Commentary

What price greed?

When you are riding a roller coaster it is rather difficult to find a reference point. So it is in times of economic and financial volatility. The severity of events of the past week have caught everyone by surprise. The collapse of Lehman Brothers has had a catalytic effect on other investment houses: Both Merrill Lynch and Bear Stearns have been sold off and over the past few days the U.S. Federal Reserve has announced that other icons of Wall Street, Morgan Stanley and the Goldman Sachs Group, will be converted into traditional bank holding companies. Now has come the announcement by Washington of a US$700 billion bailout package—more than US$2,300 for each man, woman and child in the USA—to buy up what has been quaintly termed "toxic assets" that threaten to poison the entire U.S. financial—and by implication, global— system. The veracity of that package is being questioned in Congress but at the end of the day is there any choice?

Over the past week, political pronouncements, newspaper headlines as well as financial and stock markets have given a whole new meaning to the term "volatility." And while it is true as BSP Governor Armando Tetango said earlier this week, that the exposure of the Philippines to the present crisis is limited, that does not mean that the economy will not be affected in a fundamental way. Life will never be the same again; at least not for a while.

For a start, the global lending market has all but dried up for the time being. Yes, problems in the United States and elsewhere (Europe and Russia are also seen to be likely to suffer a fallout) may make emerging markets more attractive for cash-rich companies and funds (and there are still some around) but whether the Philippines will benefit is another matter. In many ways the past eight years has been a squandered opportunity for this country to put itself in order and become a truly competitive world—or at least, regional—player.

So let's ignore the hype of political pronouncements and the optimism of the local press and try and find ourselves an anchor point. And the best such anchor point to be found is not to look outwards or upwards but back at the ground. What can we say about the fundamentals of the Philippines?

We are not denying any progress at all under the incumbent administration. But the pickings are lean. Beyond the expanded VAT what new initiatives have *really* been brought about? What has been achieved that would not have been done anyway? More importantly, what real initiatives have been taken to improve the investment climate so as to bring in foreign direct investment (FDI) that would, in turn, bring about the sea-change this country needs.

Over the eight years of the Arroyo Administration, poverty has become more acute. According to the NSCB between 2000 and 2006, the poverty threshold went from a annual PHP 11,458 to PHP15,047. in 2006 a family of five needed an income of PHP6,274 to stay above the poverty threshold. This represented an increase of 31.41 percent over the six years period. During the same period, consumer price inflation increased by 35 percent. You can do the math for yourself.

Now these are the official figures; most people would regard an annual cash income of PHP 11,000 (around $250) to be extreme poverty, not the baseline. Unsurprisingly, self-rated poverty is much higher. According to a recent United Nations country team report "*social and economic development in the Philippines remains uneven and poverty continues to be characterized by widespread disparities across regions and population groups*."

According to the July 2008 update from local pollster Social Weather Stations. Self-rated poverty had climbed by nine points between the first and second quarter of this year. In July, fifty-nine percent of Filipino families, or about 10.6 million, rated themselves as "Poor;" a further 24 percent put themselves on the "Borderline;" and only 17 percent rated themselves as "Not Poor." More alarmingly the latest survey confirms continuance of a trend that has been evident for some time: people are lowering their expectations; food substitution from high nutrition diets to less nutritious ones continues to afflict poor and even middle income families.

The next triennial *Family Income and Expenditure Survey* is not due until next year but based on an analysis of the figures from 1994 to 2006, UP Economist Ernesto Pernia believes that remittances have primarily benefitted the upper income groups, doing little for the poorest of the poor. Nonetheless he concludes that without remittance income, there would be 26.5 million more people in this country classified as poor than there are now. This is a number worth bearing in mind when we consider the dampening effect on future overseas job opportunities and remittance income from those that are part of the OFW class, should current problems in the global economy lead to a sudden reversal in this income source.

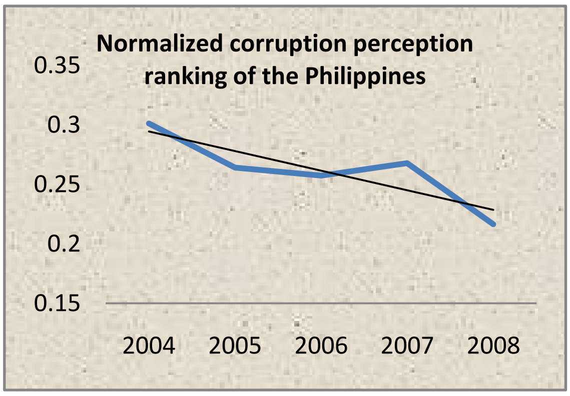
Meanwhile instead of meaningful action to redress the situation, Congress wrings its hands over whether condoms are a form of abortion.

Poverty of course is directly related to employment as well as, more generally, to economic growth. Sadly, in the case of the Philippines, "the rising tide does not lift all boats." The Philippines may have been experiencing a prolonged spell of high growth (which has now come to an abrupt end) but it has also been a period characterized as "jobless growth" whereby there has been a continued employment drift from formal sector jobs—those covered by the Labor Code of the Philippines (acknowledged to be among the most advanced within Asia) and where employees receive regular salaries or wages for their labour—to informal sector work where safety nets are minimal or nonexistent.

Recent studies have estimated that such informal sector employment may now embrace up to 70 percent of the workforce. And while unemployment hovers at around the eight percent mark officially; the official statistics hide the true situation in two ways: Firstly, the very definition of unemployment was re-engineered in 2006 so as to include only those who are in paid employment (and even one hour a week counts) or those who are actively seeking work; secondly, when you add in the figures for "underemployment"—those seeking additional hours of work the combined figure is closer to 30 percent (underemployment hovers around 22 percent). And this staggering number would be much worse were it not for the ability (up until now) of many to seek work overseas.

The dearth of quality jobs of course relates directly to the investment climate. Here again the Philippines brings up the rear within Southeast Asia when it comes to FDI. We read of regular press announcements about this or that investor setting up here and bringing with them new jobs: but at the end of the day, outside of the BPO industry, where are they? Some of these jobs may indeed be created but do they do any more than replace jobs that have been lost?

Employment growth in the Philippines, around two percent annually, is scarcely keeping pace with population growth. And this is not quality employment being created but an increase in domestic helpers, drivers and self-employed ambulant vendors.



The failure of investment is in turn linked to corruption. Here there is more bad news. Based on the most recent annual Corruption Perceptions Index of Transparency International, the Philippines ranked 131st out of the 180 nations surveyed this year and was placed alongside Burundi, Honduras, Iran, Libya, Nepal and the Yemen. When it comes to petty bribery, the Philippines is up there among the world's "top 10." To provide a proper comparative basis the chart shows a "normalized" index based on the number of countries surveyed in each year. The ineluctable conclusion is that the Philippines has steadily drifted downwards (perceived to be more corrupt) in recent years and with the sharpest "fall" between 2007 and 2008.

The perceptive decline of the Philippines

	2004	2005	2006	2007	2008
Rank	102	117	121	131	141
Total countries	146	159	163	179	180
Normalized ranking (1)	0.69863	0.735849	0.742331	0.731844	0.783333
Normalized ranking (2)	0.30137	0.264151	0.257669	0.268156	0.216667

Source: Transparency International

What does all this mean in the present climate of uncertainty? For a start, we can dismiss any political statements that smack of complacency. This is pure spin and fools nobody. Any claim that "we are doing the best we can" has a rather hollow ring if we consider this over any respectable time period. Clearly the Government of the Philippines (and in this we include Congress) has squandered one opportunity after another to put this country onto a higher growth track. Neither has the private sector nor members of the privileged class of the country risen to the challenge in terms either of making local business more competitive through an effective embrace of globalization (that would make the Philippines more competitive in the global supply chain) or through improving corporate governance and rule of law. Of course the two are interrelated.

Whether it is a tourist development in Bohol funded by an enterprising expatriate or an international retail warehousing company wishing to enter the local market and bringing with it real competition, so often local business partners end up stealing the company from their foreign partners. This does not go unnoticed. What message does it send? Indeed why would anyone invest here when the law continues to be flouted by those who feel they can get away with it?

Even without the present uncertainty it was already bad enough (and getting worse) but now another dimension has been added to the mix—the drying up of risk capital. The Philippines has been living on borrowed time and may now be called to account. In the responsible mining industry for example, which is supposed to be one of the cornerstones of government policy to revive investment and provide a catalyst for sustained rural growth, strong words have been coupled with failure to act. To cite but one example: In the case of the Didipio Copper and Gold project in Nueva Vizcaya, clearly there appears little will by the national government to act against a local governor who is determined to extort a heavy price in terms of her rent-seeking behaviour in order to permit the project to proceed. Investors are already fed up.

And with an upsurge of instability in Mindanao, where many of the best minerals projects are to be found, can we expect this industry to prosper in the manner that it should?

In recent years, an unprecedented period of worldwide growth has led to an equally unprecedented commodity boom. But that is now fading and once again the Philippines will likely have missed the boat. Those companies that have strong capital reserve positions and who can self-fund their investments may weather the harsher environment. Those looking for equity or loan funds to finance their operations will find the going that much tougher. Consumer spending is already slowing with brand and product substitution evident in the market. If remittances collapse with the downturn of the global economy, then the ride could be bumpy indeed. The mood of the country is already sombre and could get much worse.

There are reports that in the new global financial order, the salaries and bonuses of top executives may plummet by 70 percent or more. Sadly we believe it unlikely that the elite of the Philippines will follow suit. Many in this country (but not all we hasten to add) continue to be fuelled by greed, and greed is likely to continue to win out. For foreign investors, an amber light is flashing.

Corporate communications specialists

P.O. Box 2737 Makati City, Metro Manila, Philippines
Tel/Fax: (63 2) 889 6054: E-mail: michael.clancy@mayamaya.com
Document Name: 080924 Commentary
Document Printed: Friday, September 26, 2008