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**The Next President Could Be an Economist:
Or Gloria Macapagal as an Economist**

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ABSTRACT

Vice President Gloria Macapagal will become President if Joseph Estrada is removed from office or he resigns as a result of his impeachment. This paper is about the background of Macapagal who graduated with a Ph.D. in Economics from the U.P. School of Economics. The paper is divided into four sections. The first section describes the Ph.D. program as a course of study and discusses the circumstances that made Macapagal take up the course. The second section discusses her Ph.D. thesis on the real effects of government expenditures and relates it to recent theoretical developments in macroeconomics and public finance. The third part deals with the transitional problems of the post-Erap scenario, taking into account lessons from the past and the legacy of problems inherited from Estrada. The final section probes into how an economist who has the powers of the presidency would deal with economic issues of the country, based on the record of previous writings. The paper concludes on a more optimistic note about economic prospects of the country. But all would eventually depend on the still untested political skills of the successor president.

Subjects: Political economy, macroeconomics, public expenditures, economic development.

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By
Gerardo P. Sicat*

If the current impeachment of President Joseph Estrada succeeds in his removal from office, then Vice President Gloria Macapagal would become President. Her rise as a politician is one of the fastest in Philippine history. There is no doubt that her pedigree helped her a lot, as the daughter of a former President whose name is still revered despite the distant years.

But who is she, aside from the political persona?

Toward the Ph.D.

It is not as widely known that she is Dr. Gloria Macapagal Arroyo, by virtue of a Doctor of Philosophy Degree in Economics that she received from the University of the Philippines in 1985. In her submission to the School, she downplayed her maiden surname to an "M." However, she connected with that surname by dedicating her thesis "to my parents, former President of the Philippines and Mrs. Diosdado Macapagal."

Her academic preparation makes her one of the best-prepared politicians in the country from the standpoint of educational attainment. Her knowledge of economics should be helpful to a leader when presented with complex economic policy options. It would therefore be useful to appreciate this point and discuss its implications.

Given her background as the daughter of prominent parents, it is a remarkable achievement that she worked to obtain a Ph.D. degree. Young people who come from families with inherited economic stature or political power often find it hard to raise their motivation level. So much could be had for the asking, and therefore their best efforts may not be needed. The high achievement of children of well-to-do parents who work on their own efforts is a favorable reflection on the parents who had reared them.

That Gloria Macapagal took further intensive graduate study is also a tribute to her own search for self-improvement. She initially studied graduate economics at the Ateneo University where she also took a job as a faculty member in its Economics Department. Later, she sought a faculty award from the Ateneo faculty development program to enable her to enroll at the U.P. School of Economics.

Ph.D. studies are for those who seek a specialist training. The program at the U.P. School of Economics is not a shoo-in course. Economics has become a specialist subject, and at U.P., the work is

* Professor of Economics, School of Economics, University of the Philippines. In my own lexicon, this paper is a topical comment on a very important issue – the possibility that a Ph.D. in Economics and a graduate of the U.P. School of Economics could become President of the Philippines. Although after a long absence I am now back as Professor of Economics at UP, Gloria Macapagal was never my student. In fact, I recall having talked to her only once, in a neighborhood Christmas party, just before she became a candidate for Vice President (we happen to live in the same neighborhood). She was a graduate student at the School of Economics, when I was still connected with the government. The year that she finished her doctoral work, I was already working in Washington D.C., at the World Bank. My colleagues at the School remember her as a serious student.

up to current developments in the discipline. The faculty is varied, some also obtaining their degrees from graduate schools in the U.S. and elsewhere. The faculty was not only engaged in research and in policy work, but it is also well known and has a professional stature in the Asian region and internationally.

One aspect of Ph.D. study that often defeats many a student who has passed the early hurdles is the research effort that is put in the thesis. The thesis has to be of acceptable quality to the faculty. This means that the student has to aspire to the status of her mentors. The thesis is the final hurdle prior to acceptance within that select group of professionals. To qualify for that stage of research writing, it is important that the student pass comprehensive examinations for the Ph.D. candidacy. This requires written and oral examinations with the faculty. A committee of three faculty members serves a Ph.D. thesis panel, and the research is defended in an oral examination.

The Ph.D. degree is for the student with high intellectual aspirations. It is professional education of the highest order. Aside from intellectual equipment, it also requires of the student enormous personal discipline. Such a discipline would be most exacting especially in the preparation of the Ph.D. thesis. In that endeavor, the student would be essentially on his own. Many students who have already passed their comprehensive exam fail to finish their degree for a number of reasons. Some lack the concentration needed to do the research and finish the thesis. Some get lucrative jobs that get in the way. Others have family obligations to fulfill, especially in the case of married graduate students who are raising children. Still others might have a such unique difficulty focusing the research topic as to foment frustration and, later, disappointment.

It helps to be connected with a research project that provides a job as well as stimulus for the intellectual effort. This was what Gloria Macapagal had at the U.P. School of Economics. At the stage when she was about to write a doctoral thesis, she also became a teaching fellow at the School. She also got recruited into a long-term research project. This was the multi-year Economic and Social Impact Analysis Project that had for its objectives the evaluation of the impact of development projects in the government.

This project involved a large team of economists at the School of Economics that was then headed by the late renowned Dean Jose Encarnacion, Jr. Her involvement in this project helped to crystallize her research thesis related to government expenditure on tourism for the doctorate, which was to analyze the impact of tourism expenditures on the economy. Her Ph.D. thesis acknowledges this point.

Gloria Macapagal did manage to finish her Ph.D. course. She took undergraduate studies at Georgetown University, the Jesuit University in Washington D.C. This period of her studies appeared to have coincided with the years when Bill Clinton was also a co-student. She finished her undergraduate education in Assumption College. But her having finished a Ph.D. in Economics at U.P. should be her crowning achievement as a student.

In 1968, she got married to a scion of the Tuason family clan and settled in La Vista in Diliman, Quezon City, a community flanked by the campuses of UP and Ateneo and Maryknoll (now Miriam). She was married and with children when she began her graduate studies. Here was how she justified getting a job outside and studying further: "...When I got married, I lived with my in-laws. I lived with my husband's family, so I didn't really have my own home to run. So in that kind of environment, it's really conducive ... to look for something to do outside." ¹

¹ As I was finishing this paper, the timely publication of the interview by the Philippine Daily Inquirer with Gloria Macapagal appeared. This and the next paragraph are taken from that broad-ranging interview regarding her personal life, see Staff Interview (2000).

She wanted to become a teacher. She wanted to become a professional, and finally a technocrat in government. In her application for the Ph.D. course at the UP School of Economics, she said that she wanted to take up a doctorate in economics because she wanted to be a technocrat.

The doctoral thesis

The doctoral thesis that Gloria Macapagal submitted to the School of Economics provides a clue to her competence as an economist. The study was entitled, "An Investigation of the Real Effects of Government Expenditures with an Application to Tourism Expenditures." It dealt with issues in public finance and macroeconomics that were current in the profession at the time. In turn, those issues – the real effects of public expenditures on the economy, in particular on the private sector – are at the center of current doctrinal controversy in macroeconomics. This doctrinal controversy flared in the field of Economics as a result of the challenge waged against the dominant theory of aggregate demand embodied under Keynesian economics.

The doctrinal debate is in the context of the effectiveness of fiscal policy, trade-offs between inflation and growth, and, in brief, the debate between Keynesian economics on the one hand and the revival of the old classical economics through the rational expectations school. Her study sought to study fiscal expenditure issues in the context of models offered along the new classical, in contrast to the Keynesian lines.

At the heart of the issue is whether fiscal deficits lead to income expansion or provide a competition with private sector activities. The doctrinal issue critical to her question was to investigate how government expenditure affects output. In particular, is government expenditure likely to lead to an expansion of output, and if so, by what mechanism, if any? This was the topic of lively debate in recent years, a debate in which the major tenets of mainstream Keynesian economics came under attack in doctrinal terms. There were of different modes of thinking about the role of government and output, some of them emanating even from older principles. The issue centered on old propositions with new and unexpected twists.

One of these is known as the Ricardian equivalence proposition, an old idea discussed by David Ricardo, a classical economist of the 19th century. This proposition claimed that people reduce their income expectations equivalent to the amount of the repayment of the debt at a future time. In such a world, when a government incurs new debt, households anticipate this by expecting that their future income would be affected by future taxes. In that event, households discount the beneficial output effects of new deficit finance by anticipating the taxes that are due to finance the debt repayment.

The other proposition of economics is that government expenditure competes for the same resources so that government expenditure could crowd out private activity. The conventional view at that time was that in the presence of excess capacity and unemployment of labor, any new expenditure would lead to a multiplier impact that raises output and employment.

The essence of these two propositions -- resuscitated by a stream of macroeconomic critics of Keynesian economics -- was to put doubts on the effectiveness of fiscal policy. The new school of economists challenging the conventional results of Keynesian economics was called the rational expectations school.

By the 1970s and 1980s, alternative explanations were being sought to account for the failure of fiscal deficits to raise employment rates in industrial economies. This led to the formulation of alternative macroeconomic hypotheses. The debate centered on what was then called the "Philips

curve controversy." The Philips curve formulation predicted a trade-off between growth policy (represented by fiscal and growth stimulus following Keynes) and employment rates. Many observed that that trade-off was weak or did not exist, and it was the major point raised by the rational expectations school that began to challenge the macroeconomic mainstream.

The literature on public finance included a study of Robert Barro (1981), who used an insight from Martin Baily (1968, 1971), that led to the revival of the Ricardian equivalence proposition. The proposition stirred controversial waters. Empirical validation of the theory became the main issue. The empirical literature tested the effectiveness of government expenditure as an instrument of output change. At the time of the writing of her thesis, the prominent works along the line were investigations of Martin Feldstein (1982) whose work provided a defense of accepted theory of the multiplier impact of government spending. The empirical work of Roger Kormendi (1983), whose investigations provided the grist to the crowding out effect of government spending on private consumption, supported the points stressed by Baily and Barro.

Dr. Macapagal's study took a part of this tradition and used it to pose questions about public expenditure policy in the Philippines. Using national income and government spending data, she then explored alternative hypotheses with her own econometric investigations, following the lines proposed by Feldstein and by Kormendi. The effort meant estimating equations that served as alternative hypotheses for the behavior of private consumption in relation to different streams of output and other forms of expenditure. Her propositions examined consumption expenditure as being dependent on a number of factors including output (GNP), tax revenues, real transfers, the public debt as proxy for wealth, and corporate retained earnings.

These econometric calculations used statistical techniques of regression, taking care that the accepted regressions met statistical standards of goodness of fit and that the equations defined by the time series data used also satisfied tests of statistical reliability.

Her regression estimates found no evidence of the existence of the Ricardian equivalence hypothesis in the Philippine context. There was no evidence to indicate that incurring a fiscal deficit implied a corresponding anticipation that future taxation would be expected.

The more important finding in her study, however, confirmed that there was strong evidence of crowding out of private expenditure when government expenditure was introduced. Her findings on this score were robust. These findings, as discussed above, formed the article that she published in the Philippine Review of Economics and Business in 1987.

But the doctoral thesis covered more ground. The work was extended to two other aspects of the problem that were treated separately in two more chapters. The latter part of the thesis was devoted in particular to public expenditures for the development of tourism.

The chapter that focused on the expenditures on tourism examined the magnitudes the public expenditures on tourism and analyzed their impact on output. The period under study covered the 1970s and early 1980s. She found that tourism expenditure (remember the Folk Arts Theatre, the Miss Universe contest and the Ali-Frazier fight, among others?) had some multiplier effect on output. But she examined such positive findings against the alternative of employing the same amount of expenditure on social services. She concluded that the net difference in economic impact would have been higher if the resources were spent on social services rather than on tourism.

The last part of her study was far removed from the empirical investigations described above. Here, she followed a different research tradition, using input-output analysis. She undertook to verify the direct and indirect inter-industrial impact of expenditures on tourism on the rest of the economy

and compared the same with similar expenditures on social services. Using the 1978 input-output model of the Philippine economy, she applied a given final demand projection on the input-output structure. She came out with strong conclusions that social expenditures had a much stronger impact on the economy than the same volume of expenditure on tourism.

Gloria Macapagal's doctoral thesis demonstrates a state of the art effort for a Ph.D. dealing with an empirical topic. Correctly, she focused on research issues dealing with the country's problems. Her treatment of the subject contained a reasonably brief summary of the relevant theoretical literature to her research agenda. Her research covered three different approaches to the study of the impact of government spending. First, there was an econometric estimation of the determinants of aggregate consumption expenditure when the government's activities are taken into account. Second, she undertook a quantitative assessment of fiscal expenditures in the tourism sector. Finally, she employed input-output analysis to examine the comparative impact of tourism as against social expenditures.

The doctoral thesis showed Gloria Macapagal as an accomplished economist, with a good command of the current debates in economic theory. She also knew how to employ up-to-date empirical methods used in economic analysis. She was at home in different modes of economic analysis.

If she decided to become a researcher rather than a public official and a politician, she would have been properly equipped to contribute to the profession more than adequately.

The post-Erap scenario and lessons from the past

The most likely scenario of an Erap conviction, or resignation even if acquitted, is the Constitutional route. This means that Gloria Macapagal Arroyo becomes president. If this specific scenario becomes the flow of history, what economic issues of performance would await the new president?²

The removal of Erap does not guarantee better growth and development. The economy stands a much better chance of improving than under Erap, given his failure to attend to the work of the presidency to which he was elected during almost three years in office.³ The easy part is the pulling off from the nation's back the negative Erap factor. In its place, it would be possible to put in place a new start and a restoration of business and investment confidence. The negative Erap factor is mainly a perception arising from poor management, erratic style, and lack of credibility of the leadership. That perception discourages any favorable decisions that are beneficial to growth and development from being made. It is a factor that adds to the gloomy forecast of future events and makes decision-makers postpone their decisions. When the Erap factor is taken off, a leap in confidence by business and

² There are, of course, countless other scenarios. So long as the new leader faced the economic challenges of the nation squarely, the economic issues would present themselves in whatever scenario. From among the competing scenarios, the Constitutional route appears to hold sway, because it is what the country's political institutions would demand. See R. Fabella (2000).

³ In a moment of candor, perhaps a slip of the tongue, Executive Secretary Ronaldo Zamora was reported to have said in a radio interview that Estrada had the practice of sleeping during what should be his working hours. This "damaged" not only the presidency but also his ability to lead effectively. Zamora said that the economic crisis and the impeachment trial made Estrada realize that he "had to be awake at the right hour... In the morning, there is need for papers to be signed and processed." Secretary Zamora ought to know because as cabinet officer, he manages the office of the President, the center of the cabinet officialdom. See "Post Mortem..." (2000)

investors would be easier to realize until a new leadership proves its worth through hard work and wise decisions..

Based on the way the economy immediately responded to the accusations of corruption against the President, together with the other reasons that became apparent as he continued in office, the negative Erap factor could at least be around 20 percent of current indicators.⁴ The impeachment trial of Estrada in the Senate took away part of the volatility of that negative factor. It helped to produce a temporary, but relative calm in expectations. However, that calm presages a big storm afterwards, especially if the judgment on the impeachment should fail to become credible. That appears to be the way in which Erap has created divisiveness in the social fabric in so short a time.

Lessons from the post-Marcos transition.

The circumstances of the succession are in sharp contrast to the succession of Corazon Aquino to Marcos in 1986. The economic crisis of the Marcos period was prolonged. It was an ever-deepening crisis for almost three years. The crisis dated back to August, 1983 when Ninoy Aquino was assassinated and it worsened until the EDSA revolt in February, 1986. The prolonged economic crisis led to a large external debt, a legacy of economic depression and of severe shortages in the economy. The resulting crisis set the country back for almost a decade.

The problems that Mrs. Aquino faced when she took office in 1986 were far more difficult and more frustrating than those that Gloria Macapagal would face in a post-Erap world, assuming that Erap's disappearance from the scene would be accomplished by January, 2000. The economic disruptions that Mrs. Aquino endured during the transition from the Marcos rule were deep and very challenging. Some of them were psychological. The deep resentments felt by the members of the new government made them commit mistakes that could have been avoided. The government, in its zeal to correct the mistakes of the Marcos rule, committed in turn mistakes of its own.

The discontinuity that took place in some government programs were not necessarily caused by the drastic fall of fiscal resources inherited by the Aquino government during the immediate post-Marcos transition. There were economic projects and programs during the Marcos rule that were neutral from the contentious political issues that divided the nation at the time. The continuity of the civil service was one of them. A discontinuity occurred because the turnover at the top of the government echelon encouraged turnover to the senior level of the government service. Although that was not the official policy, the fact was that there were terminations and forced resignations of critical

⁴ This negative factor can be measured by using standard indicators. One approach would be to project the performance of the economy if a different leader were in charge of the country, by way of some counterfactual hypothesis. Some of the problems related to the stock market scandal and the high level of the fiscal deficit need not have happened. The loss of confidence arising from these events led to the decline of overall economic performance. A more easily calculated alternative approach would be to use the exchange rate as some measure of the negative factor. At year-end (see Manila newspaper accounts on Dec. 28, 2000), Governor Buenaventura of the Bangko Sentral said that the peso should be at around 46-47 pesos to the dollar rather than the current rate of 50-51 range if there were no political crisis. The impeachment proceeding had actually helped to stabilize the exchange rate and reduced uncertainty. Otherwise, the peso exchange rate could have risen far above the 51 pesos to the dollar rate by now if the impeachment process had not absorbed the shock of uncertain events. It is to be recalled that prior to the Asian crisis, the peso was slightly higher in value than the Thai baht. Today, despite the problems in Thailand, the peso is about 17 percent cheaper than the Thai baht in terms of the US dollar. The current baht is around 41-42 pesos to the dollar. It is therefore justified to use the base of 40 pesos to the dollar as the basis of the negative Erap factor.

personnel at the middle and senior level of the bureaucracy. These personnel were important to project management and implementation not only for their experience but also for the institutional memory that they embodied. The result was that some important programs suffered from a disruption in their work for an unduly long period.

A result of these mistakes was the neglect of some critical sectors by Mrs. Aquino's government. Toward the second half of her term when economic recovery was sucking up excess energy unused by the crisis and aging plants were becoming less efficient, the neglect of the energy sector surged to the forefront of the national consciousness. Power shortages were being experienced with daily regularity, so that the budgets of households and of business institutions became hampered by unnecessary disruptions in terms of new expenditures. The energy development program was a major casualty of political wrangling. The nuclear power project symbolized the corruption of the Marcos leadership,⁵ and it gave the succeeding leaders shortsightedness about where it could get the energy replacement for a discontinued huge power plant project that had been on stream to replace growing energy needs.

Facing the consequences of this neglect towards the end of her term, Mrs. Aquino's presidency was perceived as weak and she became the target of a constant threat of challenge from the military. (Of course, Mrs. Aquino as president had a major share of two catastrophic natural disasters that altered momentary priorities and the attention of the national leadership: the earthquake of 1990 and the Mount Pinatubo eruption of 1992, both of which had negative effects on economic performance).

The post-Erap transition.

Gloria Macapagal's transition into the post-Erap period is less filled with the problems that Mrs. Aquino had in her time. Although in political terms, it is as sensational because of the impeachment process and the public disemboweling of the accused, the post-Erap succession does not provide the dramatic backdrop on the state of the economy compared to that of the post-Marcos succession. Up to the present, the economy is still holding up. The main problem today is how not to get the economy to deteriorate any further, and to restore the momentum that was available to the leadership when political power was transferred from Ramos to Estrada. The Asian crisis provided a new dimension to the economic issues facing the Estrada presidency, but there were enormous opportunities available that he failed to take advantage of. Provided that the trial is relatively quick and the Constitutional succession does not consume a long time, it would be possible to restore the economy back to relative health. The longer the succession takes place (or if he digs in and decides to continue if an acquittal in the Senate took place), the prospects of an economic tailspin and crisis of grave costs to the nation would be almost certain.

The major political issue that Macapagal faces is how to bring about a cohesion among disparate groups that had helped to remove Erap from government because of its corruption and

⁵ The nuclear project was a flagship economic project of the government. It was conceived during the energy crisis of the 1970s when the objective was to diversify the dependence of the country on energy sources, including nuclear fuel. The plant was designed to represent a major capacity boost towards meeting the country's energy needs. Even as the project selection was about to be made in favor of General Electric, there was a reversal of the award to Westinghouse Electric, with a change in technical specifications. In later investigations of the project, it became clear that the change in the award was a classic case of corruption through commissions paid indirectly paid to a crony who was tied to the leadership. The project was almost finished by the time of the EDSA revolt. The alliance between those who criticized the project as an environmental disaster and the those who wanted to leave the project as an example of the corruption of the Marcos leadership led to the project being abandoned. But the project had cost the country billions of pesos. It was as if the country, poor in resources, decided to build an aircraft carrier and, during a typhoon while at sea, the aircraft carrier sank. Billions of pesos of business debt were sunk with it, which the country continues to pay for as part of the external debt.

inefficiency. Assurance and appeasement of the main constituency of Erap -- the poor -- will require a major effort in public information campaign on the reasons for his removal from office. This is essential because, despite the widespread publicity of the trial on television, some attitude surveys appear to indicate that Erap's hold on mass opinion continues to hold sway. The problem is how to reassure them that their conditions will improve with a change in focus of the leadership.

For the short-term, the problem of Gloria is how to reverse Erap's erratic management of the economy and to replace it with an economically focused leadership. Estrada's legacy is a compounding of the country's economic problems. Some of the missteps of Erap have caused damage to the future of the economy because of the mixed signals that they gave.⁶ Such thoughtless changes in policy were short of catastrophic, but they were certainly in a ruinous direction. Erap simply missed good opportunities and he has aggravated problems where there ought to be none. The problem of Macapagal is how to get a stalling engine to perform towards a smoother run.

This can only be done effectively by a push on the demand front -- raising investments, both domestic and foreign. Most economists understand that the reason why other Asian countries have progressed far ahead of us is that their policies had the effect of expanding the demand for labor faster than the supply. The objectives of their over-all development policy had the result of increasing the growth of investments and of industries that were efficient and competitive, growing on the market demand that they were able to command and not on the basis of the state subsidies that they received. Structural reforms that Erap inherited in the industrial and trade sectors through the major economic liberalization of policies led to an increase in foreign investments and exports. As these reforms took root, the country began to reap the harvest of rising industrial exports throughout the 1990s, especially in the second half of that decade.

The expansion of labor intensive types of export industries is an important sign that if this continued and if the export sector became more diversified, the domestic industrial base would become more integrated not only internally but also with the world economy. This would make the demand for labor grow much faster. It will only be then that the country will experience the phenomenon of a strong rise in real wages. Focusing on the expansion of investments for industries that utilize our inexpensive labor for products that are needed in foreign markets is a good focus of policy.

Estrada's poor fiscal management is a major concern. The result of this is the fiscal deficit. It has deteriorated each year of the years that Estrada has been president. From close to zero as a percent of the GDP, the fiscal deficit has been rising each year. It is inching towards 3 percent of GDP whereas it was almost zero percent when he took office. (In nominal terms, a fiscal deficit of about 120 billion pesos is expected by the end of 2000). This fiscal deficit was not only caused by a growing demand for expenditure. It was a failure to work effectively on the revenue side.

While a part of that deficit was due to the problems aggravated by the Asian economic crisis, a substantial part of the failure to deal with the deficit was the government's slow reaction to critical issues and developments. Foremost among these problems, of course, is fiscal restraint on the expenditure side. Then, the work on the revenue front has been inadequate.

In fact, the increase of the fiscal deficit was also the handiwork of sloppy work on the revenue front. First, tax administration weakened. The flip-flop regarding the pursuit of the Lucio Tan tax

⁶ An example of this was the unexpected decision to abrogate the Philippine-Taiwan air agreement, which sent the wrong message that operational rules for Taiwanese investors could change. Of course, the policy was to give support to a crony's case of strengthening the position of the Philippine Airlines in a dispute on market sharing. In the end, Estrada retreated from this position, after causing harm to the economy's investment promotion prospects and disruption of transportation routes for thousands of Filipino industrial contract workers in Taiwan's factories and establishments.

evasion case could have ruined incentives and morale in the tax collection agency front. The rise of customs smuggling has been associated with duty free imports by those with duty-free shop privileges. This was a problem of implementation that has been exacerbated by the perception that certain cronies of the President were behind the smuggling problem. All these weakened tax administration, when the duty of the President is to strengthen it.

Second, the government did not pursue the privatization program as vigorously as required by the expected budget gap. The privatization program was supposed to yield significant supplemental revenues for the government to meet part of the expected fiscal gap. By falling into a relaxed posture in implementing the privatization program, it fell further into the trap of allowing major public corporations to depend on budget subsidies because they were not allowed to pursue price increases to meet costs in selling their economic services to the general public. The contingent liabilities of these corporations became actual liabilities of the fiscal sector. Among these corporations were the Metro transit authorities, the National Food Corporation and the National Power Corporation.

The privatization of the National Food Authority was designed, from a fiscal standpoint, to bring in new and extraordinary revenues and reduce the losses that are a budget drain, aside from improving the distribution of food staples. But Erap could not make up his mind to pursue a commitment made to the Asian Development Bank in line with a program of public policy reforms designed to improve the food distribution program. This was one of the strikes, to use a baseball term, called on Erap that was to bring down his international credibility as a leader in the eyes of multilateral institutions, for there was a policy commitment in the program agreed with the ADB. A number of privatizations of state assets took place, but these were the sales that were near that stage before Ramos left the government -- the sale of the copper smelter plant and of the phosphate fertilizer plants.

But the work on privatization projects that remained have stalled. The reforms in the electricity generation sector included the law designed to unbundle the huge generating assets of the National Power Corporation by privatizing the electric generation and distribution. If the law to reformulate this sector was passed, new investments in the power sector would certainly follow. Another benefit would be to have a part of the public external debt reduced since, by virtue of privatization, some of that debt would be acquired by the private sector. But the major legislation on the power generation sector reform languished in the Congress because of lack of presidential leadership on this matter. This was a major loss in years of new investment activity because prior to the 1998 presidential election, the legislation was close to passage by Congress.

Admittedly, major economic policy problems remain unresolved. But these were the problems that Erap, with his huge mandate and popularity, failed to pursue because his attention apparently was on other things -- the things that caused his impeachment. The impeachment trial has taken valuable time to work on critical economic development issues. And the successor of Erap will inherit a legacy of unresolved and difficult problems. These hard decisions are required as important steps in lifting the confidence of the investment sector and re-introducing foreign investments to come into the country.

In reference to the rising fiscal deficit, it always poses a threat of inflation. A growing fiscal deficit could weaken the rest of the economy by transmitting higher borrowing costs on the rest of the economy. The increase in the fiscal deficit also could mean crowding out meaningful private sector activity.

Moreover and significantly, the size of the fiscal deficit has put the country out of compliance with the macroeconomic program with the IMF. This meant that the government could not turn to the IMF and other multilateral financial institutions to provide support for the financing of the fiscal

deficit. This is the reason why the government has turned towards more expensive funds (offshore dollar funds and external capital) to finance the deficit. Initially, this financing method does not pose an inflationary threat, but it raises the external debt burden and the country's foreign exchange rate exposure.

The fiscal deficit already caused the downgrades of the sovereign debt ratings of the Philippine government made independently by Standard and Poor's and by Moody's during the fourth quarter of 2000 by one notch in the rating levels, with a warning of a review for future reduction. Simply, this translates into a higher cost of borrowing for the national government when it accesses the international market. With the sovereign debt rating downgrade, the obvious secondary impact is on Philippine companies and banks. Their borrowing cost rises at least by the additional cost of the downgrades. They themselves could suffer downgrades if they are internationally rated by the credit agencies, as indeed the Philippine major banks are, for instance, Metropolitan Bank and the Bank of Philippine Islands.

The obvious costs of the rising fiscal deficit and the downgrade of sovereign debt rating is for the banks to pass on the rising cost of credit to Philippine borrowers. This means that companies and institutions in need of credit, including those that are already in debt and that have credit to refinance, will have to face an increase in interest cost. This is the lurking danger, for if borrowing costs went up with the deteriorating posture of the overall macroeconomic picture -- the negative Erap factor -- many companies that are highly leveraged are in danger of financial collapse. This could only lead to rising non-performing loans in the banking system. The average non-performing loans of the banking system have risen in 2000. Thus, a prolonged crisis will aggravate, not help, the financial position of Philippine companies.

The succeeding president is therefore faced with difficult policy issues. These issues are not popular issues that could be easily understood. Some of the measures might require pain before the gains from their adoption become obvious. The improvement would help reduce the operational deficits of the state corporation that keep rising because the government never faces the needed action to improve revenues and efficiency gains in public corporations. The first gains would therefore be felt in the improvement of the fiscal deficit. (But the popular mind does not digest the implications and benefits of reducing the fiscal deficit. It is only when its effects hit the people that people become aware of its bad consequences.) The other benefits would be improved efficiencies in the whole economy because the energy reform bill, if done right, could lead not only to cheaper energy prices in the longer term for the consuming public but also towards a large increase in infrastructure investments in the economy.

But a new, highly motivated and forceful president who does the necessary homework (unlike Erap who was essentially a sloth in these matters) could articulate these benefits and could force the solution to the issues and get the work done.

All of these will put to the test the political skills of Gloria Macapagal. This is, however, an area where she has not been sufficiently tested. Her background is largely in academic and in technocratic work in the industry department of government. Her stint in the Senate was relatively brief, and her management of the Department of Social Welfare Secretary, the assignment that she accepted as Vice President, was largely as head of a relatively safe sinecure where she could not basically be involved in the economic issues facing the Estrada government.

The political calendar has a presidential election in 2004. That is just three years away. For any new president introducing difficult economic reforms during the second half of an unexpired term could pose some serious calculations because the gains from those policies could only be realized later.

But if they succeed, enormous potentials for future expansion of the economy would be in the offing. For these would best be put in place during the first half of the presidency so that the benefits from them could be harvested during the second half. During the second half of the unexpired term of Erap that she would fill, all the potential candidates who would make their presence to challenge her. Therefore, the last three years of the unexpired term of Erap could pose difficult challenges regarding the passage of the most difficult economic reforms.

The Estrada government is remarkable in that it has failed to undertake any major reforms, because of the innate deficiencies of the president as an economic leader. Every time he proposed reforms, he retreated quickly when the criticisms got tougher.⁷ Lacking the patience or the ability to articulate these programs, he failed to make the investment climate active.⁸

Estrada's accomplishment in the economy was one of providing the conditions for relative standstill. The economy grew at a level of growth permitted by an economy already beset in part by the Asian economic crisis. The period of rising growth rate that was the result of the economic reforms were stalled because of a multiplicity of factors, including the Asian crisis, but more because of Erap's poor management style and inadequate leadership. The economic liberalization program stalled in some directions, notably in tariff reforms.⁹ There were some gains in policy -- even in the tariff reforms -- but overall, the actions of the government were to stall here and there.

Among the main problems of poverty in the country -- the main directions of reforms that a program for the poor could have made a major dent under an Estrada presidency -- is how to raise the number of jobs in the country. This is far more important than the preoccupation with protective labor legislation, which has been the hallmark for Philippine policy-makers' concern for decades. Here, the problem could have been to continue raising investments, both domestic and foreign. Ultimately, such preoccupation could impact on raising the demand for labor and therefore it is the most assured route towards raising the domestic wage rate in the country.

A sustained program that leads to high employment growth results from a robust economy in which industries thrive because they operate at a competitive level with other countries. The best medicine for rising demand for labor and a rising employment rate is to pattern the economy's growth towards the maintenance of industries that are competitive, whose existence is justified by commerce rather than protected markets. The momentum for growth was established by the strong efforts undertaken by the Ramos government to bring the country towards the international economy. But there were major shortcomings still, because there was not enough time to pursue the next stage of reforms.

Those reforms were part of the mandate of Erap that were conveniently forgotten as soon as he stepped into the government. The coming years are critical for the country because it is a period of rapid internationalization. First, the ASEAN market will be moving towards the reality of a common grouping of countries with regional commerce as a major aim. The net result is the expansion of the domestic market of the economy. Second, the world's trading rules have been redefined by treaty obligations agreed upon in the World Trade Organization. The international trading system opens up

⁷ The following are instances of these retreats. He backtracked from the pork barrel issue that he had promised to do away with without substantial legislative concessions. The retail trade liberalization was passed with much watered-down provisions. The power reform bill had not yet passed; the constitutional revisions that he proposed were shelved. The tariff reform program was not fully revised as planned.

⁸ See G. Sicat (2000) on the issue of Erap's economic leadership.

⁹ See G. Tecson (2000). Her study cautiously noticed the progress in tariff reforms. However, the study noted the setbacks from planned tariff reforms in the manufacturing sector where some reversals in tariff changes had been put into effect to favor some industries. The issuance of Executive Order 63 singles out a number of manufacturing industries in which the action to raise tariffs reversed the general trend that the government has adopted since the 1980s.

enormous opportunities for countries to reap major rewards if they play their cards right. When China – the last of the socialist countries – indorses active engagement within the World Trade Organization to promote her economic growth, it is time for a country, such as ours, to buckle up and work at how best we could gain from the international trading.

Probing what an Economist as President would do

If one's early professional work could serve as a gauge of a nation-builder's approach to problems, could we predict what President Gloria Macapagal would do?

Here I am reminded of the quote from a sage economist -- Milton Friedman, I think -- when he was posed the ultimate question. "As an economist, what would you do if you were President?" Friedman's answer was something like, "But if I were President, then I would be a politician!" Of course, this is an exaggeration.

Political skills of a leader are definitely important. But an economist seeking the ultimate improvement in the country's plight would attempt to move the country towards greater efficiency and to move towards comparative advantage as a principle of gaining world market attention. To do this, the country's factors of production have to be put on their competitive edge. This means taking advantage of the competitive edge of labor as the magnet for attracting foreign investments. An economist can read better the myths and fallacies of policy-making¹⁰ and can understand the need to avoid their worst consequences.

If her doctoral thesis in Economics could serve as a rough guide, what can we predict about her economic inclinations if she becomes President of the Philippines? As President, she would have to make decisions based on a broader set of factors, including, of course, economic factors.

It is fortunate that she chose to study government expenditure and its impact on the economy. That is an important area where it is possible to have a good reading of her views on managing fiscal issues. If her study provides a clue to what she would do if she were in the shoes of the President, I venture to make a few comments on how she would approach them if she were mainly dealing with these issues from an economic context.

First, I think she might become a fiscal conservative if she does not get afflicted with the common disease that hits all political leaders: to spend more. All political leaders tend to regard public spending as a way to demonstrate ability to serve the constituents. But economists understand better that excessive spending not matched by a growth in tax resources could lead to inflation and to other economic dislocations. She will have reservations about having large budget deficits to finance operational deficits of the government. For this reason, she will put the budget deficit under a much tighter rein. This follows from her finding that excessive fiscal deficits could "crowd out" private sector activity. She will have a healthy skepticism about so-called counter-cyclical policies.

Second, she will pay attention to the composition of public expenditure. She will make efforts to improve the share of social expenditure – education, health, and other social services. This means that specific budget components will have to be prioritized, paying greater attention to the need to improve social development services. This follows from the fact that, following her own investigations, she finds that social services have a higher impact than tourism expenditure.

¹⁰ Some of the glaring myths and fallacies that have afflicted Philippine policy-making are discussed in one piece in a recent article. See G. Sicat (1999).

Third, she will likely strengthen public investment financing so that public infrastructure investment need not hinder the growth of private investment. She will follow new techniques of financing public investment from private sector sources. But she will make an effort to make these financing arrangements productive so that they are not burdensome on the budget.

Fourth, although the responsibility of the Presidency will take on many demands, she will pay greater attention to economic issues. Her professional training as an economist will provide her with appropriate equipment in dealing with intricate issues.

Fifth, she will likely encourage the growth of the domestic economy in line with improving Philippine competitive position abroad. In doing this, she has a greater appreciation of the importance of a sound exchange rate policy, as a means of pricing Philippine factors of production more competitively for international markets. She has a more thorough understanding of many economic policy questions than most Philippine leaders, and surely she will show a quicker absorption of economic issues than her immediate predecessor.

The country therefore faces the prospects of having good luck on the leadership front after almost three years of a rudderless presidency.

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