		1.1171	4.9416	22.6060	0.0000	22.6060
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Nov. 1, 1987	AVERAGE	1.2025		1.2025	4.5993	26.1453	0.0000	26.1453
	Premium	3.4785		3.4785	7.1846	48.4161	0.0000	48.4161
	Diesel	1.0970		1.0970	4.9416	22.1993	0.0000	22.1993
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Nov. 19, 1987	AVERAGE	1.1657		1.1657	4.5993	25.3452	0.0000	25.3452
	Premium	3.3598		3.3598	7.1846	46.7639	0.0000	46.7639
	Diesel	1.0564		1.0564	4.9416	21.3777	0.0000	21.3777
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000

Annex Table 9 (cont'd)

Date	Product	TOTAL	Specific Tax	Ad Valorem Tax	Whole-Sale Posted Price (WPP)	Percent of Tax to WPP: TOTAL	Percent of Tax to WPP: Specific Tax	Percent of Tax to WPP: Ad Valorem Tax
Jan. 1, 1988	AVERAGE	1.0416		1.0416	4.4150	23.5923	0.0000	23.5923
	Premium	3.2083		3.2083	7.1846	44.6552	0.0000	44.6552
	Diesel	1.0701		1.0701	4.9416	21.6549	0.0000	21.6549
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Mar. 1, 1988	AVERAGE	1.0289		1.0289	4.2583	24.1622	0.0000	24.1622
	Premium	3.1599		3.1599	7.1846	43.9816	0.0000	43.9816
	Diesel	1.0694		1.0694	4.9416	21.6400	0.0000	21.6400
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
May 3, 1988	AVERAGE	1.0584		1.0584	4.5218	23.4066	0.0000	23.4066
	Premium	3.0421		3.0421	7.1846	42.3420	0.0000	42.3420
	Diesel	1.0510		1.0510	4.9416	21.2684	0.0000	21.2684
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
May 3, 1988	AVERAGE	1.0584		1.0584	4.3569	24.2925	0.0000	24.2925
	Premium	3.0421		3.0421	6.6846	45.5091	0.0000	45.5091
	Diesel	1.0510		1.0510	4.6916	22.4017	0.0000	22.4017
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Jul. 1, 1988	AVERAGE	0.9633		0.9633	4.2368	22.7365	0.0000	22.7365
	Premium	3.1006		3.1006	6.6846	46.3842	0.0000	46.3842
	Diesel	1.0401		1.0401	4.6916	22.1694	0.0000	22.1694
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Aug. 18, 1988	AVERAGE	0.9633		0.9633	4.1025	23.4808	0.0000	23.4808
	Premium	3.1006		3.1006	6.4846	47.8148	0.0000	47.8148
	Diesel	1.0401		1.0401	4.3916	23.6839	0.0000	23.6839
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Sept. 1, 1988	AVERAGE	0.8963		0.8963	4.1242	21.7327	0.0000	21.7327
	Premium	2.8742		2.8742	6.4846	44.3235	0.0000	44.3235
	Diesel	0.9258		0.9258	4.3916	21.0812	0.0000	21.0812
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Nov. 1, 1988	AVERAGE	0.8044		0.8044	4.1509	19.3789	0.0000	19.3789
	Premium	2.5261		2.5261	6.4846	38.9554	0.0000	38.9554
	Diesel	0.7932		0.7932	4.3916	18.0618	0.0000	18.0618
	Fuel Oil	0.0000			2.8225	0.0000	0.0000	0.0000
Nov. 8, 1988	AVERAGE	0.8044		0.8044	3.3852	23.7623	0.0000	23.7623
	Premium	2.5261		2.5261	5.4846	46.0581	0.0000	46.0581
	Diesel	0.7932		0.7932	3.3916	23.3872	0.0000	23.3872
	Fuel Oil	0.0000			2.3225	0.0000	0.0000	0.0000

Source: Annex 2b of the Final Report of the Ad Hoc Inter-Agency Committee on Petroleum Product Tax Structure (July 26, 1988).

Annex Table 10

EFFECTIVE TAX RATES AND TAXATION OF INPUTS IMPLIED BY THE EXCISE TAX ON FUEL OIL, 1987 a/

Code	DESCRIPTION	1987 E2	T2	E2-T2
1	Palay	0.005949576	0	0.005949576
2	Corn	0.004883226	0	0.004883226
3	Coconut	0.002591683	0	0.002591683
4	Sugarcane	0.007660269	0	0.007660269
5	Banana	0.006031442	0	0.006031442
6	Other crops incl. agric. services	0.002378766	0	0.002378766
7	Livestock and its products	0.007755781	0	0.007755781
8	Poultry and its products	0.009121831	0	0.009121831
9	Fishery	0.016627862	0	0.016627862
10	Forestry and logging	0.129145990	0	0.012914699
11	Metallic mining	0.024643843	0	0.024643843
12	Nonmetallic mining and quarrying	0.023234661	0	0.023234661
13	Rice and corn milling	0.011321084	0	0.011321084
14	Sugar milling and refining	0.015869302	0	0.015869302
15	Milk and other dairy products	0.012842327	0	0.012842327
16	Coconut oil, cake and meal	0.019434361	0	0.019434361
17	Refined cooking oil and margarine	0.023417515	0	0.023417415
18	Meat and meat products	0.009084032	0	0.009084032
19	Flour and other grain mill products	0.009832251	0	0.009832251
20	Animal feeds	0.012499521	0	0.012499521
21	Other processed food	0.015498023	0	0.015498023
22	Beverage industries	0.015311875	0	0.015311875
23	Tobacco manufactures	0.010612980	0	0.010612980
24	Textiles and textile goods	0.024721863	0	0.024721863
25	Wearing apparel and footwear	0.013469840	0	0.013469840
26	Lumber, plywood and veneer	0.028334854	0	0.028334854
27	Other wood, cork and cane products	0.016859204	0	0.016859204
28	Furniture and fixtures	0.018804915	0	0.018804915
29	Paper and paper products	0.031640192	0	0.031640192
30	Publishing and printing	0.017632837	0	0.017632837
31	Leather and leather products	0.009867655	0	0.009867655
32	Rubber and plastic products	0.017955381	0	0.017955381
33	Drugs and medicines	0.015435480	0	0.015435480
34	Basic industrial chemicals	0.025982837	0	0.025982837
35	Fertilizer	0.042436933	0	0.042436933
36	Other chemical products	0.018761003	0	0.018761003
37	Petroleum products	0.199815751	0.184	0.015815751
38	Cement manufacture	0.080728023	0	0.080728023
39	Other nonmetallic mineral products	0.033490574	0	0.033490574
40	Basic metal industries	0.033198017	0	0.033198017

Annex Table 10 (cont'd)

Code	DESCRIPTION	1987 E2	1987 T2	1987 E2-T2
41	Metal products	0.026561393	0	0.026561393
42	Machinery except electrical	0.021002510	0	0.021025101
43	Electrical machinery	0.018942036	0	0.018942036
44	Transport equipment	0.016250867	0	0.016250867
45	Miscellaneous manufactures incl. scrap	0.017281440	0	0.017281440
46	Construction	0.018633443	0	0.018633443
47	Electricity	0.107704226	0	0.107704263
48	Gas and steam	0.092730608	0	0.092730608
49	Water works	0.028171688	0	0.028171688
50	Busline operation	0.061857192	0	0.061857192
51	Other passenger land transport	0.048739561	0	0.048739561
52	Road freight transport	0.046911407	0	0.046911407
53	Water transport	0.042861581	0	0.042861581
54	Air transport	0.027953349	0	0.027953349
55	Supporting & allied services to transport	0.014782780	0	0.014782780
56	Communications	0.069011748	0	0.009011748
57	Storage and warehousing	0.028489457	0	0.028489457
58	Wholesale and retail trade	0.006200197	0	0.006200197
59	Banks, nonbanks and insurance	0.003915742	0	0.003915742
60	Real estate and ownership of a dwelling	0.005039482	0	0.005039482
61	Government services	0	0	0.000000000
62	Private education services	0.010064428	0	0.010064428
63	Private health services	0.009829551	0	0.009829551
64	Hotels and restaurants	0.018949782	0	0.018949782
65	Other private services	0.012423165	0	0.012423165
	Average	0.024661268		0.021830499

a/

The weighted average tax rate on fuel oil in 1987 is 10.4 percent. The tax rate was 26.5 percent from January 1 to March 1, 1987; 20.5 percent from March 1 to July 14, 1987 and zero thereafter.

Annex Table 11
PERCENTAGE DISTRIBUTION OF NATIONAL GOVERNMENT EXPENDITURES NET OF DEBT SERVICE
BY SECTOR, ON AN OBLIGATION BASIS, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
Total Economic Services	49.76	49.78	49.73	41.29	47.85	39.18	37.84
Agriculture	5.72	5.70	5.75	6.79	1.72	10.49	7.89
Agrarian Reform	0.62	0.71	0.49	3.03	0.40	1.43	6.34
Natural Resources	4.93	2.02	9.09	1.61	1.35	1.73	1.73
Industry	1.94	2.37	1.33	1.71	0.32	3.24	1.61
Trade	0.33	0.35	0.30	0.06	0.01	0.04	0.10
Tourism	0.23	0.29	0.14	0.13	0.02	0.10	0.18
Power & Energy	6.25	7.88	3.93	0.47	0.16	1.57	-0.13
Water Resources Development	1.20	1.35	0.99	0.38	0.01	0.66	0.46
Transportation & Communication	21.00	25.43	14.66	15.61	11.87	17.66	16.95
Other Economic Services	7.54	3.68	13.06	11.50	31.99	2.89	2.72
Total Social Services	23.30	22.81	23.99	28.75	29.13	28.24	28.84
Education	13.65	13.31	14.14	18.73	16.14	19.85	19.88
Health	4.10	4.05	4.36	4.68	3.78	4.71	5.35
Social Services, Labor & Employment	1.52	1.66	1.33	0.96	1.17	0.84	0.70
Housing & Community Development	3.73	3.59	3.93	4.17	7.87	2.65	2.45
Other Social Services	0.21	0.20	0.23	0.21	0.18	0.19	0.26
National Defense	12.95	14.46	10.79	9.70	8.88	10.19	9.97
Total Public Services	13.99	12.95	15.48	20.26	14.13	22.47	23.35
Public Administration	8.57	8.25	9.03	14.67	7.73	17.63	17.81
Peace and Order	3.91	3.48	4.52	5.04	4.61	4.83	5.54
Others	1.52	1.23	1.93	0.55	1.79	0.00	0.00
Debt Service	23.27	9.10	43.56	63.34	32.46	82.34	72.84
Grand Total - Debt Service	100.00	100.00	100.00	100.00	100.00	100.00	100.00

1/ Calculated based on data from the Department of Budget and Management (DBM). Agency level expenditures were classified according to function by using the COA Chart of Accounts.

Annex Table 12
NOMINAL GROWTH RATE OF NATIONAL GOVERNMENT EXPENDITURES
BY ECONOMIC CLASSIFICATION, ON AN OBLIGATION BASIS, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1
TOTAL	16.62	16.68	16.65	29.12	29.25	35.88	22
I. Current Operating Expenditures	18.32	17.89	19.33	36.79	23.33	64.86	25
A. Personal Services	16.71	17.10	15.79	32.78	34.98	10.35	56
B. Maintenance & Other Operating Expenditures	19.25	18.37	21.31	37.73	17.44	96.56	15
a. Interests	20.75	27.76	5.85	163.54	392.25	224.98	14
b. Transfers	11.45	16.43	8.63	25.04	22.75	-3.67	65
1. to local government	19.82	22.11	14.64	6.06	-3.41	-40.53	139
2. to all government corporations	7.00	7.37	6.14	47.47			54
3. to others	-2.44	14.35	-32.64	75.72	351.95	1.89	17
c. Loan Repayment & Sinking Fund Contribution	51.36	48.65	38.57	-92.97	-67.85	-100.06	4915
d. Other MOE	18.49	11.59	7.96	19.91	20.63	33.88	3
II. Capital Outlay	13.36	14.38	11.02	3.19	-43.65	-24.88	7
A. Land, Land Improvements & Structure Outlays	-6.58	2.25	-3.31	18.54	-37.85	149.49	6
B. Buildings & Structures			13.85	21.63	129.69	-36.73	24
C. Equipment	13.77	-2.63	64.56	-11.23	-73.57	158.32	37
D. Investment Outlay	22.83	21.78	22.13	-44.85	-9.29	-62.87	-51
a. to local government			60.46	78.59	-92.45	2679.75	136
b. to all government corporations	23.51	23.89	22.82	-43.26	-18.24	-62.49	-51
c. to others	-17.69	-1.83	-58.68	23.46	657.18	-34.19	-78
E. Loans Outlay	63.78	113.35	-11.77	79.69	552.91	-27.37	25
a. to local government			21.14	306.12	438.66	1087.35	13
b. to all government corporations	156.17	386.41	-12.73	43.63	591.51	-49.28	-15
c. to others	22.99	26.95	14.22	272.84	-85.41	14763.29	137

1/
Calculated based on data from the Department of Budget and Management (DBM).

Annex Table 13
REAL GROWTH RATE OF NATIONAL GOVERNMENT EXPENDITURES
BY ECONOMIC CLASSIFICATION, ON AN OBLIGATION BASIS, 1975-1988 1/

	1975-1985	1975-1982	1983-1985	1986-1988	1986	1987	1988
TOTAL	1.42	5.22	-6.94	21.43	27.48	25.78	11.74
I. Current Operating Expenditures	2.98	6.39	-4.88	28.64	21.64	52.68	14.78
A. Personal Services	1.49	5.67	-7.63	24.88	33.86	2.33	43.62
B. Maintenance & Other Operating Expenditures	3.78	6.82	-3.23	38.48	15.83	81.94	5.48
a. Interests	5.81	15.29	-15.56	147.85	385.51	208.74	4.28
b. Transfers	-3.08	5.87	-19.72	17.59	21.07	-18.83	58.63
1. to local government	4.28	18.19	-8.55	-8.25	-4.73	-52.36	118.63
2. to all government corporations	-6.95	-3.11	-15.33	38.78			41.85
a. to financial government corps.			81.67				
b. to nonfinancial government corps.	-8.44	-3.32	-19.36				
3. to others	-15.16	3.19	-46.27	65.26	345.76	-5.68	7.35
c. Loan Repayment & Sinking Fund Contribution	31.80	34.14	26.58	-93.39	-68.29		4478.33
d. Other MOE	-3.91	8.78	-13.88	12.77	18.98	25.78	-4.17
Capital Outlay	-1.42	3.21	-11.44	-1.07	41.69	-38.48	-1.81
. Land, Land Improvements & Structure Outlays	-13.11	-7.73	-24.46	11.48	-37.91	138.94	-3.37
B. Buildings & Structures			-9.82	14.58	126.55	-41.43	13.37
Equipment	-8.88	-12.13	31.28	-16.31	-75.98	92.83	25.23
Investment Outlay	6.12	18.08	-2.57	-48.13	-18.53	-64.89	-55.58
a. to local government			28.08	68.44	-92.55	2473.82	115.45
b. to all government corporations	6.97	11.58	-2.82	-48.52	-11.47	-65.28	-55.61
c. to others	-38.16	-35.69	-68.66	13.24	774.77	-39.08	-73.36
E. Loans Outlay	42.36	92.53	-29.62	69.08	543.97	-34.62	14.64
a. to local government			-3.36	281.95	423.48	925.88	3.87
b. to all government corporations	122.78	266.75	-38.38	35.89	582.84	-53.85	-23.81
c. to others	6.96	14.56	-8.88	249.89	-85.61	13639.48	116.71

1/ ...ated based on data from the Department of Budget and Management (DBM) and National Statistical Coordination Board (NSCB).

Annex Table 14
INCENTIVE AVAILMENTS BY TYPE OF INCENTIVE
(₱M)

	1978	1979	1980	1981	1982	1983	1984	1985
TOTAL	1,136	1,043	1,539	1,475	2,066	1,918	3,553	4,301
Tax Deductions	754	456	734	546	675	599	1,078	2,433
Organizational expenses	34	0	0	0	0	0	0	0
Accelerated depreciation	153	0	0	0	0	0	0	0
Loss carryover a/	62	35	100	98	119	7	298	375
Expansion investment allowance	153	90	175	84	149	172	236	649
Labor training	2	1	1	4	4	2	3	3
Labor and material cost	172	0	0	0	0	0	0	0
Investment allowance	78	160	51	39	27	82	8	100
Reduced Income tax	4	170	407	322	376	286	532	1,299
Export trader	4	0	0	0	0	0	0	0
Service exporter	90	0	0	0	0	0	0	0
New brand name	0	0	0	0	0	0	0	0
Water treatment	0	0	0	0	0	0	0	0
National dev. fund allowance	0	0	0	0	0	58	1	0
1% of incremental sales	0	0	0	0	0	0	1	7
Other deductions	1	0	0	0	0	0	0	0
Tax Exemptions	286	441	637	750	1,150	1,189	2,192	1,542
Duty and tax on machinery a/	142	301	508	546	841	622	1,482	1,391
Sales tax a/	111	98	103	164	203	523	598	41
Capital gains tax	33	5	26	38	97	33	77	75
Breeding stocks a/	0	37	1	1	9	11	32	0
Percentage tax	0	0	0	0	0	0	3	34
Export tax a/	0	0	0	0	0	0	0	0
Other exemptions	0	0	0	0	0	0	0	0
Tax Credits	95	146	168	178	241	130	282	606
Sales tax on raw materials a/	57	82	61	86	101	58	85	216
Domestic equipment a/	8	38	43	58	108	49	78	67
Infrastructure works	1	0	0	0	0	0	0	0
Witholding tax on interest a/	29	25	44	33	32	23	26	15
New value earned a/	0	0	0	0	0	0	44	133
Net local content a/	0	0	0	0	0	0	49	174

a/
Available under P.D. 1789 as amended by B.P. 391 and E.O. 1945.

Note : Data shown are for availments approved by the Board of Investments (BOI). Not all approved incentives are actually used.

Source: Board of Investments (BOI). As cited by World Bank, 1987.

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