

Afterthoughts

# Philippines: Why Fighting Corruption is not Enough

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After nine years of witnessing increasing poverty among the masses and spiraling corruption in high places, it is understandable that Filipinos see a strong correlation between corruption and poverty. And the judgment of many is probably correct that the candidates that are free of the taint of corruption stand the best chance of turning this country around. Moral leadership may not be a sufficient condition for successful leadership but it certainly has become a necessary condition in a country that has been so deprived of exemplary public figures like the Philippines.

Corruption, however, has become the explanation for all our ills, and this brings with it the danger that, after the elections, campaign rhetoric might substitute for hard analysis on the causes of poverty, leading to wrong, ineffectual prescriptions for dealing with the country's number one problem.

Let me be more explicit: Corruption must be condemned and corrupt officials must be prosecuted because being a violation of public trust, corruption undermines faith in government and leads to an erosion of the moral bonds among citizens that serve as the foundation of good governance. Corruption, however, is unlikely to be the main cause of poverty. Wrongheaded policies are, and clean-cut technocrats have been responsible for more poverty than corrupt politicians.

The complex of policies that have pushed the Philippines into the economic quagmire over the last 30 years might be summed up in that formidable term: structural adjustment. Also known as neoliberal restructuring, it involved prioritization of debt repayment; conservative macroeconomic management that involving huge cutbacks in government spending; trade and financial liberalization; privatization and deregulation; and export-oriented production. Structural adjustment came to the Philippines courtesy of the World Bank, International Monetary Fund, and the World Trade Organization, but it was internalized and disseminated as doctrine by local technocrats and economists as doctrine.

## **Prioritizing Debt Repayment**

Corazon Aquino was personally honest and her contribution to the reestablishment of democracy was indispensable, but her submitting to the International Monetary Fund's demand to prioritize debt repayment over development brought about a decade of stagnation and continuing poverty. Interest payments as a percentage of total government expenditures went from 7 percent in 1980 to 28 percent in 1994. Capital expenditures, on the other hand, plunged from 26 percent to 16 percent. Since government is the biggest investor in the Philippines—indeed in any economy—the radical stripping away of capital expenditures goes a long way toward explaining the stagnant one percent average yearly growth in gross domestic product in the 1980's and the 2.3 per cent rate in the first half of the 1990's.

In contrast, our Southeast Asian neighbors ignored the IMF's prescriptions. They limited debt

servicing while ramping up government capital expenditures in support of growth. Not surprisingly, they grew by 6 to 10 percent from 1985 to 1995, attracting massive Japanese investment while the Philippines barely grew and gained the reputation of a depressed market that repelled investors.

## **Trade and Financial Liberalization**

When Fidel Ramos came to power in 1992, the main agenda of his technocrats was to bring down all tariffs to 0 to 5 percent and bring the Philippines into the World Trade Organization and the ASEAN Free Trade Area (AFTA), moves that were intended to make trade liberalization irreversible. A pick-up in the growth rate in the early years of Ramos sparked hope, but the green shoots were more apparent than real, and they were, at any rate, crushed as a result of another neoliberal policy: financial liberalization. The elimination of foreign exchange controls and restrictions of speculative investment attracted billions of dollars in the period 1993-1997. But this also meant that when panic hit the ranks of foreign investors in Asia in the summer of 1997, the same lack of capital controls facilitated the stampede of billions of dollars from the country in a few short weeks in mid-1997. This pushed the economy into recession and stagnation in the next few years.

The Estrada administration did not reverse course, and under the presidency of President Gloria Macapagal-Arroyo, neoliberal policies continued to reign. New liberalization initiatives in the next few years were initiated on the trade front, with the government negotiating free trade agreements with Japan and China. These pacts were entered into despite clear evidence that trade liberalization was destroying the two pillars of the economy, industry and agriculture.

Radical unilateral trade liberalization severely destabilized our manufacturing sector, with textile and garments firms, for instance, being drastically reduced from 200 in 1970 to 10 in recent years. As one of Arroyo's finance secretaries admitted, "there's an uneven implementation of trade liberalization, which was to our disadvantage." While he speculated that consumers might have benefited from the tariff liberalization, he acknowledged that "it has killed so many local industries."

As for agriculture, the liberalization of our agricultural trade after we joined the World Trade Organization in 1995 transformed the Philippines from a net food exporting country and consolidated it into a net food importing country after the mid-1990's. The year 2010 is the year that the China ASEAN Trade Agreement (CAFTA) negotiated by the Arroyo administration goes into effect, and the prospect of cheap Chinese produce flooding our markets has made our vegetable farmers fatalistic about their survival.

## **Depressive Fiscal Policy**

What likewise became clear during the long Arroyo reign were the stifling effects of the debt repayment-oriented macroeconomic management policy that came with structural adjustment. With 20-25 percent of the national budget reserved for debt service payments owing to the draconian Automatic Appropriations Law, government finances were in a state of permanent and widening deficit, which the administration tried to solve by contracting more loans. Indeed, the Arroyo administration contracted more loans than the previous three administrations combined.

When the deficit reached gargantuan proportions, the government refused to take the necessary steps to contain the key factor acting as the main drain on expenditures; that is, it refused to declare a debt moratorium or at least renegotiate the terms of debt repayment to make them less punitive. At the same time, the administration did not have the political will to force the rich to take the brunt of bridging the deficit by increasing taxes on their income and improving their collection. Under pressure from the IMF, the government levied this burden on the poor and the middle class via the adoption of the expanded value added tax (EVAT) of 12 percent on purchases. The tax was passed on

to poor and middle class consumers by commercial establishments, forcing them to cut back on consumption, which then boomeranged back on small merchants and entrepreneurs in the form of reduced profits, forcing many out of business.

### **Facing the Policy Challenge**

The straitjacket of conservative macroeconomic management, trade and financial liberalization, and a subservient debt policy kept the economy from expanding significantly, resulting in the percentage of the population living in poverty, according to the World Bank, increasing from 30 to 33 percent between 2003 and 2006. By 2006, there were more poor people in the Philippines than at any other time in the country's history.

The country's plight under the lash of wrong policies over the last four administrations becomes even clearer in a comparative perspective. According to the United Nations Development Program Human Development Report, the Philippines registered the second lowest average yearly growth rate, 1.6 percent, in Southeast Asia in the period 1990 to 2005 —lower than that of Vietnam (5.9 percent), Cambodia (5.5 percent), and Burma (6.6 percent). The only country registering average growth below that of the Philippines was Brunei, which, being an oil-rich high-income country, could afford not to grow.

So yes, we must wage an unrelenting campaign against corruption because it destroys faith in government and weakens the moral fiber of the country. And yes, let us by all means punish corrupt officials and elect morally unquestionable people to power. But let us not mistake corruption as the principal cause of poverty and believe that anti-corruption crusades provide the main response to the country's economic ills. The main source of our lack of economic dynamics is a wrong policy paradigm that we have allowed ourselves to be straitjacketed into.

It is disturbing that the policy errors that have led to our present state are hardly mentioned in the presidential debates. It is unfortunate that we are not taking advantage of the current international economic crisis that has dragged down our local economy to debate the wisdom of the policies of globalization and liberalization that have brought us to this impasse. Yes, the issues of corruption, management experience, and bureaucratic reform that dominate these debates are vital, but unless the winning team has the courage to reverse 30 years of failed neoliberal economic policies, the country will remain in the economic doldrums, unable to take off, with poverty possibly rising to the point of no return.

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