THE ANTI-DEVELOPMENT STATE:

The Political Economy of Permanent Crisis in the Philippines

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INTRODUCTION

Requiem for the EDSA System?

The history of the last eighteen years has been a dreary one for most Filipinos. The promise of political liberation and economic and social progress that accompanied the overthrow of the Marcos dictatorship in February 1986 has remained just that: a promise.

The current political regime in the Philippines stems from the historic uprising that began when tens of thousands of Filipinos congregated in late February 1986 along Epifanio de los Santos Avenue (EDSA) in front of Camp Aguinaldo to stop troops loyal to then-President Ferdinand Marcos from storming the barracks, where anti-Marcos rebel soldiers were holed up. Now remembered as the "EDSA Revolution," the rebellion triggered a chain of events that ended with Marcos's ouster and the inauguration of a new, election-based political system.

This is the regime that we call the "EDSA system" in this book. This is the system of governance that many feel is now in terminal condition, following the elections of May 2004. The administration and opposition slates were made up of candidates pirated from one another's ranks; yesterday's enemies are today's comrades. There was an overwhelming need for a program of economic growth that would address the country's gaping social inequalities, and yet it was a subject studiously avoided by the leading candidates—the administration because it led the country to its worst fiscal crisis ever, the opposition because its presidential candidate would otherwise have been exposed for his lack of grasp of basic economies.

Shortly after the elections, which were widely perceived as having been stolen by the administration, the administration admitted that the country was in the throes of a massive fiscal crisis. To plug record-breaking budget deficits, the government had incurred debt that came to 130 per cent of Gross Domestic Product (GDP). Servicing that debt in 2004 consumed 81 per cent of government revenues and was projected to eat up 89 per cent in 2005. To keep up with payments to local and international creditors, the government had to borrow more, making it ultra-sensitive to downgrades by credit ratings agencies.

A carbon copy of the electoral democracy that was the country's system of governance before it was destroyed by Ferdinand Marcos in September 1972, the EDSA system has reproduced most of the flaws of the former: it has encouraged maximum factional competition among the elite while allowing them to maintain a united front against any change in the system of social and economic inequality.

Two Sides of the EDSA System

The staying power of the EDSA system stems from the fact that, in contrasts to the Marcos regime, it is democratic. Yet it is democratic in the narrow sense of making elections the arbiter of political succession. In the principle of "one man/ woman, one vote," there is formal equality. Yet this formal equality cannot but be subverted by its being embedded in a social and economic system marked by great disparities of wealth and income. Like the American political system after which it is modelled, the genius of the EDSA system, from the perspective of the Philippine elite, is the way it harnesses elections to socially conservative ends.[1] Running for office at any level of government is prohibitively expensive, so that only the wealthy or those backed by wealth can usually think about standing for elections. Thus the masses do choose their representatives, but they choose from a limited pool of people of means that may belong to different factions—those "in" and those "out" of power—but are not ideologically different. The beauty of the system is that by periodically engaging the people in an exercise to choose among different members of the elite, elections make voters active participants in legitimizing the social and economic status quo. Thus has emerged the great Philippine paradox: an extremely lively play of electoral politics unfolding above an immobile class structure that is one of the worst in Asia.

Throughout the EDSA years, the Filipino masses were largely a force that was manipulated electorally to achieve the political ends of competing elite alliances. But alongside the electoral tradition of the EDSA system is an insurrectionary dimension that derives its legitimacy from the manner in which Marcos was ousted from power. In the last eighteen years, it was through an appeal to this insurrectionary tradition that the masses occasionally erupted on the national scene, bursting the electoral parameters to which the elite usually wanted to confine them. In January 2001, the middle class, driven by anti-corruption sentiments, served as the base for the extra-constitutional removal of Joseph Estrada from the presidency in what is now known as EDSA 2. Then three months later, in what is now known as EDSA 3, the lower classes, particularly the urban poor, came together in a mass uprising that was only dispersed by the military at the gates of Malacañang.

Especially in the case of EDSA 3, elite personalities were only nominally at the head of an angry class-based urban insurgency that took the form of a movement to restore to power a defrocked leader who, despite a record of corruption, was seen as a man of the masses. After each insurgency, however, politics settled down to a normal electoral competition managed by elite politicians.

The Anti-Development State

While entrenched corruption is the feature of the EDSA system that has elicited loud protest from the middle class, it had been the utter failure of the system to deliver economic prosperity and reduce inequality that is the greatest source of mass alienation. Close to 10 percent of the Filipino population, or more than seven million Filipinos, now work or live abroad and, according to recent surveys, one out of five Filipinos wants to migrate. The sense of frustration is deepened by the widespread perception that our neighbors in Southeast Asia were achieving "economic miracles" while we remain paralyzed by factional politics and mistaken policies. However much we decry its authoritarian policies, it is hard to deny that Singapore, with its controlled competition, prosperity, and security, has become to many Filipinos the ideal polity, the antithesis of an EDSA system that has become deeply dysfunctional.

Economic stagnation, according to some analysts, may be related to the political system's focus on elite representation and its accompanying parliamentary mechanisms rather than on the development of a strong central bureaucracy that is relatively autonomous from the private sector.[2] The influence of the pre-1930s American model of governance that guided the formation of the colonial and postcolonial state in the Philippines is again evident here. With the rationale of discouraging tyranny, the American pattern of a weak central authority coexisting with a powerful upper-class social organization ("civil society" in today's parlance) was reproduced in the Philippines, creating a weak state that was constantly captured by upper-class interests and preventing the emergence of the activist "developmental" state that disciplined the private sector in other societies in postwar Asia.

In his influential book on contemporary politics in the United States, Daniel Lazare says, "Government in America doesn't work because it's not supposed to work."[3] For much the same reason—the subversion of the democratic potential of the masses by the realities of concentrated wealth and power—one can say the same thing of the Philippines.

Let us briefly review the history of promise and disillusionment of the last eighteen years in order to grasp the depths of disenchantment.

Some say that the promise of the EDSA system was killed early on when President Corazon Aquino made two historic compromises. First, in protecting the family estate Hacienda Luisita, she failed to put her moral authority behind land reform, resulting in an agrarian reform law with a thousand and one loopholes. Second, she chose to make repayment of the foreign debt the national economic priority, thus starving the country of the investment necessary for development. The combination of the lack of structural reform and capital starvation doomed the country to stagnation in the period 1986 to 2003.

President Fidel Ramos tried to take another path, that of triggering growth by liberalizing trade, deregulating the domestic economy, and privatizing state or state-run enterprises and services in line with neoliberal, free-market doctrine. The Ramos saga ended instead with the recession of 1998, which was brought about by the panicky exit of the speculative capital that Ramos's technocrats had courted, precisely by eliminating many controls on their volatile movements and liberalizing the financial sector.

Lower-class disaffection with conservative social and economic policies resulted in the election of Joseph Estrada. Estrada's populism, however, transmogrified into a mafia capitalism in which the president became the apex of an engine of capital accumulation that linked the underworld and the state. The more established section of the elite allied itself with the middle class to overthrow Estrada and displace the nouveau riche faction during EDSA 2. The disaffected nouveau riche tried to get back by riding the spontaneous lower-class anger at Estrada's arrest during the aborted EDSA 3.

Under Gloria Macapagal Arroyo, all social-reform initiatives, including land reform, were placed on the backburner, and development policy was reduced to a strategy of getting US aid and investment by allying the Philippines with Washington in the so-called War against Terror. The Administration's overriding preoccupation became that of getting Arroyo reelected.

How long such a state of affairs can persist is anybody's guess. But the really deep sense of frustration, bitter electoral competition, and EDSA's insurrectionary tradition can interact in volatile ways. EDSA 3 showed how this mix could produce a lower-class insurgency, something that could be set off by a concatenation of events. To many observers, the question is not if EDSA 3 could happen again but when.

Plan of the Book

This book seeks to understand how and why every attempt at economic and social change failed during the EDSA period.

The first chapter, "The Political Economy of Permanent Crisis," explores the interaction of several factors to provide an explanation: the failure to address the underlying structural problems of the country with a program of agrarian reform, the Aquino and succeeding administrations' prioritizing foreign-debt service, and the hegemony of the neoliberal, free-market perspective among policy makers that was institutionalized in the program of unilateral liberalization and membership in the World Trade Organization (WTO).

The second chapter, "Agrarian Reform: Promise and Reality," is a close look at the unraveling of land reform from being what the Aquino administration labelled a centerpiece program" into its present "orphan" status under President Arroyo. A basic contention of this chapter is that a failure of leadership of great proportions must be attributed President Aquino herself. Her spectacular inability to lead by example in refusing to allow her family estate to be subjected to land reform eased the passage and implementation of a land reform law designed to make redistribution of private lands difficult and unworkable.

The third chapter, The Neoliberal Revolution and the Asian Financial Crisis," takes the reader from the rise of neoliberal ideology in the technocracy to the Asian financial crisis and its aftermath. When Ramos came to power, economic reform was high on his agenda, but reform was to be pursued by diluting the power of the state, by emasculating its ability to lead the process of change. Wrongly identifying state intervention—instead of the overwhelming power of private interests—as the main problem, President Ramos pursued a program of liberalization, deregulation, and privatization along the lines of Adam Smith's dictum that "that government is best that governs least." The result was a series of free-market reforms, including capital account liberalization, which left the economy extremely vulnerable when the Asian financial crisis hit in 1997, with the government standing on the side as speculative capital fled the country and brought down the economy.

The fourth chapter, "Multilateral Punishment: The Philippines in the WTO, 1995-2003" details the wrenching process by which the political economy of the Philippines was made "consistent" with membership in the WTO, the most potent multilateral body ever created. Paying special attention to the wide-ranging deleterious impacts of the agreement on Agriculture, the chapter places the Philippine experience in the context of international trade negotiations that climaxed with the failure of the Fifth Ministerial of the WTO in Cancum, Mexico, in September 2003.

The fifth chapter, "The Panacea of Privatization," analyses the travails of the privatization program, with the focus on the unraveling of the scandal-ridden privatization of the Metropolitan Waterworks and Sewerage System, one of the biggest privatization programs ever attempted globally.

Environmental degradation, a hallmark of the two decades of the Marcos dictatorship, continued throughout the EDSA period. The sixth chapter, "Unsustainable Development," shows how the goal of environmentally sensitive development, also known as "sustainable development," to which every administration has paid lip service, was consistently undermined by the prevailing neoliberal framework of structural adjustment.

The seventh chapter, "Corruption and Poverty: Barking Up the Wrong Tree?" brings together case studies of crony capitalism, a phenomenon that was especially evident during the Estrada presidency. Surely crony capitalism, in varying degrees, was a characteristic of other administrations. However, more important, the chapter asserts that given the fact that politics in neighboring countries which have enjoyed rapid growth have been marked by corruption and crony capitalism as bad or worse than that of the Philippines, the country's economic stagnation cannot be attributed to these factors. The chapter strongly suggests that a strong state" that promotes development and disciplines the elite and the private sector is what is missing in the Philippines.

The conclusion, aptly titled "Is There a Way out of the National Impasse?" brings together the various strands of analysis to a synthesis and offers some suggestions for the future direction of Philippine Political and economic development.

This book is the product of a truly collective process. However, specific individuals take principal responsibility for the different chapters: Walden Bello for the introduction, chapters 1, 3, and 4, and the conclusion; Marissa de Guzman for chapter 2; Marylou Malig for chapters 5 and 6; and Herbert Docena for chapter 7. Marco Garrido and Maryann Manahan contributed to chapter 2.

Notes

1. A comparison between elite democracy in the United States and the Philippines is undertaken by Walden Bello in "Parallel Crises: Dysfunctional Democracy in Washington and Manila," in *Back to the Future*, ed. Corazon Villareal (Manila: American Studies Association of the Philippines, 2003). 80-91.

2. See Paul Hutchcroft, "Oligarchs and Cronies in the Philippine State: The Politics of Patrimonial Plunder," *World Politics* 43, no. 3 (April 1991): 414-50; also, Temario Rivera, *Landlords and Capitalists* (Quezon City: UP-CIDS, 1994).

3. Daniel Lazare, *The Frozen Republic: How the Constitution Is Paralyzing Democracy* (New York: Harcourt Brace and Co., 1996), 5.

CHAPTER 1

The Political Economy of Permanent Crisis

The late 1980s and 1990s are not an appetizing subject for a student of Philippine economy. These were, for the most part, dismal years without the drama of the '70s and early '80s.

The overall reality was that of an economy trapped by its accumulated structural weaknesses. It became fashionable in line with the reigning neoliberal ideology to speak about the state suffocating the creativity of the market, but the fundamental reality that linked the Marcos period, the Cory Aquino period, and the post-Cory Aquino period was the existence of an unchanging class structure, in which asset and income distribution was one of the worst in the developing world.

Structural Change and Economic Change

For Filipinos familiar with the experience of the newly industrializing countries (NICs) of Northeast Asia, the importance of profound structural change could not be understated. Massive land reform was a necessary condition of the so-called economic miracle in these societies. Driven by counterrevolutionary motives, land reform in Taiwan and Korea was extensive and swift. Land reform created relatively egalitarian income structures that became the source of domestic demand which drove early industrialization in the 1950s and 1960s.[1]

This type of industrialization based on income redistribution was hardly noticed in the 1950s and early 1960s, when the dazzling import-substitution industrialization of the Philippines, which registered 6 percent to 10 percent annual growth rates in industry, was the envy of Southeast Asia. But the process ran aground, manifested by significantly lower growth rates, in the late '60s. The fundamental structural problem had reasserted itself: the narrowness of the market owing to massive income inequality.

However one thinks about the 1970s and early 1980s, one must acknowledge the fact that the dominant solutions offered to address the problem of underdevelopment did face the structural problem head-on. For the Communist Party of the Philippines-led National Democratic Front, the dominant force on the Left, revolutionary social change was the key, one that while addressing the inequity from a social justice perspective would also provide the solution to the development question. Revolutionary land reform and nationalist industrialization were the twin pillars of a thoroughgoing social structural transformation, one byproduct of which was economic development.

The Marcos regime's response was equally ambitious. At bottom it was Keynesian, that is, informed by a demand-led growth model. Advised by the World Bank to avoid the limited markets of the import substitution strategy, Marcos chose to hitch industrial growth in the country to export markets, which the World Bank pictured as unlimited. The export market thrust became even more critical after the failure of Marcos's land reform program, which was conceived not from a development but from a counterinsurgency standpoint.[2]

Export orientation was, however, more rhetorical than real, and the program eventually amounted to setting up a few export enclaves within a predominantly domestic market-oriented industrial and manufacturing structure. As one analyst noted:

> In fact, trade reform efforts revealed the limits on the power of the liberal technocrats and their multilateral supporters...The incentives to [import substitution] were hardly dismantled and the government's commitment to [export promotion] was limited. Export enclaves remained just that: enclaves within an inward-oriented economy.[3]

The Labor Export Policy

With land reform failing to take off and export-oriented growth lacking dynamism, a third Marcos program that was initiated in the mid-'70s became critical in addressing the problems of employment and generating income for a rapidly expanding population: the labor-export policy. Marcos bluntly stated the aims of the policy:

> For us, overseas employment addresses two major problems: unemployment and the balance-of-payments position. If these problems are met or at least partially resolved by contract migration, we also expect an increase in national savings and investment levels.[4]

What was initially conceived as a temporary palliative, however, became a permanent institution that was upheld by the administrations that succeeded the dictatorship. This was because it had become so central to the survival of millions of Filipinos amidst generalized economic stagnation. Almost 6.3 million Filipinos have been deployed for overseas jobs from 1984 to 1995.[5] Currently, according to labor-export specialist Jorge Tigno, "the total number of Filipinos overseas is estimated at roughly 6.5 million, a figure that comprises almost 10 percent of the country's total population. It is said that Filipino overseas migrant workers are approximately equivalent to as much as 15 percent of the Philippines' 26 million labor force. In Metro Manila, one out of every three households has a member who was abroad."[6]

In economic terms, the impact of labor export was massive. Recorded remittances of overseas workers rose from $103,000 in 1975 to $4.88 billion in 1995. By 2002, workers' remittances reached $6.9 billion, an increase attributable to the rise in the number of higher-paid workers such as caregivers, engineers, and performing artists in an area formerly dominated by lower-skilled workers such as domestics and seamen.[7] An International Labor Organization study, in fact, claimed that remittances could come to more than 20 percent of export earnings, and as much as 4 percent of gross domestic product (GDP).[8]

What overseas employment amounted to then was, politically, an absorber of energies that might otherwise have gone into radical or revolutionary solution and, in economic terms, an external employment mechanism in the absence of development. In fact, the economic function of labor export went beyond employment: remittances from overseas workers became a key factor in propping up the peso after the Asian financial crisis.[9]

Structural explanations and structural solutions to Philippine underdevelopment disappeared during the Aquino administration as liberal democracy was restored and the revolutionary movement ran out of steam. Under the Aquino administration, democracy was restored, but the priority of economic policy became that of repaying the country's massive external debt of $26 billion that had been contracted by the Marcos regime during the easy petrodollar era in the 1970s. One cannot, however, understand the full consequences of the debt problem without taking into consideration the imposition of structural adjustment in the Philippines.

Structural Adjustment and Debt Repayment

"Structural adjustment" did not refer to an effort to transform the fundamental socioeconomic structures of the country to consciously bring about development, but to one designed to alter the balance between the market and the state in the Philippine economy in order to promote economic efficiency. Structural adjustment in the Philippines, which was initiated in 1980, sought—at least at the rhetorical level—to achieve greater efficiency through thoroughgoing liberalization, deregulation, and privatization. Growth and development were to be byproducts of efficiency in the narrow sense of reducing the unit cost of the output of productive activity. Adjustment was not, however, divorced from conjunctural needs: among the immediate problems it was meant to address was to gain the foreign exchange to service the Philippines' burgeoning foreign debt via greater export orientation.

Adjustment unfolded in roughly three phases: the first from 1980 to 1983, when the emphasis was placed on trade liberalization; the second, from 1983 all the way to 1992, when the focus shifted to debt repayment; and the third, from 1992 until the end of the decade, when all-sided free-market transformation marked by rapid deregulation, privatization, and trade and investment liberalization was the order of the day.

During the first phase, a process of trade liberalization was pushed on a hesitant government in which close associates of the Marcos regime were waging a rearguard war to protect their privileged positions, and local firms were seeking to preserve their preferential access to the domestic market. Despite this resistance, structural adjustment, which was implemented with two laws from the World Bank, forged ahead. Between 1981 and 1985, quantitative restrictions were removed on more than 900 items, while the nominal average tariff protection was brought down from 43 percent in 1981 to 28 percent in 1985.[10]

But liberalization slowed down significantly in 1983, when international recessionary trends combined with the structural adjustment program's liberalization component and its tight fiscal and monetary policies to create a vicious cycle that plunged the Philippine economy downward. "Whatever the merits of the SAL [structural adjustment loan]," noted one analyst, "its timing was deplorable."[11] The program failed to adjust to the onset of a world recession, so that instead of rising, exports fell, while imports, taking advantage of a liberalized regime, severely eroded the home industries. Instead of allowing the government to promote countercyclical mechanisms to arrest the decline in private sector activity, the structural adjustment framework intensified it with its policy of high interest rates and tight government budgets. Not surprisingly, the gross national product (GNP) shrank precipitously two years in a row, contributing to the deepening of the political crisis that resulted in the ousting of Ferdinand Marcos in February 1986.

By that time, the Philippines' foreign debt had risen to over $26 billion from $21 billion in 1981, when the process of adjustment began. This led the World Bank and the International Monetary Fund (IMF), under strong pressure from the big commercial creditors, to put the emphasis on debt repayment on their agenda for the new administration of President Corazon Aquino. Fairly quickly, international finance faced the fledgling democratic administration with an unpalatable choice: either limit debt service payments or fully comply with debt obligations in order to preserve creditworthiness even at the risk of throttling growth.

The first position was espoused by Professor Solita Monsod, then the director of the National Economic Development Authority (NEDA) and some of her colleagues at the University of the Philippines School of Economics, who wrote: "The search for a recovery program that is consistent with a debt repayment schedule determined by our creditors is a futile one and should therefore be abandoned."[12] Central Bank Governor Jose "Jobo" Fernandez, a Marcos holdover, "warned of the risk of 'economic retaliation against the country' should it take unilateral actions in defiance of its creditors. Trade credit lines could be withheld 'paralyzing foreign trade,' and foreign assistance could be terminated."[13] Citibank President John Reed visited the Philippines and warned that debt repudiation "would produce immense suffering and difficulty for the people."[14]

The so-called model debtor strategy won, partly because proponents of the opposite position did not put up more than token opposition. This was a mistake, notes one analyst, in light of concurrent developments:

> The credibility of these threats is...open to serious doubt. Brazil defied its commercial creditors for 18 months, beginning with the unilateral suspension of debt service announced in February 1987. Its defiance provoked much posturing by the banks, but little genuine retaliation. The holders of paper assets proved to be paper tigers. Similarly, the well-publicized but less drastic debt service ceiling imposed by Peruvian President Alan Garcia did not bring grievous penalties; the Garcia government's heterodox economic program ultimately failed despite the debt policy, not because of it. More quietly, Bolivia halted most debt service payments in 1984, and three years later won [a] very favorable debt buy-back deal.[15]

The model debtor strategy was inaugurated by President Aquino's Proclamation 50, which committed the government to honoring all of the Philippines' debt, including odious ones like those contracted to build the Bataan Nuclear Power Plant as well as the so-called behest loans made by cronies of the Marcos dictatorship. The strategy was institutionalized by Executive Order 292, which affirmed the "automatic appropriation" of the full amount needed to service the debt from the budget of the national government that was originally mandated by Marcos's Presidential Decree 1177.[16]

A financial hemorrhage marked the succeeding years, with the net transfer of financial resources to external creditors coming to a negative $1.3 billion a year on average between 1986 and 1991.[17] In the late '80s, foreign-debt servicing came to $3.5 billion a year, or about 10 percent of the country's gross domestic product.[18] A decade later, in 1999, the level of outflow of financial resources continued to be massive. The fundamental irrationality of the process was underlined by the fact that as overseas workers were remitting hard-earned dollars into the country, an equal if not greater amount was leaving it.

The Neoliberal Perspective

To the neoliberal economists who came to dominate the technocracy and the academe in the late '80s and early '90s, however, structural adjustment was seen as a precondition for growth and debt repayment as an unpleasant but temporary condition. For these economists, many with newly minted Ph.D.'s from US universities, others with resumés boasting stints at the World Bank, the problem was too little market and too much state. They were deeply envious of the performance of our East Asian neighbors and were resolved to "catch up." The key to the success of the NICs, Filipinos were told, were their free-market policies. Structural adjustment was a policy in the right direction but its impact had been uneven. Freeing trade was the answer, even if this process was a unilateral one.

In 1991, while free-marketeer Jesus Estanislao was finance secretary, the Aquino administration came out with Executive Order 413, which sought to "simplify" the Philippine tariff structure into four rates: 30 percent for finished products, 20 percent for intermediate inputs, 10 percent for raw materials, and 3 percent for capital equipment.[19] Among the architects of the 1991 tariff reforms was Cielito Habito, who went on to become the head of NEDA under President Fidel Ramos (1992-1998). In that capacity he spearheaded the tariff liberalization effort that resulted in the famous Executive Order 264, which committed the Philippines to unilaterally bringing down tariffs on all but a few sensitive products to 1 percent to 5 percent by 2004.

The model for Habito and other neoliberal technocrats was the Chilean tariff reform under the dictator Augusto Pinochet, which had brought all tariffs to 11 percent or under. If the Chileans could manage to bring down their tariffs to 11 percent, surely the Filipinos could manage to bring them to 5 percent and below! In their eagerness to catch up with our neighbors, what the Filipino technocrats saw was only Chile's growth rate, not the enormous social crises that had been induced by its free-market policies.[20]

In a recent retrospective article on trade liberalization, Habito claims that a program of unilateral trade liberalization was necessary because, prior to the tariff reforms of 1991, "our average tariff rate... was well over 40 percent, which put us at a disadvantage with our neighbors who had pulled ahead of us in economic performance in the 1980s" because they "had begun simplifying and lowering their trade barriers much earlier than we did..."[21]

Habito's remarks go a long way toward revealing why the program of tariff and trade reform went so badly awry—why instead of bringing about prosperity, unilateral trade liberalization has resulted in the rapid erosion of this country's industrial and agricultural base. It is important to dwell on his analysis since it provides the rationale for fateful decisions on tariff reform made twelve years ago, which had such a devastating impact on agriculture and industry in the coming years. His comments provide a case study of how doctrinaire economics can produce analytical errors that lead to tragic policies.

Habito makes three key points: 1) that the average tariff rate stood at over 40 percent prior to the 1991 reforms, 2) that our tariff liberalization was well behind that of our neighbors, and 3) that it was their allegedly swifter and more thorough tariff liberalization that accounted for the superior performance of our ASEAN (Association of Southeast Asian Nations) competitors.

On the first point, he is simply wrong. Way before Executive Order 413 in 1991 initiated the unilateral liberalization program, the Philippine tariff structure had already been radically altered. Under the structural adjustment program of the IMF and the World Bank, the average tariff rate was brought down from 43 percent in 1980 to 28 percent in 1986 while quantitative restrictions were removed on more than 900 items between 1981 and 1985.[22]

The second point Habito makes—that our neighbors outstripped us in trade liberalization in the 1980s—does not survive critical scrutiny. The average tariff rates in Indonesia and the Philippines were just about equal in 1989, at 28 percent and 27 percent, respectively. However, the removal of quantitative restrictions in the Philippines proceeded at a faster pace than in Indonesia. In the Philippines, the percentage of goods under import restriction fell from around 34 percent in 1985 to 17 percent in 1986 and further to 8 percent at the end of 1989.[23] In Indonesia, the share of imports subject to non-tariff barriers declined from 43 percent in mid-1986 to 21 percent in 1988 to 13 percent in 1991.[24]

The average tariff rate of 28 percent in the Philippines in 1986, after the IMF-World Bank structural adjustment reform, was actually lower than that in Thailand. And, in fact, in the mid-'80s, the effective rate of protection for manufacturing in Thailand was 52 percent, compared to 23 percent for the Philippines.[25]

Misinterpreting ASEAN Industrialization

Habito's third claim—that it was trade liberalization which accounted for the high growth rates in our neighbors—is highly questionable. This assumption formed part of a broader perspective that many Filipino technocrats had when viewing our neighbors' performance prior to the Asian financial crisis: that these economies were significantly more market-friendly and experienced much less state intervention than the Philippine economy. Typical in this regard are the comments of Estanislao: "Government takes very good care of macroeconomic balances, takes care of a number of activities like, for example, infrastructure building, and leaves everything else to the private sector. And that is exactly what Singapore, Malaysia, Indonesia, and Thailand have done, and that is what the Philippines should be doing, and we are beginning to do it."[26]

This picture did not correspond to reality. True, in Indonesia, Malaysia, and Thailand, the state may have played a less aggressive role than in Korea and Taiwan, but an activist state posture—manifested in industrial policy, protectionism, mercantilism, and intrusive regulation—was central in the drive to industrialize.

For instance, Thailand began to register the 8 percent to 10 percent growth rates that dazzled the world, when it was moving to a "second stage of import substitution"—the use of trade policy to create the space for the emergence of an intermediate goods sector—during the second half of the 1980s.[27]

In the case of Malaysia, while it is true that some privatization and deregulation favoring private interests took place in the late 1980s, it would be a mistake to overestimate the impact of these policies. Two examples suffice to underline the central—and positive—role of state intervention. Petronas, the state oil company, was consistently rated as one of East Asia's best-run firms. And certainly one of the most innovative—and successful—enterprises in the whole region was a state-directed joint venture between a state-owned firm and a foreign automobile transnational corporation, Mitsubishi, which produced the so-called Malaysian car, the Proton Saga. The Proton Saga now controls two-thirds of the domestic market and turns a profit for its producers. Yet its development exemplified all the so-called sins of industrial policy that neoclassical economists such as Habito and Estanislao have warned against: discriminatory tax treatment of competitors, strategic industrial targeting or a systematic plan to manipulate market incentives to create a local car industry, and forced local sourcing of components to encourage the growth of local supplier industries.[28]

As for Indonesia, some change along market-oriented lines did take place in the 1980s and 1990s, but up to the end of the Suharto period in May 1998, the state continued to be the most important actor in the economy. Hardly any of the big state enterprises passed to the private sector. State enterprises contributed about 30 percent of total GDP and close to 40 percent of non-agricultural GDP. Government production accounted for 50 percent of the mining sector, 24 percent of manufacturing GDP, 65 percent of banking and finance, and 50 percent of transport and communications.[29] Indeed, in the last decade of the Suharto regime, there was a resurgence of statist policy in the form of trade policy, subsidies, and other mechanisms directed at the creation of a heavy-industry nucleus around which to center the economy, including the development of an automobile industry, an integrated steel complex, a shipbuilding complex, and an aircraft industry.

In sum, some liberalization was going on in our neighbors' economies, but it was selective liberalization pursued in the context of strategic protectionism driven by the state, the objective of which was to deepen the industrial structure.

To recapitulate, contrary to Habito's contention, the pace of trade liberalization in the Philippines in the 1980s did not differ from that of its neighbors, so that it is difficult to attribute the difference in economic performance to this factor. Nor is it possible to argue, as does Estanislao, that it was the presence of a non-interventionist state that accounted for our neighbors' superior economic performance, for, if anything, government was more intrusively interventionist among our neighbors than in the Philippines.

Japanese Capital: The Missing Factor

So what spelled the difference between the Philippines and its neighbors? The short answer is Japanese capital. In the period 1985-93, some $51 billion worth of Japanese investment swirled through the Asia Pacific in one of the most rapid and massive outflows of foreign capital toward the developing world in recent history. The cause of the massive outflow was the Plaza Accord of 1985. By sharply raising the value of the yen relative to the dollar and other major hard currencies, this agreement made production in Japan prohibitive in terms of labor costs, forcing the Japanese to move the more labor-intensive processes of their manufacturing operations to low-wage areas, in particular to China and Southeast Asia.

Some $15 billion worth of Japanese direct investment flowed into Southeast Asia between 1985 and 1990, with Indonesia receiving $3.1 billion, Thailand $3.7 billion, and Malaysia $2.2 billion.[30] The inflow of Japanese capital allowed these countries to have access to foreign capital at a time when US and international banks were tightening up on lending owing to the Third World debt crisis. Even more important, Japanese investment allowed the Philippines' neighbors to surmount recession and move on to a path of high-speed growth as they not only received Japanese capital but were tranformed into essential parts of regional industrial economy that was being forged around a Japanese center. As one Japanese diplomat candidly put it, "Japan is creating an exclusive Japanese market in which Asia-Pacific nations are incorporated in the so-called *keiretsu* [financial/industrial bloc] system."[31]

Thai technocrats, for instance, had no doubts about the source of their country's dynamism. As one of them wrote, "The current explanation of Thailand's accelerated growth was the 1985 appreciation of the value of the yen, rendering Japanese production more costly. Japanese multinational companies were forced to look for new lower-cost production locations. In 1987, Japanese investment approvals by Thailand's Board of Investments exceeded the cumulative Japanese investment for the preceding 20 years."[32] The truth is that whatever might have been the Thai government's policy preference—protectionist, mercantilist, or market-oriented—the vast amounts of Japanese capital coming into Thailand could not but trigger rapid growth. The same was true in the two other favored recipients of Japanese investment, Malaysia and Indonesia.

The Philippines was bypassed by this massive flow of Japanese investment. Relying on various sources, Japanese expert Kunio Yoshihara estimates that between 1987 and 1991, a paltry $797 million entered the Philippines, while Thailand received $12 billion.[33] Including investment from Taiwan and Hong Kong that followed in the Japanese wake, the difference was even more marked: Thailand received $24 billion in investment during the same period, or 15 times the amount invested in the Philippines, which came to $1.6 billion. "This difference in the flow of foreign investment from the three countries," Yoshihara rightly noted, "produced a significant disparity in growth performance of the two countries [Philippines and Thailand] during the period."[34] Moreover, in contrast to Thailand, the Philippines was barely integrated into the dynamic regional industrial economy being constructed around the Japanese center.

A Depressed Market

This brings up a more fundamental issue: Why did the Japanese avoid the Philippines? Some say it had to do with political instability—these were, after all, the years when the Philippines was wracked by six attempts at a military coup. But Japanese investors have not been known to shun conflict situations where there is a prospect of making a profit, so this was probably not decisive.

Was it because of foreign investment legislation? Again, this is unlikely since Thailand, for instance, had the same discriminatory provisions against foreign investors as the Philippines: foreigners were not allowed to own land; they were prevented from entering certain industries by Alien Business Law; they were not allowed to own majority of equity in retail trade enterprises; and there were restrictions on the number of foreign technicians allowed to work in Thailand.[35]

Were the Japanese put off by corruption? But corruption was endemic to all the Philippines' tiger neighbors that Japanese capital migrated to, from South Korea to Indonesia. Politics in South Korea, for instance, was, at least, just as corrupt as in the Philippines.[36] Indonesia was widely known in the '80s and '90s as being more corrupt than the Philippines, with Vice President Adam Malik admitting that it reached epidemic proportions in the bureaucracy and business.[37] As for another favored site, Thailand, part and parcel of the boom of the late '80s and '90s was an inflation of corruption.[38] A favorite theme of establishment writings on the tiger economies prior to the Asian financial crisis, the "neutral technocracy" theory to explain NIC success was, in fact, buried after the collapse by the same people, who began to attribute it to Philippine-style "crony capitalism" in these societies.[39]

Perhaps far more important in explaining the relative absence of Japanese capital were simple profit calculations. Japanese investors are strategic investors—that is, they invest if there is the prospect of a growing market. They are not just interested in cheap labor or using a country as an export-production platform; they are keen to exploit local markets. In the late 1980s, the Philippines was simply not attractive since development, expansion of the market, reducing poverty to create more purchasing power were all being sacrificed to the national priority of repaying the foreign debt—a goal forced on the country by the IMF and the World Bank acting on behalf of the country's foreign lenders.

The GDP registered average growth of below 1.5 percent between 1983 and 1993, and the reason is not hard to find. Government is by far the biggest investor in the Philippines, and during the Aquino administration debt repayment ate up funds that would otherwise have gone into capital expenditures. Very little could be spared for improving the country's physical, technical, and educational infrastructure. As one analyst noted toward the end of the 1980s, servicing the debt "required what are euphemistically termed 'adjustments': domestic consumption and investment had to be curtailed to free resources for debt service."[40] Moreover, the "negative net transfer can be expected to continue indefinitely, unless temporary relief arrives in the form of a massive infusion of new lending (implying in turn still larger debt service obligations in the future) or a more permanent solution is achieved by means of an alternative debt management strategy."[41]

The Aquino administration chose the path of least resistance: go into more debt. New debt was piled on to past debt, partly to pay for past debt coming due. From Php 625.6 billion in 1986, public debt rose to Php 945.2 billion in 1991.[42] Obliged to cover the payments coming due by the automatic appropriations law, the government allocated 50 percent of the national budget to debt service in 1987, with the figure not going below 40 percent in the next four years.[43]

The resulting social impact sent the wrong signal to prospective Japanese investors interested in profitably exploiting the domestic market: Filipino families living below the poverty line in 1991 came to 46.5 percent—a marginal reduction from the 1985 figure of 49.3 percent.[44] Income distribution actually worsened with the share of income going to the lowest 20 percent of families falling from 5.2 percent to 4.7 percent, while that going to the top 10 percent rose from 36.4 percent to 38.6 percent.[45] True, income inequality was also growing in our neighbors, but, unlike in the Philippines, rapid growth was pushing down poverty levels and bringing more people into the market.

From the perspective of Japanese investors, the Philippines appeared to be a strategically depressed market—one not worth sinking a lot of investment in. And so they bypassed the country and deprived it of the same externally induced boom experienced by our neighbors.

The Tragic Consequences of Doctrinaire Economics

It is amazing how these realities could elude our neoliberal technocrats. Yet it is not unusual. In the history of the natural sciences, as Thomas Kuhn claimed in his pathbreaking *The Structure of Scientific Revolutions*, paradigms harden into doctrines that filter out realities inconsistent with the premises of the paradigm.[46] The tragedy of the Philippines is that instead of being guided by realities on the ground, the neoliberals allowed doctrine—the dictum that the unfettered market would bring about the best of all possible worlds—to guide their analysis and subsequent policies. Not only did they err in discerning the causes of economic stagnation in the Philippines, but they misinterpreted the factors

that led to rapid growth among our neighbors. And it was this doctrinal distortion of our neighbors' experience that served as the justification for the policy of unilateral liberalization.

Instead of carefully calibrating trade policy and industrial policy, as our neighbors did, they brought about an indiscriminate liberalization of trade that has destroyed many local industries, destabilized agriculture, and thrown hundreds of thousands of people out of work.

Instead of taking steps to stop the hemorrhaging of financial resources, that was the main drag on development and repelled investors seeking healthy investment prospects, they allowed the bleeding to go on and on, until by 2002, the public debt was Php 870 billion more than the Philippine GNP.[47]

The hemorrhaging was not, however, only financial. Servicing the debt meant intensifying the export of natural resources to earn dollars. Natural-resource exports accounted for a staggering $23 billion of the $50 billion worth of products exported by the country between 1981 and 1989.[48] But the environmental impact of the decade-long stagnation and crisis that stemmed from the "debt repayment first" strategy was much more comprehensive. As one study pointed out, it

> created so much unemployment that migration patterns changed drastically. The large migration flows to Manila declined, and most migrants could turn only to open access forests, watersheds, and artisanal fisheries. Thus the major environmental effect of the economic crisis was overexploitation of these vulnerable resources.[49]

Instead of channeling resources generated from local production to domestic investment, instead of debt service, they chose the route of capital account liberalization to invite foreign speculative capital to play that role—a policy that led, tragically, to the financial crisis of 1997-98.

Instead of confronting head-on the roots of Philippine underdevelopment in the complex interplay of internal and external forces, structural and conjunctural factors, these academics and consultants came to power armed with a very uncomplicated approach to policy making: radically reduce the role of the state, radically expand the play of market forces.

It was a seductive doctrine that avoided having to learn from the complicated interaction of market and state that had produced the so-called Asian economic miracles. Important policy differences, such as those between selective liberalization and indiscriminate liberalization, and between opportunistic protectionism and strategic protectionism, were conveniently ignored. As a consequence, driven by technocrats who were locked into a paradigm that misinterpreted and distorted the experience of our neighbors, the Philippines passed from a regime of opportunistic protectionism to a free-trade regime that was strategically directionless, one that was simply guided by the faith that the invisible hand of the market would somehow bring about growth. After the interlude that was the Asian financial crisis, the clear superiority of the strategic protectionist model followed by Malaysia and Thailand is once more asserting itself over the indiscriminate liberalization model followed by the Philippines.

Instead of strengthening the state to push the elite and the private sector in development-friendly policy directions, as was the case in Taiwan, Korea, Singapore, and Malaysia, in the name of "market efficiency" and "weeding out corruption," they set about dismantling the state's role in planning, production, trade, and finance. Not surprisingly, under their watch, an already weak Philippine government bureaucracy was even more thoroughly colonized by private interests.

For a time, neoliberalism seduced some sectors of the population, for with its simple formula that doing nothing was government's best contribution to growth, it seemed to offer a relatively costless path to growth. No longer.

A Doctrine Discredited

In 2003 three events symbolized the discrediting of a doctrine.

The first was the admission of the outgoing finance secretary, Isidro Camacho, that owing to massive debt obligations, the country was in a very deep fiscal crisis. "[We] could not deny the numbers," he said in a speech before the Philippine Economic Society. "We have a very high debt that is not sustainable unless we do something."[50] The public sector by the end of 2003 was Php 5.1 trillion in debt. Debt servicing was costing the country around Php 357 billion, or 46 percent of the total budget. Long ignored by government technocrats as a central cause of the Philippines' inability to move into sustained growth, the debt crisis had again exploded with a vengeance.[51]

The second was increasing criticism in government circles of the World Trade Organization (WTO), which had emerged as the principal engine of global trade liberalization in the 1990s. Both the principal representatives of the government to the Fifth Ministerial of the WTO in Cancun, Mexico, then Trade Secretary Manuel Roxas II and Agriculture Secretary Luis Lorenzo Jr., opposed additional tariff reductions on agricultural and industrial commodities demanded by the trade superpowers and hailed the collapse of the meeting as beneficial for the country and the developing world as a whole. Both also proclaimed with pride the adhesion of the Philippines to the Group of 20, a new grouping of developing countries that challenged US and European Union dominance of the trade body.[52]

The third event was the issuing on October 2, 2003, of Executive Order 241, which reversed the twelve-year-old program of unilateral liberalization, much to the dismay of Habito and other architects of the unilateral liberalization program. Several executive orders also increased tariffs or froze tariff reductions on commodities such as vegetables, sugar, and fishery products.

Over two decades of trade liberalization, beginning with the World Bank-IMF structural adjustment, had reduced the effective rate of protection for manufacturing from 44 percent to 20 percent. That had been achieved at the cost of multiple bankruptcies and massive job losses. The list of industrial casualties included paper products, textiles, ceramics, rubber products, furniture and fixtures, petrochemicals, beverage, wood, shoes, petroleum oils, clothing accessories, and leather goods. An indication of the comprehensive negative impact of unilateral liberalization was the decision of a government review committee constituted under Executive Order 241 to raise tariffs on 627 of 1,371 locally produced goods to provide relief to industries suffering from unfair competition from imports.[53] One of the industries most severely affected by the tariff cuts, as well as the abuse of duty-free privileges, was the textile industry, which shrank from 200 firms in the 1970s to less than 10.[54] Camacho's words were unambiguous: "There's an uneven implementation of trade liberalization, which was to our disadvantage."[55]

While consumers may have benefited from tariff cuts, "it has killed so many local industries..."[56]

According to Rene Ofreneo, former dean of the University of the Philippines School of Labor and Industrial Relations, it is worth noting that while most of our tariffs are only a third of those in China and Thailand, it is protectionist China and Thailand rather than neoliberal Philippines that have succeeded in the international market. This outcome is contrary to the prediction of the theory of unilateral liberalization. Citing the observation of economist Josef Yap of the Philippine Institute of Development Studies, Ofreneo continues:

> [T]hree decades after [being] enthroned as the guiding economic framework, the neoliberal economic paradigm has failed to achieve the so-called structural transformation of the economy. The share of manufacturing in total employment, recorded at 10-12 percent in the 1960s, has remained stagnant at 9-11 percent and is even threatening to go down, no thanks to the absence of an active or forward-looking industrial policy that our more successful Asian neighbors have adopted. The neoliberal economic paradigm constitutes a policy of false hopes—hopes that once we open up the economy, the investors would come in and hopefully, they would create new export industries, while domestic industries, hopefully, would invest on modernization and would become globally competitive. By imposing their narrow liberalization program on society, the neoliberal economic technocrats have managed to destroy many of our domestic industries such as textile, rubber, ceramic, and so on, while succeeding only in establishing a very modest level of export orientation based on two industries (garments and electronic assembly) with a shaky and uncertain future.[57]

But deindustrialization was not the only result of trade liberalization. Camacho linked unilateral trade liberalization to the massive fiscal and debt crises bedeviling development, saying, "The severe deterioration of fiscal performance from mid-'90s to last year could be attributed to aggressive tariff reduction." Had the government not implemented its tariff reduction program, Camacho estimated that the government could have earned more than enough taxes to cover its Php 210-billion budget deficit in 2002.[58] Instead, customs collections declined from 5.6 percent

of GDP in the mid-1990s to 2.8 percent,[59] forcing government to resort to even greater borrowing from foreign and local sources.

Perhaps a fitting epitaph to the policy of unilateral trade liberalization was provided by Justice Florentino Feliciano, a former presiding judge of the WTO Appellate Body on Dispute Settlement, who called it a policy of "unilateral total disarmament."[60] Neoliberalism had been tried, and it had been found not only wanting but disastrous.

The pragmatic retreat from neoliberalism was not, however, accompanied by an ideological one, for government technocrats still articulated their goals in terms of achieving market efficiency. Nor was there an effort to supplant the discredited strategy with a new, coherent policy of development. Insofar as the Arroyo administration had a development strategy, it was the economics of military alliance with the US in the wake of September 11. Massive economic aid and investment from US business was at the top of President Arroyo's concerns when she reversed ten years of an increasingly independent foreign policy followed by the country since the expulsion of the US bases in 1992. "It's $4.2 billion, and counting," she gushed during her state visit to Washington in October 2001, calculating the sums of aid and capital promised by President George W. Bush. Most of that money failed to materialize, however, leading to a sense of malaise and drift throughout 2002 and 2003, as the fiscal crisis deepened and Arroyo increasingly devoted herself to getting herself reelected.

Economic-policy thinking in the establishment was at a dead end by the beginning of the electoral campaign of 2004—a sad state of affairs proclaimed by the fact that although economic issues were the central concerns of the population, neither the administration nor the opposition dared to talk about an economic agenda—the administration because it had brought the country to a massive fiscal crisis, and the opposition because it had no alternative to offer and because its candidate, Fernando Poe Jr., had little grasp of economic policy.

Notes

1. For an extended treatment on the importance of agrarian reform in Taiwan and Korea's development, see Walden Bello, "Agrarian Reform in Taiwan and South Korea: Positive and Negative Lessons for the Philippines,"