

Competition and Investments in the Philippines

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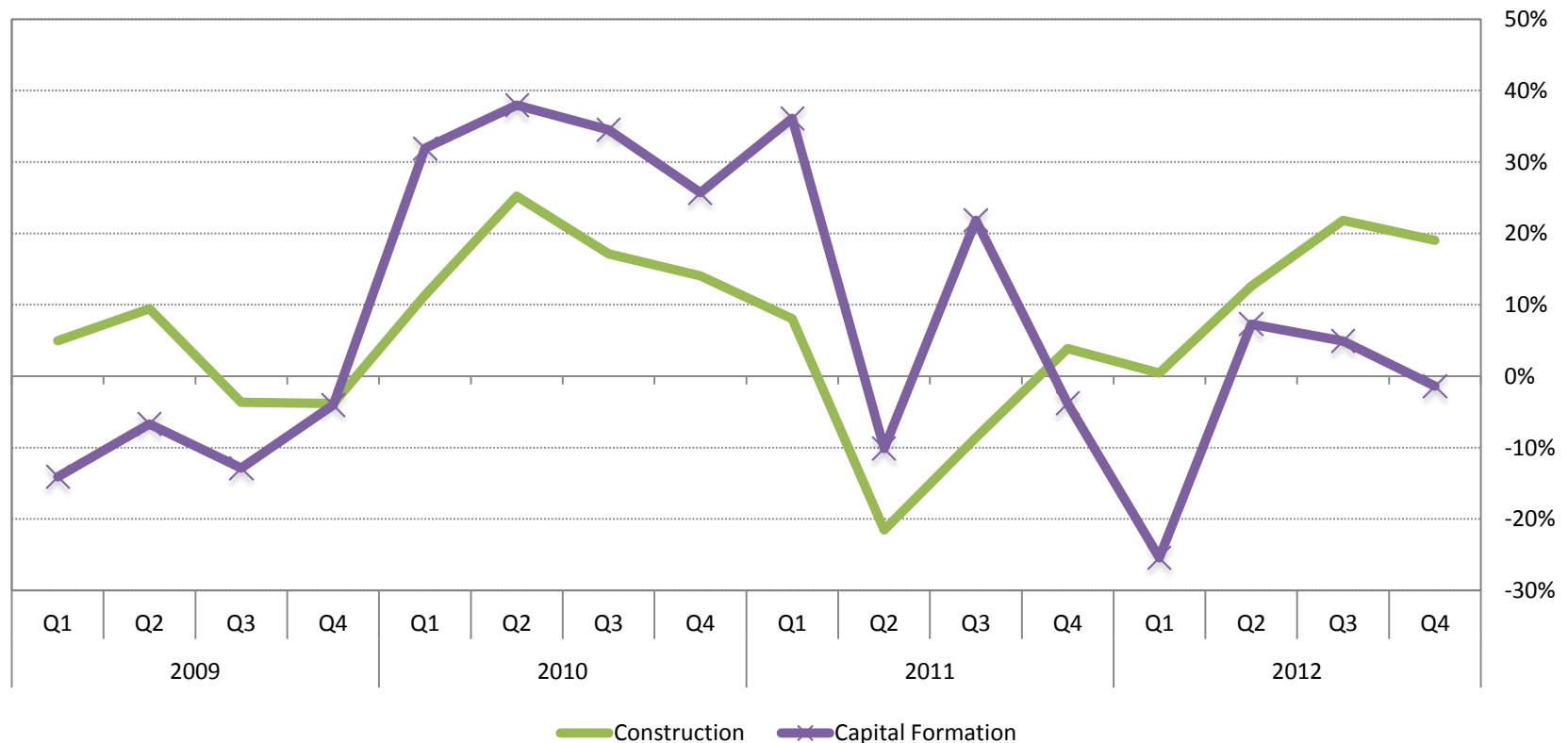
Outline

- Investment in the Philippines
- Why is the investment rate in the Philippines low?
- Is the government sincere in fostering competition?
- Issues on competition policy
- Need for political reforms

Investments in the country remain weak

Anemic investment growth has led to a decline in the investment rate from 20.5% of GDP in 2010 to 19.6% in 2012...

Capital Formation and Construction Gross Value Growth Rates

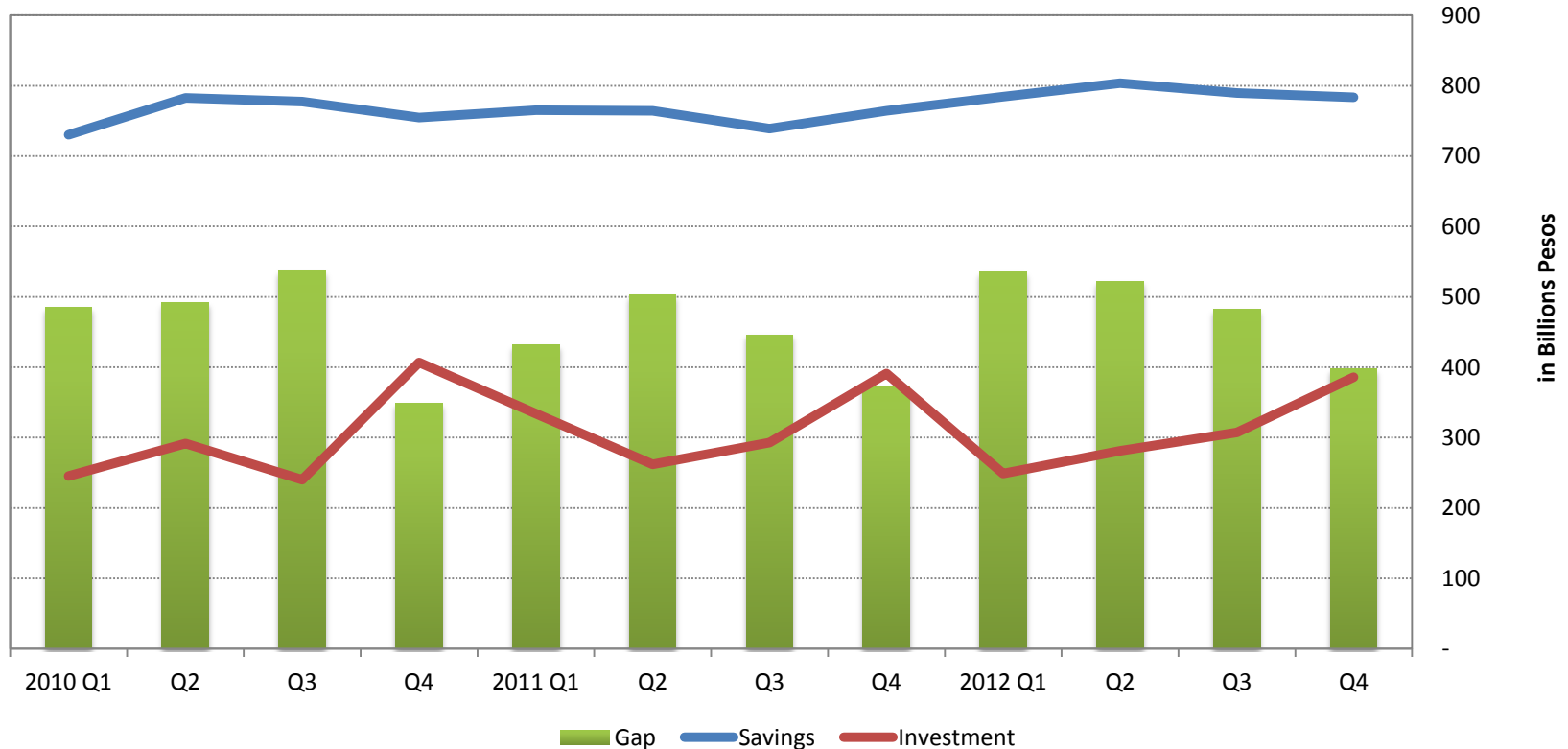


Source: National Statistical Coordination Board

Large savings-investment gap

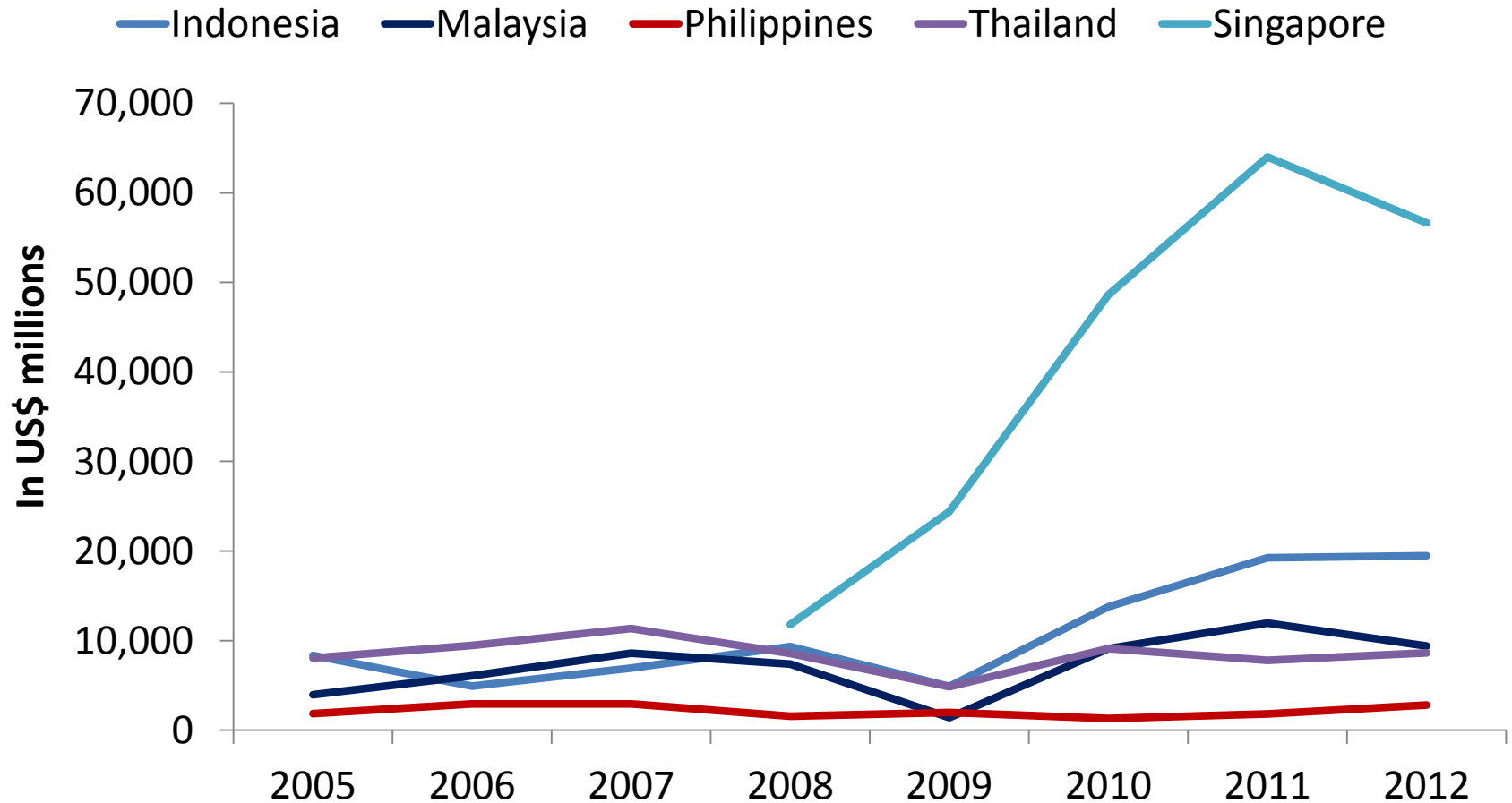
Relatively little investment activity despite the huge amount of liquidity in the economy...

Savings, Investment, and Gap



Source: National Statistical Coordination Board, IDEA Staff computation

Philippine foreign direct investments (FDIs) among lowest in ASEAN



Source: Bangko Sentral ng Pilipinas

Why the low investment rate?

- Bocchi (2008)
 1. Weak fiscal performance
 2. Capital-intensive private sector does not find it convenient to expand investment
 3. BPOs need not invest to enjoy high returns
 4. Low marginal productivity of capital due to:
 - Lack of public investment
 - Elite capture of key industries

Why the low investment rate?

Monopolies and oligopolies:

- hinder tax collection
- raise input costs of downstream and upstream industries (e.g., agriculture, transport, electricity, cement, etc.)
- Example: high rice and food prices push up the cost of living and thereby wages, leading to high labor costs

Why the low investment rate?

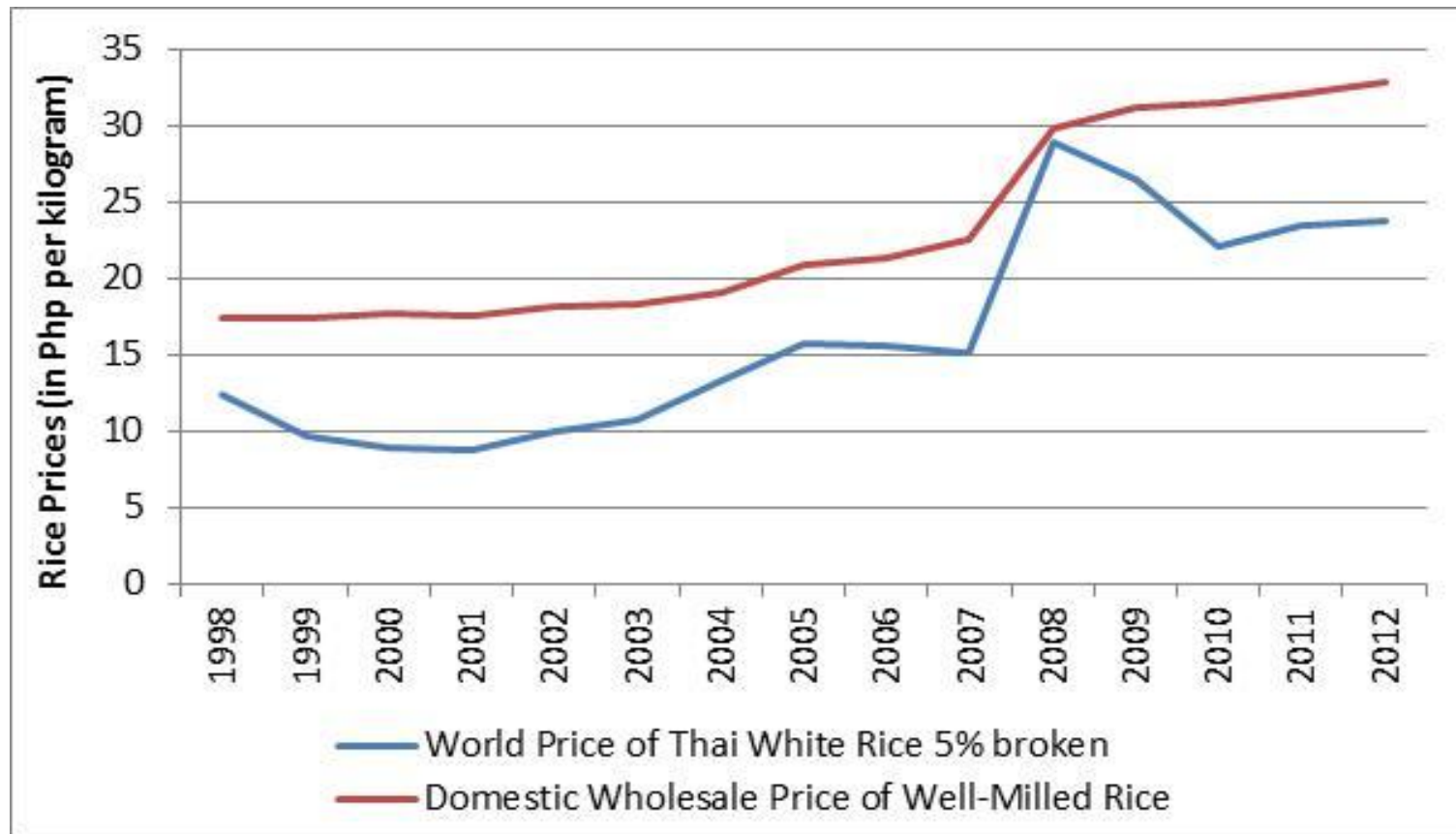
Politically-connected corporate conglomerates:

- protected by favorable rules and regulations; regulatory capture
- enjoy barriers to entry and oligopolistic market power
- sell at a high price products that are critical inputs for both upstream and downstream sectors

Is the government sincere about competition policy?

- Government monopolies: NFA, PAGCOR, PPA, etc.
- NFA monopoly taking huge toll on economy
 - large losses
 - high rice prices
 - less government funding for agri programs
 - according to COA, NFA loses more than Php100 billion in a span of 10 years
- Government refusal to remove constitutional restrictions to foreign investment

Domestic price of rice higher than world price

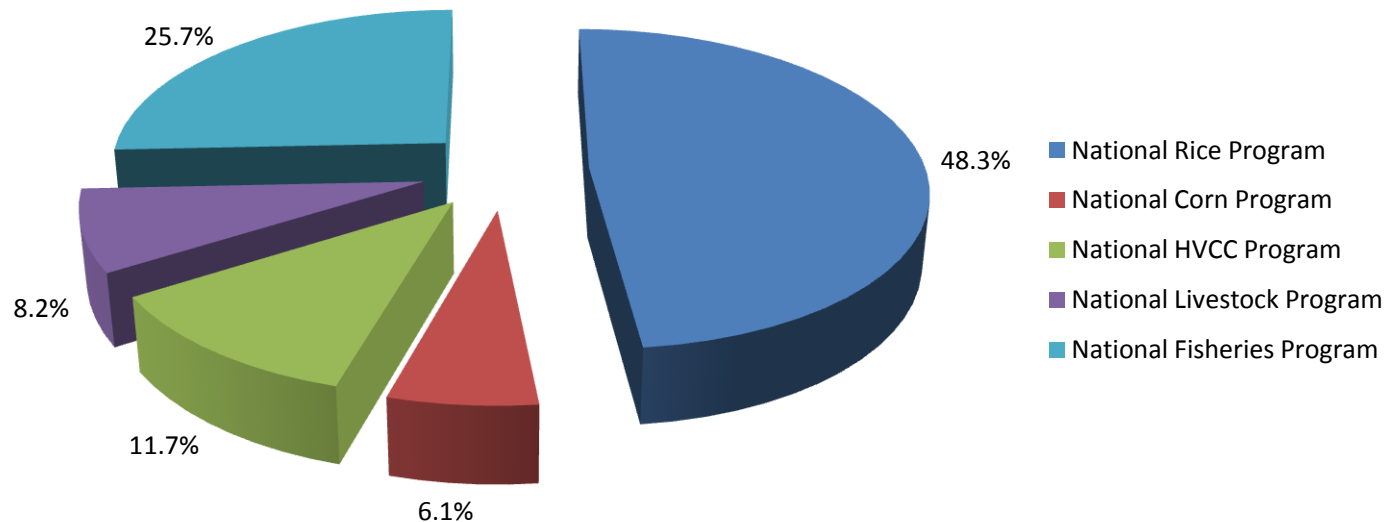


Source: *World Bank and Bureau of Agricultural Statistics*

Skewed budget priorities

Funding for rice dominates the agriculture budget (48.3%) at the expense of other sectors such as high-value crops (11.7%)...

DA Budget Allocation by Major Sectoral Programs



Source: Department of Agriculture, IDEA Staff computation

Issues on competition policy

- Smuggling undermines fair competition
→ value of smuggling activities estimated at around \$20 billion annually
- The agency problem: Will a government anti-monopoly watchdog be another extortion agency?

Before anything else: Political Reforms!

- The Philippines, a weak state:
 - dynasties and political capture
 - political campaigns fuelled by corruption and contributions from vested interests
 - lack of accountable political parties
 - low tax collection
 - politicized bureaucracy
 - corrupt judiciary

Before anything else: Political Reforms

- With a weak state, competition policy could end up ineffective, weakened through regulatory capture or court injunctions; at worst, an instrument of extortion and rent extraction.

Before anything else: Political Reforms!

Instead of a general competition policy measure:

1. Pass and implement specific reforms that foster competition:
 - open skies
 - repeal of Cabotage Law
 - de-monopolizing NFA
 - separation of regulatory and operating functions of PPA

Before anything else: Political Reforms!

2. Constitutional change

→ open up key sectors of the economy held by the oligarchy to foreign competition

3. Political reforms first

→ campaign finance reform and party development act

→ build the political foundations of competition policy

Before anything else: Political Reforms!

- → Bocchi: Adopt a competitive exchange rate policy, then build a pro-competition coalition among exporters
- Overall message: don't leave out political change from competition policy