The Philippine Review of Economics
Vol. LII No. 2, December 2015 pp. 22-37

American private direct investment in the Philippines after independence

Gerardo P. Sicat

The Philippines has lagged behind East and Southeast Asian economic growth successes in the course of contemporary times. A historical perspective is presented to explain this lag. When the country entered the definite road to independence from American rule in 1934, it adopted a political Constitution that limited foreign capital to a minority role in three industries – land, public utilities, and the exploitation of natural resources. During the colonial period and after political independence in 1946, American foreign direct investment in the country was dominant and large. This continued after independence as US citizens were granted equal rights of Filipinos and American businesses received war damage payments to rehabilitate their investments. This was further helped by bilateral preferential trade with the United States during twenty-eight years of economic adjustment. In actual practice, the restrictive provisions in the Constitution invited many virulent forms of nationalistic economic policies of exclusions of foreigners in other lines of economic activity and led to inward-looking economic development policies. These policies discouraged American foreign direct investments causing disinvestment in key areas. The restrictive economic provisions in the Constitution continue to this day even as the economy is opening more to world markets.

JEL classification: P45, D9
Keywords: Philippine economic history and development, foreign direct investment, American foreign direct investment, Philippine-American economic relations

In Hal Hill's work on the Philippine economy, he has called attention to the following conundrum: Why does the Philippines, despite its many good attributes, lag behind in economic development when compared to East Asian high economic achievers?[1] In this essay, I hark back to what I have called the "original sin", the biggest long-term mistake in our nation-building: the restrictive economic provisions in the Philippine Constitution.[2]

It is not as much a mystery. When we take a historical perspective, we link developments to the question of why American and other foreign direct investments have not come in sufficient volume to help push the growth of industry, incomes, employment and productivity. Those restrictive provisions led to protective and inward-looking policies that characterized subsequent policies promoting industrialization and economic development. In that respect, they served as a lever for bad policies that moved the country in many wrong directions.

In turn, because those provisions further strengthened the vested interest in the continuation of these policies, their reform could not take hold. Today, the problem of amending these provisions in the Constitution remains as a principal problem hindering still future progress.

Before the Second World War, United States private industrial capital in the Philippines was dominant. The public social and economic infrastructure built by the colonial administration was extensive and growing. The country was the envy of early economic development in East Asia among colonized economies. When the grant of full political independence in 1946 happened immediately in the aftermath of a ruinous war of occupation by Japan, the country was economically devastated. However, the rehabilitation from that devastation was relatively quick.

Total US direct investments[3] in the world at yearend in 2012 is estimated at US$4.45 trillion. Three-quarters (74 percent) of this total is located in highly advanced countries. Only 14 percent of American direct investments is located in Asia, principally also in the developed countries of the region. In this context, direct investments to the Philippines were hardly a speck in the numbers. A recent work summarizing data on flows of foreign direct investments (including US direct investments) going to Southeast Asian countries from 1970 to 2011 reports that Singapore, Thailand, Indonesia, and Malaysia have been the largest receivers of foreign direct investments. It also observes that the Philippines has consistently received a relatively small amount of these investment flows over the same period.[4]

To those drawn into the discussion on investment and economic policy in the Philippines, the relative insignificance of foreign direct investment numbers is all too familiar.

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[1] Hal Hill expounded on this point in seminars he delivered at the University of the Philippines School of Economics. His work on the Philippines is sometimes indistinguishable with that of Arsenio Balisacan because they have worked together in major pieces.

[2] The author tried to elaborate on this point in several short essays found in Sicat [2013:186-187]. In a presentation on the topic of restrictive economic provisions on foreign capital before an annual meeting of the Philippine Economic Society circa 2004, he called these provisions the " original sin" of development policy.

[3] See Jackson [2013].

[4] See Sjöholm [2013].

1. The triad of US-Philippine relations

The Philippines was one of the most devastated economies at the end of World War II. War confiscations and conscriptions, market disruptions, inflationary spiral especially towards the closing months, destruction due to the battle for liberation—all these led to output and physical capital losses that were substantial. The total output of the country at the end of the war in 1945, was reduced to 30 percent of the level of the pre-war GDP.[5]

Before the start of the World War II in the Pacific, the preparations for Philippine independence were in full swing. In 1934, the US Congress passed the law that spelled the road toward full political independence. A year later, the political Constitution (which had built into it the restrictive economic provisions on foreign investments) that was crafted by an elected national convention composed of Filipino leaders was approved by the American president as required. Hence, in 1936, the ten-year transitional Philippine Commonwealth took office. The Commonwealth stage was a semi-independent political status under the American dominion before the grant of full independence on July 4, 1946 as the Republic of the Philippines. This path toward independence was interrupted by a destructive war of occupation by Japan covering four years.

Economic rehabilitation from the war proceeded rapidly during the next decade after independence, starting in 1945 when Japan's occupation ended. Aside from a sustained volume of American military expenditures early in this period, three major actions propped up the economy. Such measures would involve deep economic entanglements of the Philippines with its former colonial ruler. These actions—the triad of relations—were to influence future events strongly.

First was a trade and economic adjustment to wean the country from its dependence on the US economy, an outcome of the long American occupation of the country. The US Congress enacted the Philippine Trade Act of 1946 (US Public Law 371, 79th Congress) to amend its trade and tariff policies to accommodate the new parameters that would be contained in the commercial trade agreement with its former colony. The law granted the Philippines a period of declining trade preferences and fixed quotas on certain products like sugar, coconut oil, and other major products that would end in 1973. In the early discussions of this adjustment period before the war, the proposed adjustment period was shorter, twenty years being the longest. The war destruction in part led to this extension of the period of adjustment to twenty-eight years.

Second was the payment of war damage transfers[6] to assist in speeding up the rehabilitation of the domestic economy. The war damage payments were embedded

[5] See Sicat [2015:191-204].

[6] The author uses the word "transfers" in contrast to war damage payments as reparations, which connotes monetary retribution as payment made by a defeated party after the war, as in the Japanese reparations. The US considered the payment of war damage claims (which had to be formally declared first) as assistance to help the recovery effort, more in the context of the Marshall Plan for Europe after the war.

in the law called the Philippine Rehabilitation Act (Public Law 370, 79th Congress), which contained the war damage payments and the mechanisms for delivering the program. This companion law on Philippine independence appropriated a large sum of money—US$520 million—in two parts: US$120 million to help finance and restore public buildings, roads, and social infrastructure; and US$400 million to pay war damage compensation to assist in the rehabilitation of the economy that heavily suffered during the war.

Finally, the American government required that before these new provisions were to take effect, the new Philippine republic had to give Americans the same rights as Filipino citizens. This meant in polite treaty language, "national treatment", a common feature of commercial agreements between states. Essentially, this meant protection from confiscatory national policies and guarantee from discriminatory policies. The restrictive provisions in fact were directed at foreign control of the economy, which was dominated by American investments at the time. President Franklin Delano Roosevelt approved the Philippine Constitution as prelude to the process leading to Philippine independence early in his first term in office at the bottom of the Great Depression in 1934. Faced with more pressing economic issues at home, he approved the restrictive provisions in the Philippine Constitution. It therefore would fall on Harry S. Truman (the successor to the presidency upon Roosevelt's death in 1944) to exact parity rights as a condition to protect American investor interests after Philippine independence. For the Philippines to yield to this demand, a constitutional amendment had to be secured by plebiscite. The plebiscite was made and the government of Manuel A. Roxas, the first president of the Republic, triumphed in his sponsorship of the yes vote.[7]

The 1935 Constitution limited foreign capital participation in three economic markets—utilities, land, and exploitation of natural resources—to a maximum of 40 percent, meaning that such industries must have 60 percent Filipino control of the capital equity. This was a key intent of the "nationalistic" provisions of the Philippine Constitution when it was enacted in 1935 in reference to corporate activities. Had the basic law of the land simply remained silent on this issue, it would still have been possible to enact nationalistic provisions, but they would not need to be cast in solid stone to accommodate changes in national moods and perception.

Thus, a package of three important economic actions was needed before the road toward full economic rehabilitation and adjustment of the newly independent republic could proceed. To nationalistic Filipino leaders, the grant of equal rights to Americans was economic blackmail. To the Americans, these actions were pragmatic elements to help a former colony recover as well as to protect the rights of its citizens who continued to have vital interest in the Philippines. To the incumbent, newly elected leaders of the Philippine government (led by

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[7] The parity rights amendment was held on March 11, 1947 with 79 percent of voters casting approval.

President Manuel A. Roxas, who was then the newly inaugurated first president of the republic), this was a realistic compromise to ease the way for the newly independent country.

Another element of relations with the US at the inception of the Philippine republic was the military bases agreement. This could be considered the fourth element of the post-independence conditions with the former colonial master. The US was given a military foothold for 99 years to operate military bases in the country. Two major military bases were principally included in this agreement, the Clark Air Base and the Subic Naval Base, in addition to a number of military installations that were installed during the long American colonial period.

From an economic viewpoint, this agreement helped to provide for the country an important American military shield. A steady flow of earnings of foreign exchange resulted from US military operational spending in the bases throughout the post-war period when the military bases were stationed in the country. From a defense standpoint, the newly independent country was kept from undertaking a heavy domestic expenditure on defense matters. Defense expenditure was a major expense among newly independent countries.

2. The war damage payments by citizenship of recipients

The war damage payments made to American citizens give a clue to the amount of American private capital in the Philippines. The losses were therefore compensated at the original value of acquisition. When the payments were made, the replacement cost of capital was already three times the cost of capital before 1940. They were disbursed in pesos at the fixed exchange rate of 2 pesos to a dollar.

About two-thirds of the war damage compensation was to pay war damage to the private sector on the basis of claims of war damage filed before the Joint Philippine-American War Damage Commission[8] (henceforth referred to as the Commission). The first job of the Commission was to pay as much of the small claims first. Approximately one million claimants, out of a total of 1.25 million claimants, filed claims for US$500 or less. According to the final report[9] of the Commission, these claimants were paid a total of US$131,766,435 as of end of December 1950, or, converting the amount at the 2 pesos to one dollar fixed exchange rate, ₱263,532,870. The total amount of these small payments amounted to 32.9 percent of the US$400 million that was appropriated for private payments. It was safe to assume that all the small payments were received by Filipino citizens.

[8] The Commission had three members: two Americans and a Filipino, with one of the American commissioners serving as chairman. The activities of the Commission and their actions with respect to implementing its mandate are explained in the main study.

[9] See Philippine War Damage Commission [1951].

The question of how much war damage compensation was received by Americans meant that that the citizenship of the recipients had to be known. The law on the war damage payment was only to qualified American and Filipino citizens and citizens of other nations that were not enemies, to include also corporations owned by such citizens. The report of awards did not track the citizenship of the awardees. In order to make an estimate of awards by citizenship, an effort is made to classify the citizens that filed claims and who were issued approvals for those claims.

The task was to classify by citizenship of awardees of the "large" payments, that is, those exceeding US$500 and above. To get a distribution by citizenship of all these awards, I had to tag each of the recipients—individuals or enterprises—with the appropriate citizenship: Filipino, American, Chinese, and the like. The greatest area of doubt was in determining whether some recipients were Filipino or American citizens.

The individual recipients of war damage awards could be fairly identified by their names, although this was not fully accurate. The names of business establishments were another matter. Most of the establishments were corporations. From the names of these recipients, I tried to form some basis for the citizenships by identifying each recipient with a citizenship label. The classification by citizenship was essentially educated guesswork to determine overall magnitudes that yielded approximate orders of magnitudes.

I labeled familiar Filipino names "Filipino" by citizenship. American names, and those I associate with American enterprises, I labeled "American". Chinese names were easy to identify when they used proper names. Uncertainty was greatest in identifying the citizenship of enterprises, for which I could only add the label "American or Filipino". These recipients were separated from those tagged more definitely as either American or Filipino. In all these labeling efforts, acceptable errors were likely to be made.

The corporate names of the firms were more challenging. There was little to go by that could give the citizenship of the ownership of corporate enterprises. Sometimes the corporate names gave a clue. This was clear enough for some businesses, as when the corporate names were emblazoned with Chinese names or titles. Most of the time, an educated guess sufficed, for instance, from studies listing industries and establishments[10], from personal and imperfect memory growing older, and from introspection on the business of the corporation and the likely citizenship of the owners.

[10] The study of Kunio Yoshihara [1985] on Philippine industrialization used some names of Chinese, American, and Filipino enterprises during the 1960s. Many of these firms existed before the war. A more assiduous study would have been to use an establishment set of names from the Securities and Exchange Commission in an earlier period or some listing from the Bureau of Commerce and Industry. I had no resources for hiring research assistants, and neither did I have the luxury of time to study this aspect of the problem. In any case, relative accuracy, not definite accuracy, was what I was after.

American investments were heavily in sugar centrals, mining, logging and timber exploitation; in public utilities such as power generation and distribution, transportation, both land, sea and air; in domestic and international trading; in manufacturing operations that processed agricultural products; in construction and metallic fabrication; and in banking and finance. They were typically the larger industrial enterprises operating in the country, although there were also some Filipino-owned industrial enterprises in similar fields.

There were many instances when it was difficult to tag the enterprise definitely, in which case they were identified as "Filipino *or* American". Exact judgment depended on subjective judgment, a dubious but necessary method in order to establish a reasonable measure of allocation in the absence of total information. For a norm, that probability could be 50-50. An optimistic judgment that the group of "American or Filipino" recipients thus tagged contained more Americans represents "60 percent likelihood of being American". A less optimistic assessment on the opposite side could be one in which 60 percent likelihood of being Filipino". I use these subjective judgments in providing a "high" and "low" estimate of American citizen recipients.

Finally, there were awardees whose citizenship did not belong to the three above-mentioned. These awards were made principally to religious institutions that received war damage compensation. I labeled most of these "Other" citizens. Catholic Church institutions could have been grouped under "Filipino", but they fall under the hierarchic control of the Vatican. Therefore, all the war damage payments to archdioceses, bishoprics, and foreign Catholic religious institutions that received awards were classified as "Other citizens".

3. Summary of war damage payments by citizenship

Table 1 presents a comprehensive table. Part A is the raw table showing the citizenships of the large recipients of war damage as approved by the Joint Philippine-American Commission. The citizenships of recipients separated those grouped under American, Filipino, "American *or* Filipino", Chinese, and Other.

Part B of the table uses the "high" scenario in which American citizens received 47 percent of the large payments made by the US government. In this estimate, Filipinos received 42 percent. These numbers are seen in the last column under Part B. The ratio of awards to the amount of claims (seen in the second to last column) is slightly higher for American awardees, probably not out of bias but by virtue of the greater reliability of claims made by larger claimants—corporations with much better record keeping.

Part C of the table shows the "low" scenario result. From the viewpoint of the immediate impact on the economic rehabilitation efforts, the issue of who received more of the war damage payments between Filipino and American citizens did not matter as much. However, this exercise is helpful in identifying the amount of private American capital in place in the country before the war.

There were no reliable estimates of American private investments that I could find before the war. An estimate due to the American Chamber of Commerce in the Philippines was ₱537 million, of which ₱200 million was in sugar, coconut, and abaca plantations, mining, and lumber operations. (In US currency, this was US$268 million at the fixed rate of two pesos to a dollar.[11]) Another estimate of US$160 million in direct investments and US$36 million held in Philippine bonds and securities (or nearly US$200 million) was due to a presentation made by the US National Foreign Trade Association president before a hearing on Philippine independence issues.[12] These were very sizable magnitudes of investment in an economy that was undergoing steady economic development before the war.

TABLE 1. Summary of US war damage payments ("large awards"), by citizenship of awardees

Citizenship of awardees	Value of claims submitted in thousand 1940 pesos	Amount of war damage approved in thousand 1940 pesos	Ratio of award to claims	Percentage distribution of awards to total
A. Raw estimates				
Filipino	203.02	87.41	43.1%	30.2%
American	166.46	85.00	51.1%	29.4%
American or Filipino ("AF")	161.77	85.90	53.1%	29.7%
Chinese	26.87	7.67	28.5%	2.6%
Others	50.50	203.02	46.7%	8.1%
TOTAL	608.63	289.56	47.6%	100.0%
B. High estimates (Americans 60% of "AF")				
Filipino	267.73	121.77	45.5%	42.1%
American	263.53	136.54	51.8%	47.2%
Chinese	26.87	7.67	28.5%	2.6%
Others	50.50	23.59	46.7%	8.1%
TOTAL	608.63	289.56	47.6%	100.0%
C. Low estimates (Americas 40% of "AF")				
Filipino	300.08	138.95	46.3%	48.0%
American	231.17	119.36	51.6%	41.2%
Chinese	26.87	7.67	28.5%	2.6%
Others	50.50	23.59	46.7%	8.1%
TOTAL	608.63	289.56	47.6%	100.0%
D. Estimated high estimates calibrated to 2015 US Dollar (based on Part B estimates)				
Filipino	4,015.92	1,826.52	2,007.96	913.26
American	3,952.95	2,048.05	1,976.47	1,024.02
Chinese	403.08	115.00	201.54	57.50
Others	757.53	353.84	378.77	176.92
TOTAL	9,129.48	4,343.40	4,564.74	2,171.70

Source: From basic table of war damage payments. G.P. Sicat, "US War Damage Payments Income Flows After Independence and Philippine Economic Development," UP School of Economics, forthcoming, 2016.

[11] See Hartendorp [1953].

[12] See United States [1938].

My objective in presenting these estimates is to show that for the economic rehabilitation during the early years of the Philippine republic, a sizable amount of American capital was returned to their proper owners. Since the war damage payments were linked with the rehabilitation of the damaged economic establishments, this return of American capital also signified the continuing commitment to the future of the Philippine economy. The war damage payments also helped to identify orders of magnitude that had a direct connection to the amount of capital in place before the war.

The Commission in its final report indicated that replacement cost of damaged capital at the time of payment was three times more than before the war, even though the approved payments represented only about 52.5 percent of the submitted claims. When replacement cost was therefore taken into account, the recipients effectively received only around 20 percent of the value of replacement costs. The award of war damage payments could therefore act as supplying merely a significant stimulant for the rehabilitation process. On this point, the report of the commission said: "They permitted many industries and other activities to attract new capital or obtain credit to start rebuilding the industrial commercial, and other agricultural enterprises which provide employment and otherwise benefit the Philippine economy."[13] Some slippage from this objective or procedure might have occurred, but most of the payments of war damage were made after proof of rehabilitation work was made available.

In other words, although the war damage payment might have constituted a fifth of the total investment requirement to rehabilitate an enterprise, in effect it performed a multiplier impact on the rehabilitation effort. Such an amount of new payments would have implied an expenditure multiplier close to 5, but it surely was much less since the payments would have triggered a high bill of imports of materials and equipment not available in the domestic economy. The country's productive capacity had been rendered very low due to the ravaged productive capacity after the war.

Finally, a point to be made here is that the amount of money transferred to private pockets at that critical time was very significant in relative value even when viewed today. Using the price multiplier for the value of the US dollar in 1940 compared to the much inflated 2015 US dollar, here are some results.[14] The US$520 million valued at the 1940 US dollar (which was allotted for public and private war damage) is roughly the equivalent of US$7.8 billion in 2015 dollars.

[13] See Philippine War Damage Commission [1951]. The report further stressed that "before second and final payments were made on claims for which combined payments would amount to US$25,000 or more, the Commission … communicated with the claimants to make certain that the first payments had been expended in accordance with their sworn statements and that, second payments would also be used for rehabilitation."

[14] I use an inflator-multiplier of 15 to compare the pre-war US$ to the current US$ for 2015, taking into account the changes in prices in 1940 to the present in the Philippines. In the paper calculating the war damage from the Japanese occupation (see footnote 6), I used the same inflator. In this context, these calculations are relatively conservative.

Since the amount was converted at the fixed exchange rate of 2 pesos to one dollar, the equivalent of this sum in 1940 Philippine pesos was ₱15.6 billion. The amount of US$400 million which was appropriated for private war damage compensation, using the same approximations, meant US$6 billion in 2015 US dollars. In the peso values of 1940, this amounted to ₱12 billion. (A proper adjustment would of course also be reckoned in the much depreciated pesos of 2015, which I do not show.) By whatever measures, these numbers are very significant, especially as they were made for a newly independent country with a population size of 19 million. (In 2015, the Philippine population is nearing 100 million.)

Part D of Table 1 shows the same calculations for the amounts of payments made by citizenship of the awardees.[15] Following the discussion for the "high" case estimates of American awardees, we specifically track the amounts paid (shown in last column of Part D). American citizens received approximately US$1,024 million, or around US$1 billion in US dollar values of 2015. The total amount of payments for all awardees was US$2.171 billion measured in 2015 US dollars. (The peso values of the awards that are calibrated to 2015 US dollars but are converted at the 2 to 1 dollar exchange rate of the 1940 pesos are shown in column 3 of Part D.)

4. Three reasons

From the viewpoint of the newly independent nation, the trade adjustment of twenty-eight years brought about a stable relationship in trade and economic relations with the strongest economy in the world at an opportune time of global growth after World War II. Further, parity rights, which gave Americans the same opportunities as Filipinos, promised to continue attracting American investments. At the same time, the extraordinary war damage payments provided new income flows essential for rehabilitation. In particular, as it pertained to American investments, the income flows awarded to Americans were linked to the rehabilitation of their damaged businesses in the country.

This question then arises: Why has American capital not come to the country in droves after the war and during the long interim period to the end of special relations in 1973? Three reasons come to mind why this has transpired:

- First, the restrictive provisions in the Constitution abetted other policies that further relegated the role of foreign capital in other parts of the economy, thereby rendering the development process more difficult and perilous;
- Second, the evolution of American firms in the country reacted to the time-bound adjustment process more as a signal to divest rather than to be more fully engaged in the economy; and

[15] Since I am interested only in understanding the orders of magnitudes for the war damage payments then, I simply return to the 1940 fixed exchange rate of the US$ to the peso. The average exchange rate for the pesos to the dollar in 2015 is ₱46 per US$1. The contemporary pesos would be very much depreciated.

- Third, inward-looking development strategies were implemented by industrialization efforts based on import substitution. To implement it the government undertook nationalist policies that equated promotion of industry with the exclusion of foreign economic participation.

4.1. Restrictive policies

The restrictive economic provisions were designed to spell out the boundaries of foreign investment participation in certain economic sectors, implying that those not so mentioned were to welcome foreign capital. In its place, the legal language of restrictive provisions provoked measures of economic nationalism that encouraged exclusion or limited participation rather than suggest the attraction of foreign capital to speed up development in the rest of the economy. In practice therefore, the provisions incited other restrictive economic policies.

A wider network of economic policies limiting foreign investments in other sectors ensued during the early years of political independence. Commercial banking was closed to foreign participation, except for those already allowed before. The licenses for new banks were issued only to Filipino capital even under low capitalization requirements. For many years until the 1970s, no new foreign banks were allowed to enter the economy, except the four foreign banks that were in operation at the time of independence. It would take the 1990s, when more openness to the participation of foreign banks in the country would be allowed.

When import and foreign exchange controls were instituted in 1949, the allocation decision became one of administrative selection rather than market solution.[16] In an environment of economic controls, selectivity implied that resource allocation happened through regulation and administration rather than through the market. In this climate of policy, industrial and agricultural projects were the result of selection criteria in which nationality was a critical element in the choice.

A further consequence of the restrictive economic provisions was that they encouraged policies that were discriminatory over foreign economic interests. In 1955, retail trade nationalization was passed by Congress. The new law placed restrictions that excluded foreigners from the retail distribution sector of the economy. The measure was designed to encourage Filipino retailers to take over the small *sari-sari* corner store from the Chinese merchants. But the retail distribution network extended to big stores too, and this led to the exclusion of foreigners from the retail distribution industry.

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[16] See Golay [1961] for a longer discussion of nationalistic measures during the first two decades of independence.

The rhetoric of industrial and economic policy in the 1950s was "Filipino First", echoing the demands of those who wanted more protection for Filipino enterprises and the exclusion of foreigners from the nation's economic development. Though such rhetoric was removed from the official language in the investment promotion programs, the industrial and investment priority schemes for new industrial projects emphasized that priority areas of investments were reserved for Filipino enterprises under the Board of Investment. Only industries classified as "pioneer" were listed as investment areas where foreign direct investments would be allowed up to 100 percent equity from foreign enterprises. In many East Asian countries, especially at the beginning of their industrial promotion efforts, businesses that were 100 percent owned by foreigners were typically allowed to receive government incentives in order to attract new foreign capital.

4.2. The divestment of American firms

Before the war, American investments were strong across the spectrum of economic sectors. Specifically, they were dominant in agriculture (sugar, coconut processing, abaca, and other plantation agriculture), natural resources extraction, especially mining and forestry, and in public utilities. Targeted constitutionally by the restrictions on foreign ownership, the grant of parity rights meant that they could remain in American hands even after independence. However, the future prospects for these investments in spite of parity rights became bleak in the face of nationalistic regulations and policies.

The strength of the economic rehabilitation efforts after the war emanated partly from the participation of American companies that were awarded war damage payments. Agricultural enterprises, especially in sugar and coconut industries, were able to recover easily and enabled export earnings to begin to recover. These were big contributors to the export sector. The same story applied to the mining companies that resumed their operations after the war. The re-entry of mining firms into the production picture helped the mining industry recover.

The public utilities were among the biggest recipients of war damage payments and their restoration of service was quick. Meralco—the electricity retail distribution monopoly in the Manila area—was one of the biggest recipients of war damage. The company was able to undertake resumption of service and to re-expand destroyed facilities. The telephone and telecommunications sector re-established services. These utilities were most exposed to dealings with the local regulators.

By the late 1960s, American companies in the country began to feel the pinch. Nationalistic economic policies and regulations foreshadowed future difficulties for them, and so it was better to move ahead of 1974. Even if parity rights gave American investors some comfort as they faced the future, it was a kind of restless comfort. As the period of special economic relations was coming to a close at the historical time line of 1974, the end of parity rights was written on the wall. Eventually, the public utilities saw the future as bleak for full control of management, and they sold to partners toward the years before the end of parity rights.

During this period then, the incentive to reinvest and to expand existing capacities began to weaken as more restrictive economic measures were added to those already in place. Thus, the stream of divestments began. Some American investors sold the land they owned to other Filipinos. Companies that had a desire to remain in business accepted the implications on land policies. They created a land company that was owned by their workers' provident funds to which they sold the land. In turn, the land company that was owned by at least 60 percent by Filipinos leased back the land for the company's use. This roundabout method of dealing with the land question made investors essentially temporarily satisfied, but it added complications to the company's structure and, hence, its decision making. Even this solution did not please those that wanted complete divestiture. In the latter case, the local partners often had the inside track and benefited handily. The lack of a strong market to buy up these assets meant that the local partners had the upper hand and bought the assets at favorable prices.

Some American investments found business opportunities in the domestic economy, and they ventured further into purely local markets. New investments took place behind the logic of import substitution, but they reflected small-scale commitments of new capital since the domestic market was limited. Formerly imported goods had better economic logic being assembled for the domestic market so as not to lose the market. This was the case for many industrial products that thrived in food, cosmetics, pharmaceuticals, and energy refining, where the buyers were home consumers. The end of parity rights was not a problem for these industries for they had a comfortable position participating in the domestic market. The same domestic protection given to local industries was accorded these investments. American companies that had an early foothold before with imports of these goods established their manufacturing and processing plants in order to keep their domestic market share. This industrial foothold anticipated a future in the country's growing market. But these industries were relatively small in themselves because they simply undertook production for the local market like most of the industries promoted by the protectionist industrial policies.

Plantation agriculture in old lines of agriculture continued in part because of the early economic foundation laid by export industries destined for the American market. This was the case for the quota-based industries, such as sugar and the traditional coconut-based processing industries, and in the case of the pineapple industries, which had natural markets in other countries as well. The banana industry was such a case, with markets intended for third countries like Japan. However, the banana industry—which started originally as a proposal to set up an investment by the United Fruit company—got shot down. It was resuscitated when domestic interests took over production while they allowed marketing functions to the American investors. Dole Plantation got an earlier foothold, with large land areas made available through government lease at the beginning. Later expansions led to innovations in contract farming with local landowners. What has thrived well was the profitable contract farming arrangements with local planters, which involves other technical and other production tie-ups and marketing agreements. In general, because of land reform issues which limited future land use to smaller plots of land, even plantation agriculture became almost a closed field for investment expansion.

It was only after the late 1970s that more enthusiastic American capital began locating in new investment areas. These new investments arose from the globalization of the international division of labor in the electronics industry. Philippine entry into this lucrative opening for foreign direct investments in general was the establishment of export processing zones. These export processing zones enabled industrial locators to speed up export or import processing, the acquisition of land for factories, the isolation from much bureaucratic red tape and control measures that are often associated with tight, inward-looking policies. By the mid-1990s, the investment attraction framework within export processing zones accelerated further and, finally, the Philippines is able to again attract new flows of foreign direct investments, including American capital. In short, it opened up industry for the participation of a wider range of foreign direct investments without being hampered by the restrictive economic policies of an inward-looking industrial framework. In this, American capital had found a way to come back more strongly.

Despite the improved capacity to attract foreign capital-engaged electronic parts assembly, the country lost its competitiveness in expanding the garment-making industries. In this case, the economic policies that continued to hamper the growth of this industry were tied up with labor market policies, especially those linked with minimum wage setting. American investment in garment making was a strong presence very early during independence and should have expanded more. But the import substituting framework for industrial growth favored the highly protected textile industries and disfavored the importation of raw materials from the world for the garment makers. And then, rising domestic wages for formal employment in organized manufacturing further edged out industries engaged in exports that were heavily labor-intensive.

4.3. Inward-looking policies

The inward-looking approach promoted measures to replace imported goods rather than an industrialization that was based on comparative advantage. This program was a hollow strategy. Most of the promoted industries using domestic capital were mainly import-dependent operations that assembled imported raw material inputs. With little domestic feedback on production and lacking scale in production size, these new industries simply produced profits for their investors while raising the cost of the products to Filipino consumers. The opportunities that were built on tariff protection and other forms of subsidies to domestic industrialists also worked for import-substituting American investors.

The protectionist industrial policies emanated from the early import and exchange controls and by tariff protection. These policies created a large group of domestic industries that depended mainly on protection. As a result, future efforts to reform the framework to allow for amendments that opened the industries to more competition encountered strong opposition.

The special trade preferences, for instance, heightened the economic isolation of the country in international trade. The special preferences made it difficult for the country to multilateralize its approach to international economic issues. The special concessions to trade under the US-Philippine bilateral tariff preferences and quotas for specific industries (sugar and coconut industries) created the excuse to resist multilateral trade policies. Thus, the country did not join the General Agreement of Tariffs and Trade.[17] Industries that benefited from tariff preferences were more concerned about enjoying those preferences. Of course, the General Agreement of Tariffs and Trade was for multilateral trade and not bilateral preferential trade. And it would be many decades later, in 1994, at the birth of the World Trade Organization, the successor to the General Agreement of Tariffs and Trade, before it could join fully the world's trade rules.

In one sense, the Philippines was uniquely blessed with special preferential treatment with the United States for that market represented an infinite potential for economic growth, if the trade opportunities were fully exploited for domestic reasons. Under the revised Laurel-Langley Agreement, the terms of tariff preferences were even better than those originally under the original agreement. But the import-substitution climate of domestic industrial protection and extreme nationalistic measures influenced by the original restrictive economic provisions of the Constitution swamped all reasons for exploiting an open trading system.

Without the blessings of a similar preferential trade agreement with the United States, the economies of South Korea, Taiwan, Hong Kong, and Singapore (and later East Asian countries)—by simply espousing a more open foreign direct investment policy for themselves—were able to reap major benefits by attracting heavily American direct investments which manufactured labor-intensive consumer products for the US markets. Because of the unlimited growth prospects that were opened for their exports to the rich American market, these countries realized their industrial revolutions much sooner and more quickly than the Philippines.

University of the Philippines School of Economics

[17] The multilateralization of trade commitments would only come about with the entry of the Philippines into the World Trade Organization. The Philippines had participated in the negotiation of the later rounds of multilateral tariff negotiations, beginning with the Tokyo Round and the Uruguay Round that ultimately led to the formation of the World Trade Organization in 1994.

The author is Professor Emeritus at the University of the Philippines School of Economics. This paper is part of his longer study of the US war damage payments to the newly independent Republic of the Philippines after World War II. Collection of data arose out of an unplanned research effort in 2003 when the author found the individual records involving the recipients of war damage payments in the official minutes of meetings of the Joint Philippine-US War Damage Commission that were lodged in the US National Archives in Washington D.C. The festschrift for Hal Hill was the immediate incentive for him to restart the study. The author uses segments from this study to restate an old theme concerning the missed opportunities arising out of Philippine-US economic relations.

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