GENERAL AGREEMENT
ON TARIFFS AND TRADE

RESTRICTED
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Committee on Balance-of-Payments Restrictions

FULL CONSULTATION WITH THE PHILIPPINES UNDER ARTICLE XVIII:12(b)

Background paper by the Secretariat[1]

1. This paper has been prepared in accordance with paragraph 7 of the Declaration on trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205).

I. Previous Consultations with the Philippines

2. The Philippines has held six consultations in the Committee since its accession to the GATT in 1980 (1980, 1982, 1984, 1986, 1988 and 1991). At the last full consultation, held on 10 December 1986, the Committee noted that the Philippines had pursued a balanced package of domestic and external adjustment policies, including fiscal and monetary measures, trade and exchange control liberalization and flexible exchange rate policies, which had led to a considerable improvement in the balance-of-payments situation. The Committee observed that remaining import restrictions covered by the present programme were limited in scope and welcomed the Philippines' undertaking to notify all such remaining measures in detail to GATT. The Committee looked forward to the phasing out of remaining restrictions according to the timetable set out by the Philippines authorities.

3. At the last (simplified) consultation, held on 19 March 1991, the Committee congratulated the Philippines on its liberalization programme in force, which was being pursued under difficult economic circumstances. Members of the Committee also expressed concerns regarding uncertainties surrounding the import surcharge which had recently been established at 9 per cent. It invited the Philippines authorities to notify this surcharge to the GATT as soon as possible.

4. At the 1991 consultation, the Committee agreed that a full consultation should be held with the Philippines.

II. The Philippines' Trade and Exchange System: Evolution since the last Consultation

5. The Philippines embarked on a programme of trade reform in 1981 to improve the efficiency of resource allocation and to foster the development of internationally competitive industries. This programme has had two main components. First, there has been a significant shift away from

[1]This consultation with the Philippines is being held in conjunction with the Trade Policy Review in the GATT Council. In accordance with the decision of the Committee (BOP/R/199), in such cases the Secretariat prepares only a short factual background paper containing aspects relevant to the work of the Committee. In trade policy related questions, this paper draws on the TPRM report prepared by the Secretariat (C/RM/S/33). The report prepared by the Government of the Philippines for the Trade Policy Review (C/RM/G/33) should be considered as the Basic Document for the Consultation.

quantitative restrictions to more transparent tariff protection. Secondly, both the average level and the dispersion of tariff rates have been reduced, reflecting a diminished reliance on tariffs as sources of revenue and method of protection. To complement these changes, import and export procedures have been simplified and restrictions on foreign exchange transactions on the trade account have been reduced. At the same time, additional incentives have been introduced to encourage exports and to diversify the export base.

(a) Import restrictions

6. At present, imports are classified into three categories according to the degree of restriction involved.[2] Importation of Freely importable items is neither regulated nor prohibited, and does not require the prior approval of, or clearance from, any Government agency. Importation of Regulated commodities requires clearance or permits from appropriate Government agencies, including, in some cases the Central Bank. Importation of Prohibited commodities is not ordinarily allowed under existing laws.[3]

7. Over the last decade, the importation of a substantial number of items has been liberalized.[4] Between 1981 and 1986, before the Import Liberalization Programme(ILP) began, 999 commodities (classified according to the 1977 PSCC Code) had been deregulated. In the first phase of the ILP, between April 1986 and April 1988, a further 1229 items were liberalized. In the second phase, which is yet to be completed, 533 items had been liberalized between September 1988 and December 1992, 135 items continue to be regulated, based on 7-digit Philippines Standard Classification Code (1977) lines. After the completion of Phase II of the ILP in 1994, 69 items will continue to be regulated for health, safety and national defence purposes.[5]

8. Explicit import quotas operate only on two products: feeder cattle, and horses. Gamefowl imports were liberalized in September 1992.[6]

(b) Exchange regulations affecting trade[7]

9. Exchange rates of the Philippine Peso are determined on the basis of demand and supply in the foreign exchange market. However, the authorities intervene when necessary to maintain orderly conditions in the market and in light of their policy objectives. Policy decisions on foreign exchange are made by the Monetary Board and are administered by the Central Bank.

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[2]Until June 1992, imports were classified into five categories: freely importable, prohibited, banned, regulated and liberalized. For further details see document C/RM/S/33, in Chapter IV(2)vii.

[3]The list of Regulated and Prohibited items is presented in Tables IV.6 and IV.8 in document C/RM/S/33.

[4]See Table IV.5 in document C/RM/S/33.

[5]See Table IV.7 in document C/RM/S/33.

[6]See section (2)ix in Chapter IV in Document C/RM/S/33

[7]For more detailed information regarding trade related aspects of the foreign exchange regime see Chapter III in document C/RM/S/33.

10. Recently, the Philippine Government has lifted several restrictions on the flow of foreign exchange. As a rule, foreign exchange may be freely sold and purchased outside the banking system. Previously, only Authorized Agent Banks, authorized foreign exchange agents and Authorized Foreign Exchange Buyers could engage in both sale and purchase operations in foreign exchange. Foreign exchange receipts, acquisitions or earnings may also be deposited in foreign currency accounts, whether in the Philippines or abroad.

11. Since August 1992, Philippine exporters are no longer required to sell their foreign exchange receipts to banks and can retain or invest them, also abroad. Up until 1991, exporters could retain only 2 per cent of their receipts. Thereafter, the amount that they could retain was raised to 40 per cent and subsequently increased to 100 per cent by Central Bank Circular No 1353.

12. In principle, all payments for invisibles are permitted with prior Central bank approval. Since September 1992, the mandatory surrender requirement was eliminated for all types of earnings from services, including remittances from overseas workers.

13. All foreign exchange remittances for imports must be transacted through the Authorized Agent Banks of the Central Bank, and can take place under specified modes of payment.[8]

(c) Import duties and preshipment inspection

14. In the Philippines, a major Tariff Reform Programme is being implemented, based on Executive Order No.470, which took effect on 25 August 1991. The principal objective of the programme is to rationalize the protection structure by reducing the overall level of protection and the dispersion of tariff protection within and across industries.

15. Executive Order No.470 established a new simplified four-tier rate tariff structure: (i) 3 per cent for goods previously exempt from tariffs and those subject to a tariff of 5 per cent; (ii) 10 per cent for raw materials, capital equipment for which no locally produced substitutes are available, and spare parts; (iii) 20 per cent for intermediate and semi-processed goods and capital equipment for which there are locally produced substitutes; and (iv) 30 per cent for finished goods. Several exceptions have been made to the new basic rate structure to address the needs of particular industries.[9] The Tariff and Customs Code of August 1991 also specifies the rates for each year until 1995 which will prevail thereafter unless modified.

16. Estimates by the GATT Secretariat indicate that the current (1992) nominal unweighted average tariff rate is 25.6 per cent, while in 1980 it was over 41 per cent. The nominal unweighted average tariff rate for agricultural products is 41.2 per cent, on industrial products 23 per cent. By 1995, when the tariff reform has been implemented, the simple average tariff is expected to decline to around 20 per cent.

17. An additional import duty (5 per cent, effective 11 December 1990, and subsequently adjusted upward to 9 per cent, effective 18 January 1991) was levied on all imports to boost Government revenues by an estimated amount of about Peso 25.6 billion. The additional levy was originally scheduled to last until 30 June 1992, but the Government decided to lift it with effect from

[8]For information regarding the modes of payment see document C/RM/S/33, Chapter IV, Section (2) (i).

[9]For more information regarding exceptions see Chapter IV, section (2)(ii) in document C/RM/S/33.

1 May 1992. However, certain items continue to be subject to the additional levy of 9 per cent ad valorem.[10]

18. In 1987, to address the problem of misdeclaration of imports, the Government of the Philippines introduced the Comprehensive Import Surveillance Scheme, with the Société General de Surveillance(SGS) as the designated inspector. The preshipment inspection requirement initially applied to imports coming from 10 countries. With effect from 16 March 1992, imports originating from all sources of supply were subject to inspection by the SGS. The minimum value of shipments that require SGS inspection is US$500.

III. Macroeconomic and Trade Developments[11]

(i) Introduction and overview

19. The growth record of the Philippines since the mid-1970s has been one of expansion till the early eighties, followed by a recession and an unsteady recovery beginning in 1986. Real GNP grew at an average annual rate of about 6 per cent between 1970 and 1980. These high rates of growth were financed by high external borrowing, which was largely used for public sector expansion. Growth slowed in 1980-85 as the Philippines was affected by a series of external shocks, including the second oil price increase, the rise in real interest rates, the global recession of the early 1980s and the withdrawal of commercial banks from developing country financing. The internal political situation added to the loss of confidence in the economy. As a result, there was a major recession in 1983-85, real GNP falling by 1.4 per cent annually during 1980-85.

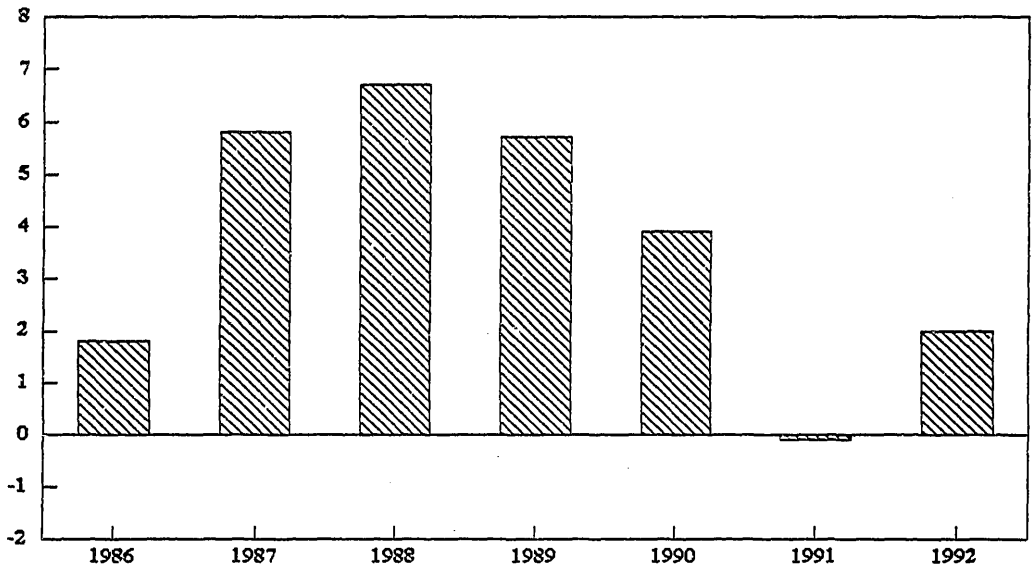
20. The economy recovered beginning in 1986, and real GNP grew by 4.8 per cent on average between 1986 and 1990 (Graph 1). However, GNP growth slowed from 6.7 per cent in 1988 to 5.7 per cent in 1989, and 3.9 per cent in 1990, while at the same time expansionary fiscal and monetary policy led to an increase in inflation, the public sector deficit and the current account imbalance. During the 1990-91 period the country was again confronted with a number of shocks, including a coup attempt in December 1989, a number of natural disasters -including the July 1990 earthquake and the June 1991 eruption of Mount Pinatubo - and the Gulf crisis starting in August 1990. The latter had a negative impact on the current account by raising the country's oil import bill.

21. A stabilization programme was put in place in 1991 that helped contain inflation and reduce the public sector and current account deficits. This was accompanied by a contraction in aggregate demand. Gross domestic investment fell by 14 per cent, private investment fell, as did industrial output. As a result, real GNP remained virtually constant in 1991. Preliminary data for 1992 suggest that real growth will not exceed 2 per cent. The removal of the import surcharge in May 1992 and an increase in domestic consumption is expected to lead to a slight increase in the current account deficit. Based on ten months data, exports for 1992 are estimated to have increased by about 10 per cent. Imports of raw materials and capital goods have increased by over 20 per cent.

[10]These items include: crude petroleum oils and oils obtained from bituminous minerals, lubricating oil, fuel oils, naphtha, gas oils (including diesel oil and other heavy oils), kerosines, motor gasoline and other oils and preparations (excluding low aromatic solvents).

[11]See Chapters I, II and III of document C/RM/S/33. Footnotes have been included in instances where there were important differences between the IMF statistics used in the Secretariat's report and those referred to in the comments by the Philippine government on the final draft of this report.

Graph 1 - Philippines - Real GNP
(Annual percentage change)



Source: IMF.
Note 1992 figure is a projection.

22. National savings have been less than gross domestic investment since 1987, as reflected in inflows of foreign savings, i.e., in current account deficits. In the 1986-89 period these deficits resulted from public sector savings-investment gaps (Table 1). Private sector savings exceeded private investment during this period. However, in 1990 a private sector savings-investment gap also emerged, although the difference between private savings and investment was much smaller than for the public sector. National savings increased from 16.3 per cent of GNP in 1990 - equal to the average achieved over the foregoing five years - to 17.5 per cent of GNP in 1991. Tax and other revenues exceeded current expenditure (i.e., excluding investment) of the public sector in 1991, resulting in public savings of 2.9 per cent of GNP. As private savings were equal to private investment in 1991, the total shortfall of national savings - the current account deficit - was equal to 2.3 per cent of GNP. This was a significant decline as compared to the previous year. In 1990 private investment exceeded private savings by 0.5 per cent of GNP, and the public savings-investment gap reached 5.6 per cent of GNP. The resulting current account deficit was 6.1 per cent of GNP.[12]

23. Gross domestic investment declined sharply after the 1983 crisis. Since 1987 it has been rising, increasing from 16.2 per cent of GNP to 22 per cent in 1990. Most of this rise reflects an increase in private investment. Public investment has fallen markedly since the early 1980s, declining

[12]Philippine Government data indicate public savings in 1991 to be 4.2 per cent of GNP; the private savings investment gap in 1990 to be 1.8 per cent of GNP and the 1990 public savings-investment gap to be 4.3 per cent of GNP. There is agreement on the current account figures.

from 17.6 per cent of GNP in 1983 to about 5 per cent in 1991. Since the mid-1980s, foreign investment has grown as a percentage of new private investment, which is related to the increasing liberalization of rules restricting direct foreign investment.

Table 1
Philippines investment and saving, 1986-92[1]
(Percentage of GNP; end of period)

	1986	1987	1988	1989	1990	1991	1992[4]
Gross domestic investment	13.2	16.2	17.4	22.1	22.4	19.7	19.9
Public	3.0	3.6	3.3	4.3	5.3	5.2	4.7
Private	10.2	12.6	14.1	17.8	17.1	14.6	15.2
Gross national saving	16.5	14.9	16.3	18.7	16.3	17.5	17.8
Public	-0.9	1.5	0.9	-0.4	-0.3	2.9	3.0
Private[2]	17.4	13.4	15.4	18.3	16.6	14.6	14.8
Foreign savings[3]	-3.3	1.3	1.1	3.4	6.1	2.3	2.1
Memorandum items:							
Public investment-saving gap	3.9	2.1	2.4	4.7	5.6	2.3	1.7
of which: National government deficit	(5.1)	(2.9)	(2.8)	(2.1)	(3.4)	(2.1)	(0.6)
Private investment-saving gap	-7.2	-0.8	-1.3	-0.5	0.5	0.0	0.4

1 Components may not add to totals due to rounding.
2 Derived as a residual.
3 Current account deficit (+)/surplus (-) in the balance of payments
4 Projection

Source: IMF.

(ii) Balance of Payments

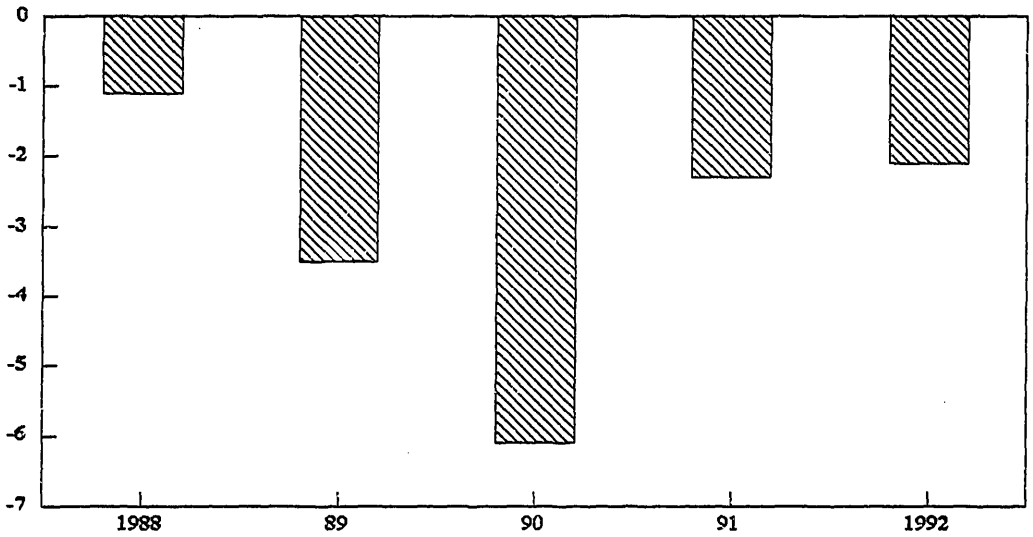
24. Persistent current account deficits occurred in the late 1980s and early 1990s, mainly driven by large merchandise trade imbalances (Table 2 and Graph 2). The current account deficit grew from US$390 million in 1988 to US$2.7 billion (6.1 per cent of GNP) in 1990, reflecting mainly the economic recovery and the increase in domestic demand after 1986 (Table 2). The substantial growth in the current account deficit during 1989-90 was also due in part to a decline in the terms of trade of 9.9 per cent during 1989-90, weak export growth and the unwillingness of policymakers to allow the peso to depreciate. However, the unsustainable current account deficit forced the government to devalue the peso by 25 per cent at the end of 1990. As compared to 1989 this implied a decline in the average market rate against the U.S. dollar of 17 per cent; the real effective exchange rate depreciated almost 16 per cent.

25. The peso depreciation and the implementation of a temporary import levy (imposed in January 1991) led to a narrowing of the current account deficit in 1991, to US$1 billion (2.3 per cent of

GNP). A recovery of world demand for semiconductors and fruit exports helped boost exports. The import levy, the slump in economic activity, the peso depreciation, and a good rice and corn harvest contributed to the slowdown in import growth. The resumption of worker's remittances in the latter half of 1991 and an increase in net transfers - the latter reflecting in part transfers associated with the Mount Pinatubo disaster- further increased revenues. At the same time, substantial capital inflows continued. These were in part autonomous - attracted by high real interest rates - and in part the reflection of a reduction in medium and long-term debt servicing obligations. The overall balance of payments attained a surplus of US$1.4 billion in 1991, as compared to a deficit of US$185 million in 1990. International reserves, which had been relatively stable at some US$2 billion in the late 1980s, increased markedly in 1991 to US$4.5 billion, equivalent to more than three months of imports of goods and services (Graph 3).

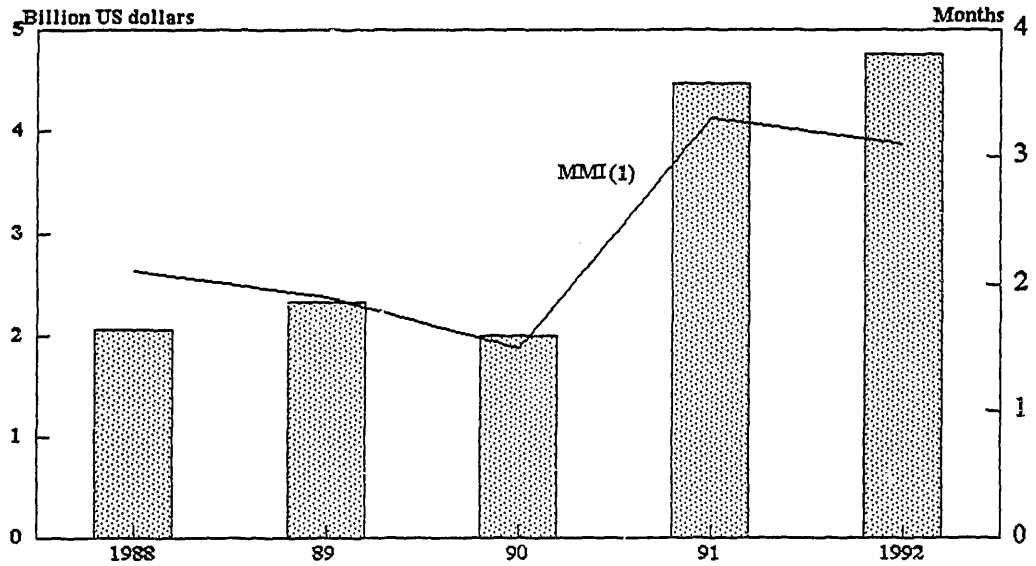
26. The current account deficit declined fruther in the first half of 1992. During the first semester of 1992 both exports and imports of merchandise and commercial services grew in comparison to the same period in 1991. The overall balance of payments is in surplus and is expected to remain so for the year as a whole. Foreign exchange reserves continued to increase during 1992 following the liberalization of the foreign exchange régime. International reserves attained US$5.4 billion in March 1992. The elimination of outstanding swaps and the May debt buyback (see below) lowered reserves to US$4.1 billion in June, almost equal to three months of imports of goods and services. Large capital inflows and the reduction in the current account deficit were accompanied by a substantial appreciation of the peso. Notwithstanding Central Bank intervention, the real effective exchange rate appreciated by 14.6 per cent in 1991 and by a further 7.9 per cent in the first half of 1992.

Graph 2 - Philippines - Current account balance, 1988-92
(Percentage of GNP)



Note: 1992 figure is a projection.
Source: IMF.

Graph 3 - Philippines - Gross international reserves and months of merchandise imports



(1)MMI refers to equivalent months of merchandise imports (right -hand scale).
Note: 1992 figure is a projection.
Source: IMF.

Table 2
Balance of Payments, 1989-92
(millions US dollars)

	1989	1990	1991	1992	1991	1992
				Projection	January - May	
Trade balance	-2598	-4030	-3211	-4165	-1563	-1889
Exports, f.o.b.	7821	8186	8840	9655	3439	3720
Imports, f.o.b	10419	12206	12251	13820	5002	5609
Services and transfers (net)	1142	1325	2178	3023	902	1333
Services (net)	312	611	1351	2115	512	961
Receipts	(4586)	(4842)	(5624)	(6653)	(2227)	(2865)
Interest payments	(2411)	(2154)	(2157)	(1867)	(886)	(841)
Other payments	(1863)	(2077)	(2116)	(2671)	(829)	(1063)
Transfers (net)	830	714	827	908	390	372
Current account	-1456	-2695	-1033	-1142	-661	-556
(In percent of GNP)	(-3.5)	(-6.1)	(-2.3)	(-2.1)	(...)	(...)
Capital account	550	827	825	474	895	41
MLT loans	-753	-458	-427	-1078	-100	-840
Inflows	(1440)	(2638)	(2000)	(2256)	(933)	(802)

Table 2
(Cont'd)

	1989	1990	1991	1992	1991	1992
				Projection	January - May	
Outflows	(2193)	(3096)	(2427)	(3334)	(1033)	(1642)
Foreign investment (net)	843	480	654	1009	333	425
Debt conversion	(306)	(226)	(273)	(313)	(138)	(118)
Other	(537)	(254)	(381)	(696)	(195)	(307)
Short-term capital (net)	-89	19	369	427	307	430
Other	549	786	229	116	355	26
Rescheduling [1]	1357	1683	1613	1695	499	602
Paris Club III	588	610	293	--	...	...
Paris Club IV	...	...	514	1007	...	...
Commercial banks	769	1073	806	688	...	...
Net international reserves (-increase)	-451	185	-1405	-1027	-733	-87
Memorandum items						
Gross official reserves	2324	1993	4470	4762	...	...
(In months of imports)	1.9	1.5	3.3	3.1	...	...
External debt oustanding	27616	28549	29956	30086	...	...
(In percent of GNP)	66.0	64.4	65.7	56.1	...	...
Debt service ratio [2]						
Before rescheduling	38.5	37.7	33.7	28.8	...	...
After rescheduling	27.6	24.8	22.6	18.4	...	...
Interest due in percent of GNP	5.8	4.9	4.7	3.5	...	...

1 Excludes rescheduling of maturing monetary liabilities.
2 Debt service as a percent of exports of goods and services; includes cash value of repayments related to debt conversions, but excludes payments related to 1990 and 1992 buybacks.

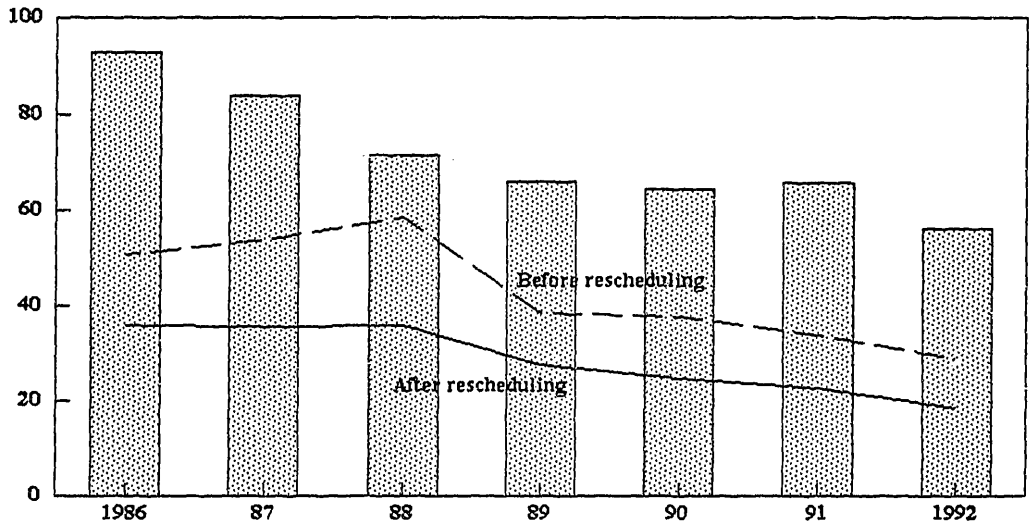
Sources: IMF.

Foreign indebtedness

27. Having relied on external borrowing to cover its current account deficits, the Philippines was faced with a debt crisis in 1982-83. External debt stood at some US$24 billion in 1983 (72 per cent of GNP), with total debt service equal to US$3 billion (36 per cent of exports of goods and services). In 1986 total debt had increased to 95 per cent of GNP (US$28.5 billion), reflecting the economic contraction that occurred after 1983. Debt rescheduling and other forms of debt relief, combined with the resumption in economic growth after 1986 led to a reduction in external debt and debt servicing obligations. External debt fell to 66 per cent of GNP in 1991, while the ratio of total debt service to exports of goods and services declined to 23 per cent (Graph 4). The government has continued to pursue debt relief in 1992. In July a debt reduction package involving US$4.5 billion of medium and long term commercial bank debts was signed. It includes both a debt buyback and a debt conversion option (the latter including three types of bonds, one involving new money). In May the

buyback was completed with commercial banks tendering US$1.2 billion for a buyback at a price of 52 cents per dollar of debt. The cost of some US$650 million was financed from reserves. On December 1, 1992 US$3.2 billion of debt was tendered for converted into bonds. Total debt outstanding is projected to fall to 56 per cent of GNP in 1992, while debt service obligations are expected to be equivalent to approximately 18 per cent of total exports of goods and services.

Graph 4 - Philippines - External debt as percentage of GNP and debt service ratio, 1986-92



Note: 1992 figure is a projection.
Source: IMF.

28. The price of Philippine debt obligations increased somewhat subsequent to the buyback, but not significantly. As of December 1992 Philippine commercial debt continued to trade at a substantial discount of 44 per cent on secondary markets. Although debt servicing burdens have declined, external debt remains a heavy burden on the economy. At the end of 1991 the stock of external debt was about US$30 billion, a figure that is not expected to decline much in 1992. As is the case with other highly indebted countries, debt relief has resulted in a substantial change in the creditor composition of outstanding external debt. The share of official creditors has increased, whereas the share of private creditors (commercial banks) has declined. In 1986, about 60 per cent of the stock of external debt of the Philippines was held by private creditors; in 1990 this share had dropped to 40 per cent.

Trade

29. In the last two decades, the pattern of trade in the Philippines changed considerably as non-traditional exports such as garments and electronic components became more important than traditional exports such as coconut products, sugar and copper. Since the mid-1980s the share of agricultural exports such as sugar, coconut products and fruit and vegetables has fallen from 25 per cent to 17 per cent. Exports of manufactures have increased substantially, from 55 per cent in 1985 to 72 per cent in 1991. Electronic equipment and textiles and clothing currently account for about 26 per cent and 22 per cent of total exports, respectively (Table 3). Overall, exports have been growing slowly steadily since 1985, almost doubling in nominal terms.

Table 3
Exports by major commodities, 1985-91
(US million dollars and percent of total exports

	1985		1988		1991	
	US$ m.	%	US$ m.	%	US$ m.	%
Total exports	4,629	100.0	7,074	100.0	8,840	100.0
Agriculture	1,178	25.4	1,442	20.4	1,480	16.7
Coconut products	466	10.1	582	8.2	447	5.1
Sugar products	185	4.0	74	1.0	136	1.5
Fruit and vegetables	256	5.5	306	4.3	393	4.4
Others	271	5.8	480	6.8	504	5.7
Natural resources	860	18.6	1,187	16.8	858	9.7
Forest products	199	4.3	261	3.7	73	0.8
Mineral products	570	12.3	764	10.8	610	6.9
Petroleum products	91	2.0	162	2.3	175	2.0
Manufactures	2,539	54.8	4,338	61.3	6,403	72.4
Electronics	1,056	22.8	1,476	20.9	2,293	25.9
Textiles	662	14.3	1,388	19.6	1,961	22.2
Chemicals	150	3.2	256	3.6	304	3.4
Processed food and beverages	106	2.3	184	2.6	233	2.6
Footwear and travel goods	59	1.3	99	1.4	186	2.1
Machinery and transport equipment	30	0.6	54	0.8	181	2.0
Furniture and fixtures	84	1.8	184	2.6	177	2.0
Wood manufactures	43	0.9	79	1.1	117	1.3
Non-metallic minerals	24	0.5	33	0.5	74	0.8
Others	325	7.0	585	8.3	877	9.9
Special transactions	12	0.3	27	0.4	17	0.2
Re-exports	40	0.9	80	1.1	82	0.9

Source: Central Bank of the Philippines

30. As noted earlier, imports have grown substantially since the mid-1980s, more than doubling since 1985. As a result the merchandise trade deficit has increased steadily. Imports of raw materials intermediate goods account for about half of total imports of the Philippines, followed by capital goods and mineral fuels and lubricants (Table 4). The relative importance of mineral fuels and lubricants in total imports varies substantially from year to year, reflecting changes in world oil prices. The composition of non-oil imports has changed substantially during the 1985-91 period. Capital goods have steadily risen in importance, from 21 to 29 per cent of total non-oil imports. In contrast, the share of imports of both intermediate inputs and final consumer goods declined in recent years. Intermediate and consumer goods accounted for 63 and 18 per cent of non-oil imports in 1988. In 1991, their shares had fallen to 57 and 10 per cent, respectively.

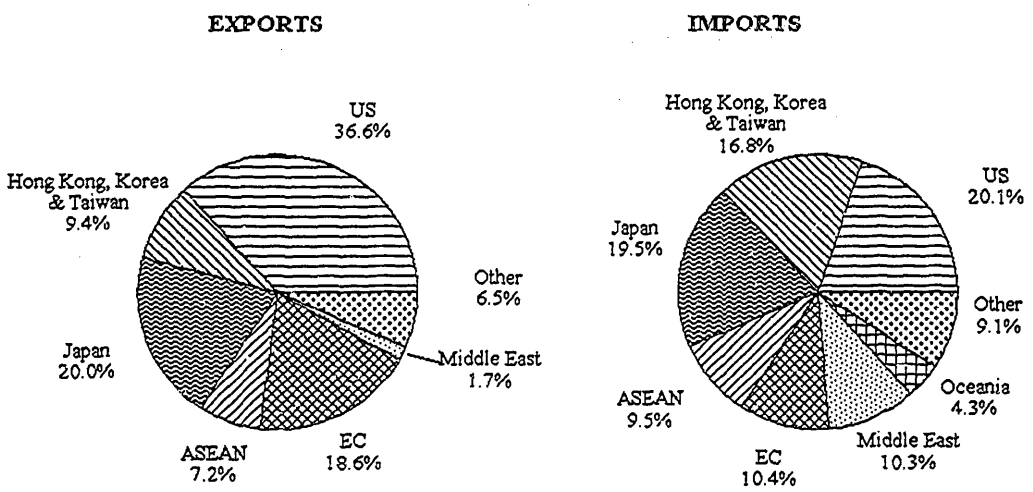
Table 4
Imports by Major Commodities, 1985-91
(US million dollars and percentage of total imports)

	1985		1988		1991	
	US$ m.	%	US$ m.	%	US$ m.	%
Total imports	5,111		8,159		12,051	
Capital goods	769	15.0	1,637	20.1	2,952	24.5
Elec. and non-elec. machinery	626	12.2	1,279	15.7	2,384	19.8
Power generators	337	6.6	639	7.8	1,047	8.7
Office and EDP machines	29	0.6	69	0.8	151	1.2
Telecom equipment elec. machinery	289	5.6	571	7.0	1,186	9.8
Land transport equipment excl. passenger cars	34	0.7	144	1.8	186	1.5
Aircraft, ships and boats	20	0.4	123	1.5	238	2.0
Professional scientific instruments	60	1.2	91	1.1	144	1.2
Raw materials and int. goods	2,338	45.7	4,415	54.1	5,851	48.5
Wheat	106	2.1	136	1.7	172	1.4
Crude mats., inedible	150	2.9	413	5.1	597	5.0
Chemicals	584	11.4	1,039	12.7	1,328	11.0
Manufactures	508	9.9	1,238	15.2	1,714	14.2
Embroideries	196	3.8	377	4.6	514	4.3
Material for manufacture of electrical equipment	585	11.4	910	11.2	1,208	10.0
Other	209	4.1	302	3.7	318	2.6
Mineral fuels and lubricants	1,452	28.4	1,096	13.4	1,784	14.8
Consumer goods	320	6.3	597	7.3	990	8.2
Food and live animals	239	4.7	379	4.6	460	3.8
Other	81	1.6	218	2.7	530	4.4
Special transactions	232	4.5	414	5.1	474	3.9

Source: Central Bank of the Philippines

31. The United States and Japan are the major markets for Philippine exports, accounting for 35.6 per cent and 19.9 per cent of the total value of exports in 1991, with the EC a close third (Graph 5). Trade with ASEAN countries has grown, their share of Philippine exports attaining over 7 per cent in 1991. The United States and Japan are also the Philippines' major sources of imports, accounting for 20.1 per cent and 19.5 pe cent, respectively, of the total f.o.b. value of imports into the Philippines in 1991 (Graph 5). Taiwan, South Korea and Hong Kong are all important suppliers, representing 6.9, 5.1 and 5.0 per cent, of total imports, respectively. the EC and the Middle East accounted for 10.3 per cent each of the total value of imports, while ASEAN countries supplied for 6.6 per cent of imports.

Graph 5 - Philippines - Geographic patterns of merchandise exports and imports, 1991



Source: IMF.

(iii) Macroeconomic developments

32. The Philippine Government has tended to run chronic fiscal deficits. Up to 1983 shortfalls were financed in large part by foreign savings (external borrowing). After the 1983 financial crisis, public sector deficits were financed through issuing public domestic debt instruments - largely Treasury bills - as the Central Bank refused to monetize (print money to finance) the deficits. Domestic public debt outstanding grew rapidly as a result, at an average annual growth rate of 17 per cent during 1984-1990. One result was an increase in interest rates and crowding out of the private sector. Between 1985 and 1989 public debt rose from 19 to 25 per cent of GDP, real ex-post interest rates on Treasury bills increasing from 3 to over 10 per cent on average. The stock of domestic public debt also rose due to Central Bank open market operations, under which the Bank sold its own securities to the public so as to reduce domestic liquidity. These operations have been very costly for the Central Bank, as these securities carry an interest cost of around 20 per cent.

33. The national government budget deficit was 3.4 per cent of GNP in 1990, the consolidated public sector deficit attaining 5.5 per cent of GNP in that year (Table 5). The two percentage point difference between the national government and the consolidated deficit was largely the result of the

operations of the Oil Price Stabilization Fund (OPSF) and the Central Bank. The OPSF effectively subsidized domestic consumption of oil by not passing through completely increases in world prices for oil and the effect of the depreciation of the peso. The Central Bank incurred significant losses associated with foreign exchange liabilities (see below). In 1991 the national government and the consolidated deficits were reduced to 2.1 and 2.3 per cent of GNP, respectively. The substantial decline in these deficits was due to a number of factors. The national government budget deficit declined because revenues rose faster than expenditures, despite unplanned spending related to national disasters such as the Mount Pinatubo eruption. The OPSF registered a large surplus as the result of a fall in world oil prices. This decline in world oil prices was not passed through fully to domestic consumers, the resulting revenue being used instead to reduce the public sector deficit.

Table 5
Consolidated public sector deficit 1987-92

	1987	1988	1989	1990	1991	1992[1]
			Billions of pesos			
National Government deficit	-20.1	-23.2	-19.6	-37.1	-26.3	-9.0
Monitored corporations deficit	-3.2	2.1	-4.4	-19.1	-8.7	-17.7
Oil price stabilization fund deficit	...	...	-9.0	-7.4	12.3	3.5
Adjustment for intra-PSBR transfers[2]	8.4	3.9	2.8	12.9	6.9	1.3
Monitored public sector borrowing requirement (PSBR)	-14.9	-17.2	-30.2	-50.7	-15.8	-21.9
Surplus of government financial institution (GPIs)[3]	1.3	2.1	3.3	1.8	1.1	3.2
Net imcome of Central Bank[4]	-10.9	-16.9	-20.8	-21.9	-22.7	-17.7
Other[5]	5.6	5.6	4.2	11.6	8.1	9.5
Adjustments for other transfers within the public sector[6]	0.3	...	2.5	0.1	-	0.1
Consolidated public sector deficit	-18.6	-25.0	-41.0	-59.1	-29.2	-26.8
			Percent of GNP			
National government deficit	-2.9	-2.8	-2.1	-3.4	-2.1	-0.6
Monitored corporation deficit	-0.5	0.3	-0.5	-1.8	-0.7	-1.3
PSBR	-2.1	-2.1	-2.2	-4.7	-1.3	-1.6
Consolidated public sector deficit	-2.6	-3.0	-4.5	-5.5	-2.3	-1.9

1 Projections.
2 Includes adjustments for net lending for debt buybacks, National Government (NG) net lending and equity to monitored corporations, NG transfers to the OPSF, and OPSF settlement of arrears included in Philippines National Oil Company (PNOC) cash generation.
3 Philippine National Bank (PNB), Development Bank of the Philippines (DBP), the Philippine Export and Foreign Loan Guarantee Corporation (Philguarantee), and the Land Bank.
4 Net of the impact of debt reduction, estimated at P1.9 billion in 1990, P2.1 billion in 1991, and P2.3 billion in 1992.
5 Includes the Local Government Units (LGUs) and the social security institutions.
6 Includes NG net lending and equity to GFIs.
Source: IMF.

34. In the first six months of 1992 the consolidated public sector registered a small surplus. Projections for 1992 indicate the consolidated public sector deficit will be about 1.9 per cent of GNP. The national government deficit is expected to be reduced to 0.6 per cent of GNP in 1992, reflecting sharp cuts in spending. However, the marked decline in the national government deficits is offset by a projected increase in the deficits of monitored public corporations.[13] The National Power Corporation in particular has been confronted with a rise in operating costs as a result of the drought. This has not been offset by greater revenues.

35. It can be seen from Table 5 that the losses incurred by the Central Bank in 1991 were almost as large as the national government's budget deficit, and are expected to exceed the government deficit by more than 50 per cent in 1992. The reasons for the losses incurred by the Central Bank include the following. The Central Bank has been obliged to buy foreign exchange in order to service foreign debt obligations incurred by certain public and private enterprises during the 1980s. These liabilities were made the responsibility of the Bank in 1986 under a debt restructuring programme. The Bank also assumed the external payments liabilities of domestic borrowers, as amended by the 1986 restructuring agreement. In addition to these obligations, the Bank incurred significant losses on swap and forward cover transactions. The Bank concluded a number of swap transactions with commercial banks in the mid-1980s, under which a peso loan was exchange for a foreign currency loan. In periods when the peso depreciated, the foreign exchange cost of - the loss associated with - servicing the liabilities resulting from such swaps increased.[14] The Bank also has a portfolio of non-performing loans to domestic financial institutions and has incurred losses on its open market operations. Notwithstanding the peso appreciation and the decline in interest rates during 1992 - which resulted in lower losses than forecast - the large losses of the Central Bank imply that the effective national government deficit remains around 2 per cent of GNP. It is likely that the national government will have to take responsibility for the liabilities imposed on the Central Bank during the 1980s. Until this is done the Bank will be severely hampered in pursuing monetary policy.

36. The government has made efforts both to raise revenues and to reduce expenditures. Attempts to increase revenue have involved both enhancement of tax collection efforts (including policies to reduce tax evasion) and broadening the tax base. Total revenues have been rising gradually to reach 17.5 per cent of GNP in 1991, and are composed largely of tax revenues. Import duties are the largest component of government tax revenue, accounting for 29 per cent of total revenues in 1991. The importance of tariff revenues in total revenues has declined in recent years partly as a result of the tariff reform programme undertaken during the 1980s, and a duty exemption scheme.[15] An ongoing privatization programme has recently become a source of additional revenue.

37. Current operating expenditure in 1991 accounted for 79 per cent of total government expenditure, down from 83 per cent in 1989. Interest payments were the largest expenditure item (30.2 per cent of the total) in 1991, closely followed by wages. Capital expenditure has risen steadily, from 11.7 per cent of total expenditure in 1986, to 13.1 per cent in 1989 and 17 per cent in 1991. Capital expenditure by the government as a proportion of GNP has also increased in recent years, moving from a low of 2 per cent in 1988 to 3.3 per cent in 1991. Projections for 1992 suggest that capital expenditure will fall this year to 2.3 per cent on GNP. Indeed, the forecast decline in the

[13]There are 14 such corporations. They include entities such as the Metropolitan Water and Sewage System, the National Power Corporation, the Philippine National Oil Corporation, the National Irrigation Administration and the National Food Authority.

[14]Outstanding swaps of about US$965 million were eliminated in july 1992 and some US$600 million of external debt was extinguished in May 1992.

[15]See GATT document C/RM/S/33, Chapter IV.

national government deficit for 1992 (see above) is largely driven by a reduction in capital expenditure and net lending to public corporations and government financial institutions.

38. Consumer prices increased by 12 per cent on average during 1988-90. Inflation accelerated to about 19 per cent for 1991 as a whole. These price increases were due to a mix of expansionary monetary policy and cost-push pressures - e.g., increases in food prices subsequent to natural catastrophes during this period, a rise in the prices of public transport and utilities implemented as part of the structural adjustment programme, and the implementation of the 1989 Minimum Wage Act. Between the second half of 1991 and the summer of 1992, inflation declined sharply, standing at 9 per cent (annual rate) at the end of June 1992 despite the persistent large foreign exchange inflows. In the period between June and November 1992 inflation remained at this level. The decline reflects the economic slowdown during 1991, complemented by the stricter control of the money supply. The appreciation of the peso in 1991 and early 1992 also helped to reduce inflation.