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Chapter 1

An Overview of the Philippine Economy and Its Foreign Trade Regimes

The main purpose of this study is to examine the effects on growth, resource allocation, and income distribution of the various exchange controls and commercial policies utilized by the Philippine government from the end of World War II through 1971. Special attention is devoted to assessing the efforts to liberalize exchange controls. Since trade and payments policies are only one means (although a very important one) employed by governments in pursuit of their goals of growth, resource allocation, and income distribution, it is also necessary to consider the role of other major policy tools in that pursuit. In particular, the fiscal and monetary measures that accompanied shifts in trade and payments policies will be examined in order to place the latter in their proper perspective.

To provide a general perspective for the subsequent detailed description and analysis of the exchange controls and related measures employed between 1946 and 1971, a brief overview is presented in this chapter first, of the nature of the Philippine economy, and second, of the various exchange-control phases through which the economy has moved during those years.

THE STRUCTURE OF THE PHILIPPINE ECONOMY

A unique geographical feature of the Philippines is that the country consists of some seven thousand islands stretching over an area of more than a thousand miles from north to south and about seven hundred miles from east to west. However, the combined land area of the islands is only 115,000 square miles. The country's population in 1971 was 37 million. This is roughly comparable to that of such other countries in Southeast Asia and the Far East as Thailand (34 million), Burma (28 million), and South Korea (32 million). The population density of the Philippines is, however, greater than that of any other Southeast Asian country except Singapore.[1] Like several countries in this region, the rate of population growth in the Philippines has averaged about 3 per cent annually since 1950.

The per capita gross domestic product of $179 in 1970 places the Philippines among the lower half of all developing countries in the world, but among the highest of the developing countries in South Asia, Southeast Asia, and the Far East.[2] For example, 1970 per capita gross domestic product (GDP) in Thailand was $174; in Indonesia, $70; in India, $91; in South Korea, $257; and in Taiwan, $414.[3] The country's average annual growth of real GDP of 5.9 per cent from 1961 to 1970 was somewhat higher than the average for all developing countries during this decade, but within Southeast Asia and the Far East such countries as Thailand, Malaysia, Singapore, South Korea, and Taiwan grew at a faster pace.

The growth pattern of Philippine gross domestic product and of net domestic product and its components during various subperiods between 1946 and 1971 is indicated by the data in Table 1-1. As is shown in this table and in Chart 1-1, the average annual growth rate of gross national product was very rapid during the reconstruction period in the latter part of the 1940s, and also was quite high during the early period of import-substitution policies in the first half of the 1950s. A slowdown to a 5 per cent annual growth rate occurred in the last part of the decade, but this was reversed in the 1960s as the average rate rose to 5.6 per cent and 6.0 per cent annually in the next two periods. Manufacturing activity also expanded very quickly during the reconstruction period, and this growth continued at an annual rate of more than 12 per cent from 1951 to 1955. The pace of development in this sector not only then declined to 7.7 per cent annually in the 1956–60 period, but the fall continued, reaching an average annual growth rate of 4.0 per cent in the next five-year period. However, the rate rose from 1966 to 1971 to 5.9 per cent.

The rapid rate of growth in manufacturing resulted in an increase in the share of this sector in net domestic product from 10.7 per cent in 1948 to 17.9 per cent by 1960. Between 1960 and 1971, however, the relative share failed to increase further and stood at 17.6 per cent in 1971.

As is indicated by the data in Table 1-2, one result of the increase in the relative importance of the manufacturing sector has been a sharp decline between the end of the 1940s and the early 1970s in the share of imports consisting of simple manufactures and foodstuffs. On the other hand, the import share of such items as machinery and transportation equipment as well as

TABLE 1-1

Average Annual Net Domestic Product by Industry, Average Annual Gross National Product, and Population, 1946–71

	1946–50	1951–55	1956–60	1961–65	1966–71
Agriculture, fishery, and forestry					
Value[a]	1,619	2,407	2,981	3,574	4,774
Growth rate[b]	12.4	7.2	3.0	4.2	5.7
Mining and quarrying					
Value[a]	41	100	148	176	365
Growth rate[b]	70.3	12.0	8.4	4.5	19.9
Manufacturing					
Value[a]	440	1,000	1,609	2,058	2,672
Growth rate[b]	50.5	12.1	7.7	4.0	5.9
Construction					
Value[a]	323	346	370	422	489
Growth rate[b]	38.1	−2.7	0.3	8.0	−1.9
All other					
Value[a]	1,760	2,924	4,146	5,407	7,138
Growth rate[b]	16.9	9.1	5.9	5.5	5.2
Net domestic product					
Value[a]	4,194	6,776	9,255	11,637	15,399
Growth rate[b]	18.9	8.1	5.0	5.0	5.4
Gross national product					
Value[a]	4,700	7,619	10,420	13,398	18,207
Growth rate[b]	19.9	8.1	5.0	5.6	6.0
Population					
Thousands	19,044	21,886	25,435	29,526	34,941
Growth rate[b]	2.3	3.1	3.1	3.0	3.0
Per capita GNP					
Value[a]	246	347	409	453	522
Growth rate[b]	17.1	4.9	1.9	2.1	2.9

SOURCE:

Income data: 1948–67—National Economic Council, *Statistical Reporter*, January–March 1969, pp. 12–13 and 19; 1968–70—National Economic Council, *Statistical Reporter*, April–June 1971; 1971—National Economic Council.

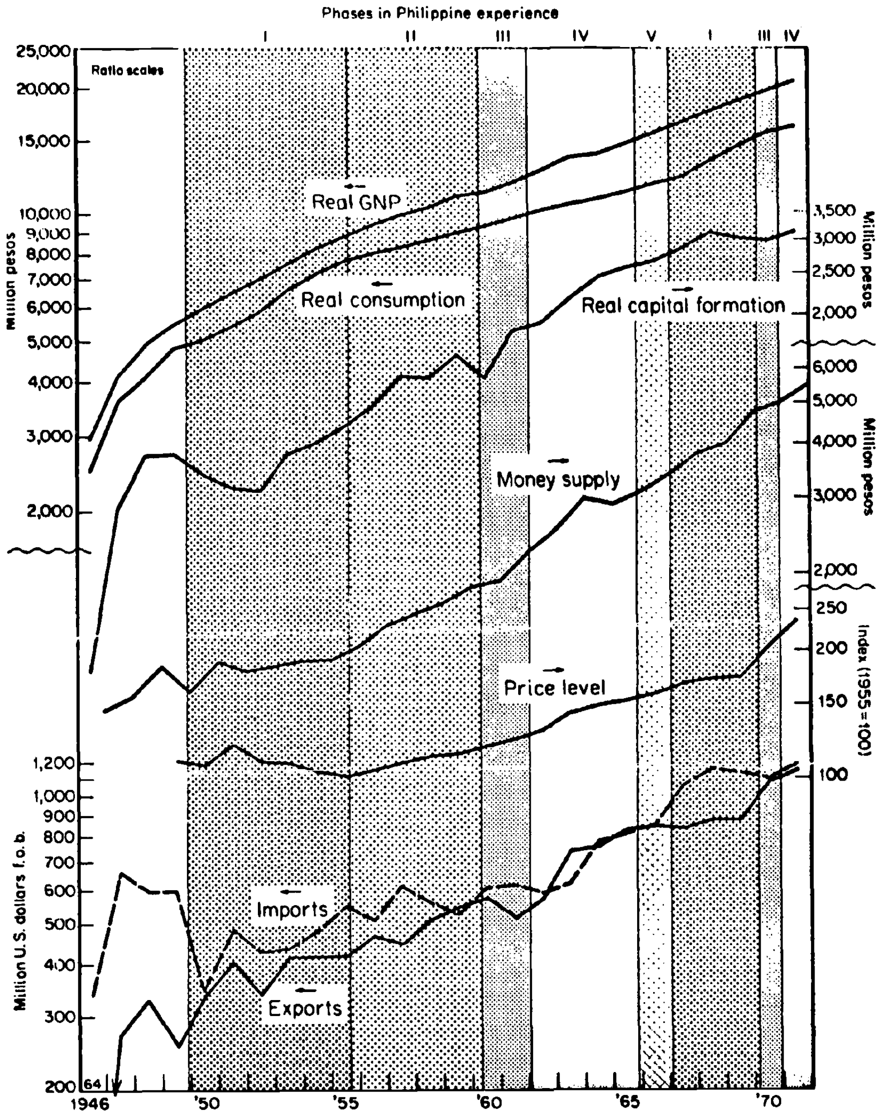
Population: 1946–59—Bureau of Census and Statistics, *Handbook of Philippine Statistics*, 1960 and 1963; 1960–71—Bureau of Census and Statistics.

a. Average annual level in millions of pesos at 1955 prices.

b. Average annual percentage rate of growth.

CHART 1-1

Macroeconomic Indicators and Phases, the Philippines, 1946–71



SOURCE: Real GNP, real consumption, and real capital formation for 1946–70 from National Economic Council, *The Statistical Reporter*, January–March 1969 and April–June 1971; 1971 from National Economic Council, "The Gross National Product and National Income of the Philippines, Calendar Year 1969 to Calendar Year 1971," mimeographed; real values are expressed in 1955 prices. Money supply, price level, imports, and exports from Central Bank of the Philippines, *Statistical Bulletin*, December 1971.

TABLE 1-2

Philippine Imports, 1949–71

Year	Total (mill. U.S. dol.)	Percentage Distribution: Food	Beverages and Tobacco	Crude Materials	Mineral Fuels	Chemicals	Animal and Vegetable Oil	Mfrd. Goods Classified by Materials	Misc. Mfrd.	Machinery and Transport. Equip.	Misc. Commodities
1949	586	25.3	3.4	0.6	6.0	6.0	.4	37.6	7.9	12.8	0.04
1952	421	18.2	4.7	1.2	9.9	7.7	.2	37.2	5.5	15.2	0.01
1953	452	17.0	3.4	1.3	10.8	8.5	.4	36.9	5.0	16.7	0.05
1954	479	16.5	2.3	1.2	11.3	8.0	.4	36.3	5.7	18.2	0.10
1955	548	18.7	2.9	1.6	9.8	8.0	.3	34.9	4.4	19.0	0.4
1956	506	17.4	1.4	2.3	10.4	7.7	.4	32.2	3.2	24.8	0.1
1957	613	17.6	0.3	2.9	9.4	9.3	.4	33.5	3.3	23.0	0.2
1958	559	21.0	0.6	4.0	10.9	9.2	.4	27.7	3.1	22.6	0.3
1959	524	13.0	0.5	5.1	11.4	11.2	.5	26.4	2.9	28.5	0.4
1960	604	14.1	0.1	5.4	9.9	9.1	.4	21.7	2.8	36.0	0.4
1961	611	16.6	0.1	6.0	8.1	10.1	.4	21.7	2.8	33.4	0.7
1962	587	14.9	0.3	6.9	10.2	10.4	.6	20.6	3.0	32.3	0.7
1963	618	16.9	0.3	6.2	10.0	8.9	.6	19.1	3.0	33.8	1.2
1964	780	15.7	0.2	5.3	9.9	9.0	.6	19.7	3.0	35.1	1.5
1965	808	19.2	0.3	4.4	9.5	9.0	.5	18.7	2.6	34.2	1.8
1966	853	14.4	0.5	6.0	9.9	9.2	.5	20.8	2.7	34.8	1.3
1967	1,062	15.1	0.6	4.2	8.8	9.1	.4	19.9	2.5	38.3	1.2
1968	1,150	11.5	0.7	5.9	9.2	9.5	.4	20.3	2.8	38.5	1.1
1969	1,131	11.0	1.0	5.2	9.4	10.0	.4	20.4	2.7	39.2	0.6
1970	1,090	9.6	0.7	5.5	10.9	11.6	.4	21.7	2.5	36.7	0.4
1971	1,186	12.3	0.5	5.6	11.9	12.2	.5	16.5	2.6	37.4	0.4

SOURCE: Central Bank of the Philippines, *Annual Report* for various years.

various raw materials expanded significantly, reflecting Philippine industrialization efforts.

The share of agricultural, fishing, and forestry activity in net domestic product during the postwar period followed a path roughly inverse to that for manufacturing, falling from 38.2 per cent in 1948 to 31.4 per cent in 1960. In 1971, it was 30.6 per cent. As is typical in developing countries, the share of the labor force employed in agriculture is much larger than the share of agriculture in net domestic product. In 1948, the labor force share for agriculture was 71.5 per cent, whereas in 1971 it was 56.0 per cent. Manufacturing absorbed 6.6 per cent of the labor force in 1948 and 11 per cent in 1971.

The importance of the agricultural sector in the Philippine economy is reflected in the composition of the country's exports. As is indicated by the data in Table 1-3, seven of the ten leading exports are crude or simply processed agricultural commodities, namely, copra, sugar, desiccated coconut, coconut oil, copra meal, canned pineapples, and bananas. The other three items—logs and lumber, plywood, and copper concentrates—are forest or mineral products. (See Chart 1-1 for the behavior of total exports and imports over time.) These latter exports reflect the rich endowment of forest and mineral resources in the country. In the mid 1950s more than 60 per cent of the total land area was covered by forests, and logs and lumber have been the fastest growing export items during the period covered by this study. Copper mining is by far the most significant activity in mining and quarrying, contributing 75 per cent to the net value added of this sector; but gold mining, iron ore mining, and chromium ore mining also are moderately important. In addition, manganese ore, mercury, lead, silver, zinc, and molybdenum are mined.

Table 1-4 contains data for the components of the Philippines' balance of payments for various subperiods. The average annual growth rate of exports of goods (in constant prices) over the entire period from 1949 to 1971 was 5.8 per cent. Between 1950 and 1955, the rate was 7.4 per cent; between 1955 and 1960, it was 4.5 per cent; between 1960 and 1965, 7.1 per cent; and between 1965 and 1971, 4.7 per cent. The share of exports of goods and services in real gross national product was 14.5 per cent as of 1971 (see Table 1-5)—about the same as in 1952. The openness of the economy in terms of exports is roughly comparable to that of Thailand, but considerably less than either Malaysia or Taiwan.

It is also brought out in Table 1-5 that gross domestic capital formation is a significant share of gross national product, an important finding. The 19.5 per cent level in 1971 is comparable to the level in such industrial countries as the United Kingdom and Italy and only about three percentage points less than that in Taiwan and Thailand. The steady rise in this figure from around

12 per cent in the early 1950s to its present level is one of the more important economic changes that has taken place in the Philippines over the last twenty years (see Chart 1-1).

In 1969 the per capita official flow of external resources to the Philippines amounted to $3.72. This flow was higher than to Thailand ($2.59), Indonesia ($3.13), or Pakistan ($3.37), but less than to South Korea ($12.72) or Ceylon ($4.00).[4] Foreign aid was much more important in the late 1940s and early 1950s, however. Approximately $1.2 billion of rehabilitation aid was furnished by the U.S. government between 1944 and 1950.[5] Between 1951 and 1956 U.S. economic aid amounted to $171 million and was equivalent to 28 per cent of the investment expenditures of the Philippine government.[6]

Compared to many developing countries, the role of the Philippine government in economic activities has been moderate. Total government expenditures in 1970 were equal to 11.3 per cent of the gross national product in that year. Comparable percentages for other countries at about this time were 20 per cent for Thailand, 24 per cent for Malaysia, 16 per cent for India, and 19 per cent for South Korea.[7]

Although the ratio of government expenditures to GNP has remained roughly the same since the late 1940s, there has been an important shift in the method of financing these expenditures. In 1950 indirect taxes (less subsidies) amounted to 47 per cent of government current receipts, while direct taxes and current transfer payments from abroad were 10 per cent and 39 per cent, respectively.[8] In 1970 the indirect and direct tax components had risen to 68 per cent and 22 per cent, respectively, while foreign transfer payments contributed only 4 per cent.

The inflation record of the Philippines is reasonably good in comparison to many other developing countries. Between 1963 and 1970, for example, wholesale prices rose 45 per cent in the Philippines in contrast to 66 per cent in India, 116 per cent in South Korea, 46 per cent in Turkey, 565 per cent in Chile, and 802 per cent in Brazil. On the other hand, the wholesale price rise during these years was only 7 per cent in Taiwan, 33 per cent in Egypt, 22 per cent in Mexico, and 17 per cent in Thailand.[9] The average annual increase in wholesale prices in the Philippines between 1949 and 1970 was 3.2 per cent. Most of the rise in prices between these years occurred in the 1960s (see Chart 1-1).

As will be explained in more detail in later chapters, monetary policy has often been used to improve the re-election prospects of a particular administration, as well as for furthering the goals of economic development. Between 1949 and 1970, the average annual increase in the money supply was 7.6 per cent (Chart 1-1). The government likewise incurred budgetary deficits for both short-run political purposes and longer-run economic functions. The

TABLE 1-3

Philippine Exports,[a] 1949–71
(millions of U.S. dollars)

Year	Total Exports	Exports of Principal Commod- ities[b]	Copra	Sugar	Abaca	Logs and Lumber	Desic- cated Coconut
1949	247.9	188.3	89.6	45.2	28.9	3.3	19.4
1950	331.0	246.2	138.0	45.9	41.6	10.7	24.2
1951	427.4	287.3	153.1	64.2	67.0	17.3	14.9
1952	345.7	245.9	90.7	89.9	41.0	18.9	9.7
1953	398.3	292.9	117.0	95.8	38.9	28.9	15.7
1954	400.5	315.2	130.1	105.6	26.3	35.6	13.5
1955	400.6	314.5	118.7	106.3	27.8	41.5	12.8
1956	453.2	345.9	134.1	100.6	35.0	48.8	12.9
1957	431.1	322.7	132.0	82.8	39.0	45.1	15.1
1958	492.8	396.9	139.1	115.5	28.8	69.7	16.4
1959	529.5	420.9	138.1	112.6	38.9	80.4	18.2
1960	560.4	446.9	138.6	133.5	41.8	91.6	18.8
1961	499.5	396.2	88.2	135.1	28.8	92.4	14.5
1962	556.0	454.6	113.0	122.0	24.7	112.8	15.1
1963	727.1	609.1	168.3	146.5	31.6	152.9	18.4
1964	742.0	602.6	156.1	148.3	30.4	143.1	19.5
1965	768.5	637.6	170.0	132.4	24.2	162.0	20.4
1966	828.2	705.6	157.2	133.0	18.7	204.7	17.7
1967	821.5	673.9	129.4	141.7	14.7	212.2	17.0
1968	857.3	726.2	123.0	144.0	11.2	216.6	24.6
1969	854.6	709.0	87.3	148.8	14.3	226.0	16.1
1970	1,061.7	877.7	80.1	187.6	15.3	249.8	19.4
1971	1,121.8	928.2	114.0	212.3	[c]	225.9	20.7

Coconut Oil	Copra Meal or Cake	Pine-apples, Canned	Bananas	Veneer	Plywood	Copper Concen-trates
17.5	3.9	6.8	0	0.021	0.02	2.5
12.5	3.8	9.5	0	0.02	0.06	1.7
24.5	3.5	8.1	0		0.06	1.6
15.4	5.7	11.3	0	0.09	0.05	4.2
17.1	4.0	11.0	0	2.6	0.01	3.3
16.6	3.8	4.7	0	0.4	0.2	5.0
16.5	4.4	5.9	0	0.9	0.9	7.4
24.0	5.0	5.5	0	1.2	1.5	13.6
21.4	4.2	4.6	0	1.4	2.3	15.4
24.1	4.4	4.4	0	2.1	6.5	16.8
22.5	5.4	8.0	0	3.2	13.6	21.9
15.7	4.9	7.4	0.02	4.5	6.5	29.6
15.9	4.2	10.5	0.02	4.4	8.0	27.4
31.6	9.1	11.4	0	6.0	11.2	28.6
46.7	11.8	7.3	0	9.3	16.0	41.3
59.9	10.9	7.7	0.01	11.5	22.8	34.3
68.1	11.8	8.7	0	10.5	17.6	46.5
74.5	17.2	8.9	0.02	10.2	17.7	74.6
59.3	10.9	10.1	0.03	8.7	18.2	74.9
77.3	11.0	18.8	0	11.5	21.5	89.2
50.6	9.4	17.2	1.3	10.9	19.5	132.8
95.6	13.9	21.4	4.9	c	19.7	185.2
103.4	16.2	19.7	13.5	c	16.4	185.9

SOURCE: Central Bank of the Philippines, *Annual Report* for various years.

a. The individual commodities listed include all those that were among the leading ten in 1969, 1970, and 1971.

b. This total consists of the ten leading commodities as of 1971.

c. No longer among the ten leading exports.

TABLE 1-4

International Transactions, 1946–71
(millions of U.S. dollars)

	1946–50	1951–55	1956–60	1961–65	1966–71
A. GOODS AND SERVICES					
Exports (f.o.b. incl. nonmonetary gold)	250.40	397.60	507.50	682.77	945.06
Imports	−504.82	−476.12	−561.10	−680.82	−1,080.45
Trade balance	−254.42	−78.52	−53.60	1.95	−135.39
Transportation and merchandise insurance	—	—	−60.58	−53.06	−76.95
Travel	—	—	−11.51	−23.32	17.29
Investment income	—	—	−58.47	−26.64	−86.22
Services rendered to U.S. military	241.18	143.12	25.34	24.89	59.52
Pensions from U.S. govt.	—	—	62.23	53.07	63.84
Private transfers	11.80	6.02	13.98	23.92	29.59
Other services	−77.88	−104.10	—	—	—
Other	—	—	9.58	63.15	26.76
Total A	−79.32	−33.48	−73.03	63.96	−101.20
B. OFFICIAL GRANTS AND LONG-TERM CAPITAL					
Reparations from Japan	—	—	20.74	12.21	32.53
Other official transfers	45.00	—	25.07	5.36	11.79
Private loans	—	7.34	10.24	2.02	73.68
Official loans	—	−1.36	5.38	20.82	23.43
Long-term foreign investment	20.20	28.20	26.93	−10.80	−4.78
Other official capital	5.50	−5.20	4.61	−0.20	−0.84
Total B	70.70	28.98	92.97	29.41	135.81
C. PRIVATE SHORT-TERM CAPITAL AND NET ERRORS AND OMISSIONS					
Private short-term capital	−18.82	−31.66	−0.40	−38.34	67.64
Net errors and omissions			−27.24	−83.58	−130.86
Total C	−18.82	−31.66	−27.64	−121.92	−63.22
D. ALLOCATION OF SPECIAL DRAWING RIGHTS	—	—	—	—	5.84
E. OVER-ALL POSITION (A + B + C + D)	−27.44	−36.16	−7.70	−28.55	−22.77

(continued)

TABLE 1-4 (*concluded*)

	1946–50	1951–55	1956–60	1961–65	1966–71
F. MONETARY MOVEMENTS					
Net IMF accounts	—	2.00	−1.58	0.36	15.70
Commercial bank liabilities			−2.08	36.92	15.19
Other central bank liabilities			5.74	21.87	36.79
Commercial bank assets[a]	52.20	39.56	−1.45	−3.15	−9.45
Central bank foreign exchange[a]			6.86	−9.02	−26.35
Central bank monetary gold[a]			0.13	−4.66	−4.80
Total F	52.20	41.56	7.62	42.32	27.08

SOURCE: Central Bank of the Philippines, *Annual Report*, various years.
a. Minus sign indicates increase.

TABLE 1-5

Distribution of Expenditures on Real Gross Domestic Product,[a] 1948–71
(percentage distribution)

	1948	1952	1955	1958	1961	1964	1967	1971
Personal consumption expenditures	84.0	84.0	87.7	83.8	81.9	78.6	74.6	72.8
General government expenditures	8.0	7.8	7.9	7.7	8.4	9.4	9.2	8.5
Gross domestic capital formation	19.0	11.0	12.3	13.6	15.2	17.5	17.3	19.5
Construction	12.6	8.1	7.2	7.8	8.0	8.4	8.2	5.4
Durable equipment	4.0	1.9	3.2	4.1	5.2	7.0	7.5	11.8
Change in stocks	2.4	1.0	1.9	1.7	2.0	2.1	1.6	2.3
Exports of goods and services	21.3	14.0	12.8	10.2	10.0	11.3	13.0	14.5
Less: Imports of goods and services	26.1	13.2	15.0	10.9	11.7	15.4	18.2	14.0
Expenditures on GDP	106.2	103.6	105.7	104.4	103.8	101.4	95.9	101.3

SOURCE: 1948–67—National Economic Council, *Statistical Reporter*, April–June 1969, p. 62; 1971—National Economic Council, "The Gross National Product and National Income of the Philippines, Calendar Year 1969 to Calendar Year 1971" (May 1972; mimeo.).

a. Prices for 1955 were used to deflate the figures in current prices for 1958 to 1967; 1967 prices were used to deflate 1971 current values.

average annual cash deficit of the national government between 1957 and 1970 was P51 million, an amount equal, however, to only about 2 per cent of average operating disbursements during this period.

PHASES OF EXCHANGE CONTROL IN THE PHILIPPINES

This section contains a brief survey of the payments policies pursued by the Philippine government between 1949 and 1971, presented in terms of the five phases of exchange control suggested by Bhagwati and Krueger (see Table 1-6).[10]

TABLE 1-6

Exchange-Control Phases in the Philippines, 1949–71

Dec. 1949–Sept. 1955	Phase I	Introduction and intensification of exchange controls
Sept. 1955–Apr. 1960	Phase II	Adoption of ad hoc measures to offset some of the unfavorable aspects of exchange controls
Apr. 1960–Jan. 1962	Phase III	Introduction of exchange-control liberalization
Jan. 1962–Nov. 1965	Phase IV	Continued liberalization of exchange controls
Nov. 1965–June 1967	Phase V	Period of complete liberalization
June 1967–Feb. 1970	Phase I	Return to moderate exchange controls
Feb. 1970–Dec. 1970	Phase III	Floating of peso and relaxation of some exchange controls
1971	Phase IV	Further relaxation of exchange controls

In Phase I, exchange controls are introduced, usually in response to an unsustainable balance-of-payments deficit, and gradually intensified. In the Philippines, exchange controls were first introduced in December 1949, after the government had experimented unsuccessfully earlier in the year with import quotas on luxury items. The immediate reason for the use of exchange controls was a full-scale foreign-exchange crisis near the end of 1949 that was closely associated with the expansionist monetary and fiscal policies pursued in connection with the presidential election in the fall of that year. More fundamentally, however, in the immediate postwar period the combination of pent-up demands for consumption and capital goods coupled with the reintroduction of the prewar peso-dollar exchange rate (P2 per dollar), despite a much increased relative cost structure, exerted considerable pressure on the trade balance. This pressure was initially contained by means of large-scale aid furnished by the United States. When this aid began to decline, in 1949, balance-of-payments problems quickly emerged.

Not only did exchange controls gradually intensify in the 1950s, but they became increasingly used to promote industrialization via import substitution. Industrialization became an important goal in the country immediately after the establishment of Philippine independence in 1946. However, although special tax exemptions were granted "new and necessary" industries as early as 1946, it was not until import and exchange controls were introduced that significant progress beyond restoring prewar manufacturing was made in substituting domestic manufacturing for imports of manufactures. Imports of consumption goods under the exchange-control system were, for example, reduced from 50 per cent of total imports in 1950 to less than 15 per cent by 1960. Thus, although exchange control was not deliberately introduced for the purpose of fostering import substitution, this goal soon served as the main rationale for continuing controls over foreign-exchange transactions.

In Phase II policymakers begin to perceive such undesirable effects of comprehensive exchange controls as the disincentive effect on exporters and the reaping of large windfall gains by importers. Consequently, the government adopts various ad hoc measures to combat these effects. It is not possible accurately to date the beginning of Phase II in the Philippines. To a growing degree, as the 1950s progressed, there was dissatisfaction with the system and a realization that there were serious drawbacks associated with it. The main attempt to offset part of the penalty imposed on exporters by the overvalued exchange rate was the enactment, in September 1955, of a law permitting a limited amount of export goods to be bartered for imports outside of the exchange-control system. Efforts to obtain part of the windfall gains related to exchange controls occurred as early as 1950 with an increase in the sales tax and in 1951 with the imposition of a 17 per cent excise tax on the peso price of foreign exchange sold by the banking system. The rise in tariff rates under the Laurel-Langley Agreement in 1955 was also partly directed at capturing windfall gains.[11]

Phase III in the Bhagwati-Krueger schema, the period when formal liberalization efforts are initiated, began in the Philippines in early 1960 when the Central Bank introduced a multiple exchange-rate system. Except for gold sales and tourist receipts as well as purchases of essential goods and certain services, all transactions took place at rates higher than the traditional figure of P2 per dollar. This exchange depreciation was considered to be a first step in a gradual and orderly liberalization process that was to extend over three or four years. It was followed, in the fall of 1960 and spring of 1961, by further increases in foreign-exchange sales by the Central Bank at the depreciated rate (P3.2 and then P3.0 per dollar).

With the inauguration of a new president, in 1962, the plan for gradual liberalization was scrapped in favor of almost complete decontrol and a temporary (until June) floating of the exchange rate. This marked the beginning of Phase IV in the Bhagwati-Krueger schema of exchange regimes, namely, a period of continued liberalization. The decontrol effort fell short of complete liberalization because of the introduction of special time-deposit requirements for letters of credit (in place of the levy on foreign exchange, which was abolished) and a requirement that 20 per cent of export receipts be surrendered at the old exchange rate of P2 per dollar. The time-deposit requirement was gradually liberalized in 1963 and 1964, but the penalty rate for exporters was not removed until a unified rate of P3.90 per dollar was established in 1965.

From late 1965 until mid-1967 the Philippine economy was free of all forms of exchange control and thus could be characterized as being in the final stage of the Bhagwati-Krueger schema, namely, Phase V. The period of complete liberalization was comparatively short-lived, however. Balance-of-payments problems due to the high import level stimulated by the government's easy credit policies and expanded development-oriented expenditure programs were held off for a few years by extensive foreign borrowing from official and private sources. However, as the limited nature of these resources became obvious, the Central Bank reintroduced time-deposit requirements for various classes of imports in June 1967. A steady worsening of the balance-of-payments situation in 1968 and especially in 1969 led to a rise in these requirements in 1968, and finally, in 1969, to the banning of certain nonessential imports. Thus, in 1967 the Philippines could be characterized as re-entering Phase I of the exchange-control schema, though the controls were moderate compared to those of the early 1950s.

When a severe exchange crisis developed, in late 1969 and early 1970, the government elected, in February of 1970, to float the peso and simultaneously eliminate many of the exchange controls that had been introduced since 1967 rather than hold to the existing exchange rate and adopt much more stringent exchange controls. In other words, the government adopted the kind of liberalization policies that typify Phase III in the outline of exchange-control stages. As with the 1962 currency depreciation, exporters were not permitted to exchange all of their dollar earnings at the market rate. Instead, it was required that 80 per cent of the receipts from the major export products be exchanged at the old rate of P3.90 per dollar. This discriminatory treatment of exporters was, however, soon replaced, in May 1970, by an arrangement that permitted exporters to sell their foreign exchange at the free rate but required them to pay a tax on the value of their exports ranging from 8 to 10 per cent. The exchange rate was eventually fixed, in December 1970, at P6.4 per dollar. Gradual movement during 1971 toward further liberalization meant that the economy could be said to be in Phase IV of the exchange-control schema. However, as of early 1972, a prior-deposit requirement still existed, the importation of certain items still could be made only with permission of the Central Bank, and the export tax still was in effect. The exchange rate was also permitted to rise again, in April of 1972, to P6.7 per dollar.

In the next two chapters, a much more detailed description will be given of the various trade and payments policies as well as the related monetary and fiscal measures that were used in the Philippines during the various exchange-control phases of the Bhagwati-Krueger outline. One of the justifications for the series of country studies of which this is a part is that, in order to make further progress in understanding the reasons for the success or failure of various foreign-trade regimes, it is necessary to examine in detail the nature of these regimes in several countries. In short, one must get down to the "nitty gritty" of exchange-control and commercial policies in different economic environments in order to discover why these policies succeed in some circumstances and fail in others. One of the benefits of this approach is that it indicates how a whole series of domestic and international policies are used in an interrelated manner to achieve a goal such as industrialization. To understand the protection afforded to import-competing industries in the Philippines, for example, an investigation limited to exchange-rate and tariff policies is not enough. Such measures as discriminatory sales taxes, margin-deposit requirements, tax exemptions, subsidized lending, and special foreign-exchange fees have been important complements of these policies.

Still another advantage of attention to detail is that it brings out how varied and rapidly changing has been intervention by the Philippine government in the trade and payments field. Economic policy in most countries is not run as if some superhuman mind clearly perceived the economic objectives to be pursued or how any particular measure would affect the achievement of these goals. Instead, there are often elements of both contradiction and overkill in the several policies employed in attempting to reach a particular goal. Moreover, when new groups achieve governmental power or old ones gain experience, the package of economic policies often changes significantly.

A drawback of an in-depth description of external and internal economic policies is that one may be unable to see the forest for the trees. In order to help overcome this problem, brief outlines of the major measures adopted in a particular period will be presented in Chapters 2, 3, and 4 as well as occasional summaries of the main trends. In addition, in Chapter 5, quantitative estimates over time of the combined protective effect of the various policies reported in Chapters 2, 3, and 4 will be presented. Included in an appendix to Chapter 5, for example, are quantitative estimates of the relative importance of the different measures employed to encourage industrialization. The main purpose of the detailed presentation in Chapters 2 through 4 is, therefore, to convey to the reader an appreciation of the complexity and changeability of Philippine economic policies as well as an understanding of the techniques employed to achieve (often conflicting) economic goals.

NOTES

1. Southeast Asia is generally defined as being composed of the following nine countries: Burma, Thailand, South Vietnam, Laos, Cambodia, Malaysia, Singapore, Indonesia, and the Philippines.

2. An average exchange rate for 1970 of P5.895 per dollar is used in this calculation.

3. United Nations, Department of Economics and Social Affairs, *Statistical Yearbook, 1971* (New York, 1972).

4. Ibid., *1970*, p. 712.

5. Frank H. Golay, *The Philippines: Public Policy and National Economic Development* (Ithaca: Cornell University Press, 1961), p. 294.

6. Ibid., p. 300.

7. United Nations, Economic Commission for Asia and the Far East, *Statistical Yearbook for Asia and the Far East, 1971* (Bangkok, 1972).

8. Income from government property added another 4 per cent.

9. International Monetary Fund, *International Financial Statistics*, December 1970 and December 1971.

10. See Appendix A for a detailed description of the phases.

11. The Laurel-Langley Agreement, or the Revised Trade Agreement as it is officially called, is a modification of the U.S.-Philippine Trade Act (the Bell Trade Act) of 1946, which stipulated the manner in which free trade between the two countries would gradually end. The Laurel-Langley Agreement raised the Philippine tariff level and accelerated the pace at which imports from the United States would be subject to the full Philippine tariff rates.