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How the Philippines copes with the global financial crisis

In the midst of falling stock indices, tight liquidity, low investor confidence and failing financial institutions, the International Monetary Fund has described the current financial crisis as the "largest financial shock since the Great Depression."

While it initially reared its ugly head in Wall Street, analysts believe it has now begun to spread to the real economy, threatening the growth prospects of people on Main Street. Worse, its effects are being felt not just in the United States, but in other parts of the world as well, including the Philippines.

Stable financial sector

The Bangko Sentral ng Pilipinas (BSP) said that some local banks had around US$386 million of investments in Lehman Brothers, one of the investment houses that failed as a result of the crisis. It pointed out, however, that this amount represents less than one percent of the entire banking system.

It said that key performance indicators showed sustained strength of banks' balance sheets, continued asset expansion and a growing deposit base. There are likewise no apparent problems with liquidity, as evidenced by a 24.1 percent year-on-year increase in bank lending in August, up from the 23.9 percent growth in July. Bulk of the growth came from loans for production activities which grew by 19.8 percent.

The steady flow of remittances from OFWs has also helped stabilize the economy by driving consumption growth and ensuring a steady influx of foreign exchange. It hit US$14.5 billion in 2007 from US$12.7 billion in 2006. Government expects remittances to hit US$17 billion this year.

In addition, government's fiscal position has been improving. "The budget deficit fell to PhP12.4 billion in 2007 from PhP187 billion in 2004 while public sector accounts have posted surpluses in recent quarters, thanks largely to fiscal reform measures such as the Expanded Value Added Tax law," said Socioeconomic Planning Secretary Ralph Recto.

Sound macroeconomy

Recto explained that fiscal reforms, effective monetary management and sound macroeconomic policies enabled the economy to post a record 7.2 percent GDP growth in 2007. With the onset of the multiple crises plaguing the international market, however, growth has slowed to 4.6 percent in the first half of this year.

The economy's performance may have slowed, but it is nonetheless respectable considering that other countries in the region also suffered a slowdown. "Economic growth in the Philippines as well as those of Asian neighbors was dragged down by high inflation and slower growth among advanced economies, which hurt consumer demand. The slowdown is more pronounced in Singapore which only posted 2.1 percent this quarter from 9.1 percent in the same period last year. Hong Kong also posted 4.2 percent growth from 6.2 percent in the same quarter last year," Recto said. For this year, government expects growth to hit 4.1 percent.

Shielding the poor

A Standard and Poor's official recently said that the Philippines remains "an island of calm" amid the global financial crisis, but government continues to be on alert.

To soften the impact of the global financial crisis on the poor, President Gloria Arroyo set aside PhP4.5 billion from VAT collections for "pro-poor" employment and livelihood programs.

Standby fund, higher PDIC insurance and OFW contingency plan set up

Malacañang has likewise partnered with the private sector to set up a PhP100 billion "crisis fund" to finance projects that will further protect the country from the global crisis. Under the President's proposal, half of the fund will be raised by government while the other half will be shouldered by the private sector.

Recto, who is also Director-General of the National Economic and Development Authority, clarified that the fund will not be used to rescue ailing financial institutions like what the US did in September. He said the amount will be used as standby fund that will be tapped for future pump-priming projects.

Government also proposed increasing the maximum deposit insurance amount to PhP1 million from PhP250,000 for three years as a pre-emptive measure. If it pushes through, 98.4 percent of all deposit accounts will be covered by insurance, compared with the current level of 95.1 percent.

The Department of Labor and Employment has likewise come up with a contingency plan for OFWs that could be displaced by the crisis. The plan involves helping affected OFWs find alternative livelihood or employment opportunities in the country, as well as assisting those who still wish to work abroad.

More spending and tax cuts

The proposed 2009 budget, if approved, will increase overall spending by 15 percent and outlays in infrastructure by 20 percent.

Under the Comprehensive and Integrated Infrastructure Program for 2008 to 2010, the transport sector has the highest investment share at 38 percent or PhP755 billion out of the PhP2 trillion total investments. In the transport sector, roads and bridges and rail transport, with 44 percent and 39 percent of the pie respectively, comprise the biggest share.

Aside from infrastructure, the big winners will also be social services such as education and health.

On the supply side, government has passed a law that exempts minimum wage earners from the income tax so they can have more to spend on food and education. Corporate income tax rates will also fall from 35 to 30 percent starting 2009 to encourage businesses to expand and create more jobs.

Other reforms

Aside from spending, the absorptive capacity of government agencies will also be increased. The national government will also improve its coordination with local government units to make sure that infrastructure projects go to where they are needed the most. Trade, investment and tourism with other emerging markets, particularly China and the oil-rich Arab economies, will also be expanded.

For the next two years, Recto summarized strategic investments needed to boost growth in HEARTS, meaning Health, Education, Agriculture, Roads/Bridges/Railroads, Technology/Tourism and Security/Shelter/Social Protection/Subsidies, with a focus on R for infrastructure investments.

Taking stock

As the world continues to suffer from a financial contagion, governments around the world are doing everything they can to end the crisis. Aside from that, they are also taking stock of the events of the past year to identify reforms measures that need to be enacted, and make sure that a similar crisis won't happen again in the future.

Thankfully, the Philippines has done its homework and is in a better position to weather the global economic storm. Despite that, government along with other stakeholders remain on alert, and will continue to do so until this crisis finally reaches a decisive end.