The circumstances are different but the situation is similar. Newly-elected President Joseph Ejercito Estrada enters Malacañang in 1998 amidst an economic crisis, a scenario quite like the time when former President Corazon Aquino assumed office in 1986 where she inherited an economy battered by the 1984–1985 debt crisis and when former President Fidel Ramos became the country’s leader in 1992 where the Philippines was suffering from an energy crisis and a post-Gulf War effect. Thus, President Estrada faces a huge task ahead. Still, the effect of the economic and social reforms implemented in the past 11 or 12 years and the smooth and peaceful transition of government should provide the Estrada administration with enough momentum to guide the country through the adverse impacts of the ongoing financial turmoil gripping not only the Philippines but the entire East Asian region.

But just how well did the Philippine economy fare in the last 11 years? Has it truly recovered from being the “sick man of Asia?” How far has the country reached the goal of sustainable growth and development? Is the Philippines better off today than it was more than a decade ago?

In a major forum sponsored by the Philippine Institute for Development Studies (PIDS) last July 22, Dr. Josef T. Yap, together with the other Research Fellows of the PIDS, presented a comprehensive assessment of the performance of the Philippine economy during the period 1986-1997. Using the 1992-1997 Medium-Term Philippine Development Plan (MTPDP) as a benchmark for their assessment and examining how close the country has satisfied the conditions considered as determinants of long-term economic growth from both the theoretical and empirical standpoints, Yap and associates concluded that despite the overall economic gains evident during the period under review, the Philippines still faces daunting problems and, in many...
areas, pales in comparison with its neighbors, notwithstanding the adverse effects of the regional financial crisis on the latter. The key, according to the PIDS team, is in terms of productivity performance.

In examining the factors affecting the Philippines’s economic performance, the PIDS team classified them into two broad categories. One relates to the elements of recovery and economic growth which consists of the aggregate factors like trade and industrial policy, productivity trends, macroeconomic stability and infrastructure. Another refers to the microeconomic set of factors affecting the sustainability of economic growth and development. This includes technology policy, human resource development, poverty alleviation and equity promotion, and environmental management. Clearly, if the economy is to travel the path of sustainable growth and development, the government should not simply focus its attention on the aggregate factors but also, and equally important, on the microeconomic elements.

Assessing the Past Decade

When a new administration took over in 1986, economic reforms were earnestly put into place. This was followed by more reforms through the years especially during the Ramos administration. As a result, gross domestic product (GDP) expanded, per capita income increased from US$426 in 1986 to US$507 in 1997, the level of poverty incidence declined, the consolidated public sector account yielded a surplus in 1996, the first in two decades, inflation was on a steady decline, and export growth became positive.

Despite these significant gains, and those in almost all sectors, however, the Philippines still lags behind its neighboring countries. Per capita income, albeit its increase, remains to be lower than most East Asian economies and improvements in the quality of life as measured by the UN Human Development Index have not been as dramatic as in other countries over the past 15 years (Table 1). Notwithstanding the tremendous negative impact of the current regional financial crisis on some of these East Asian economies, it would still take some time for the Philippines to reach the development level of, say, Malaysia or Thailand.

It is to be noted, too, that while a marked improvement in the investment climate through greater outward orientation, better infrastructure and more sound macroeconomic fundamentals was evident during this period under review, progress in terms of microeconomic reforms was quite slow. This can be gleaned in the poor record in technology upgrading, persistent underinvestment in human resource development, extremely slow pace in poverty alleviation and equity promotion, and sharp deterioration in the quality of the environment. Said shortcomings in the microeconomic reforms prevented potential gains from being realized.

Particularly alarming is the resulting picture in both the manufacturing and agriculture sectors. For manufacturing, despite the trade and industrial reforms implemented and the apparent efficiency gains, its growth performance during the period was generally disappointing. Meanwhile, the agriculture sector continues to exhibit low growth rates. The inappropriate exchange rate policy, low investment rate as well as price distortions are major culprits. But besides these, the continuing decline in the sectors’ growth performance has been largely attributed to the current regional financial crisis on some of these East Asian economies, it would still take some time for the Philippines to reach the development level of, say, Malaysia or Thailand.

A Closer Look into the Story

Aggregate factors

- Trade and industrial policy and the manufacturing sector. Despite the policy reforms where the Philippines took great strides to enhance its outward orientation and be competitive in the process of globalization, manufacturing growth has not performed up to expectations. This is due to the exchange rate policy, the poor record in labor productivity and total factor productivity. Between 1987 and 1995, the unit labor cost—which is the ratio between nominal wage and labor productivity—increased and placed the country at the lowest rung in terms of productivity performance. The manufacturing sector’s unit labor cost rose by 21 percent, which can be attributed to

Table 1: Economic Indicators

<table>
<thead>
<tr>
<th>Per Capita Income (PPP$)</th>
<th>HDI*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Philippines</td>
<td>2,170</td>
</tr>
<tr>
<td>Indonesia</td>
<td>1,820</td>
</tr>
<tr>
<td>Malaysia</td>
<td>5,070</td>
</tr>
<tr>
<td>Thailand</td>
<td>3,280</td>
</tr>
<tr>
<td>China</td>
<td>2,470</td>
</tr>
</tbody>
</table>


*An index nearer to 1.0 indicates a higher quality of life.
a stagnant labor productivity rather than to rising nominal wages. The low labor productivity, in turn, may be due to low domestic investment rate, infrastructure development, and social sector policies. The first factor points to insufficient accumulation of capital to support the labor force while the third refers to a persistent underinvestment in human resource development.

**Agriculture.** The sector which contributes 20 percent to the GDP and 40 percent to the employment rate has had a miserable performance since the 1980s. The growth rates of its gross value added and exports in the 1980s and 1990s have been lower than other Asian countries. With the exception of livestock, poultry and some crops, most crops and fishery exhibited declining competitiveness. Although crop productivity per hectare increased, the pace had been slower than the 1960s and 1970s. This dull performance is attributed to

- increased protection of the sector,
- penalty against exportable agricultural commodities,
- inadequate agricultural support services, and
- land market distortions.

There have been confusions arising from the implementation of the Comprehensive Agrarian Reform Program (CARP), particularly in terms of property rights. On the other hand, public expenditure for agriculture focused on redistribution and the strengthening of environmental management rather than on investments to enhance productivity such as research and development (R&D) and infrastructure.

**Employment, wages and productivity.** In 1996, unemployment rate was estimated at 7.4 percent. The decrease was 1.7 points lower than the 1987 rate of 9.1 percentage. This commendable performance was based on the increase in the number of employed Filipinos especially during the period 1993-1996 when an average of about one million net new jobs per year were generated, a number quite close to the target cited in the MTPDP.

Despite this positive performance, however, one aspect remains worrisome. This is in the area of competitiveness. Clearly, with the unit cost of labor rising from an index of 1.0 in 1992 to an index of 1.3 in 1995, a slippage in competitiveness can be gleaned. The sad part is that data show that such weakening of competitiveness began as far back as 1987 when the index stood at 0.5.

As noted earlier, the high labor cost is attributed to a stagnant labor productivity which in turn may be traced to

- low investment rate,
- weakness in attracting FDIs,
- poor infrastructure development,
- low level of effort in R&D, and
- persistent underinvestment in human capital.

**Investment, saving, fiscal adjustment and macroeconomic stability.** Investment is at the heart of economic growth. Compared to its Asian neighbors, the Philippines has a very low investment rate, explaining the mediocre economic performance of the Philippines and its poor labor productivity record vis-à-vis other Asian economies. One reason for the country’s low investment rate is its low saving rate as related to the country’s poor record in macroeconomic stability where periodic boom-bust cycles were in evidence.

While macroeconomic stability showed a marked improvement in 1992–1997 characterized by a downward trend in inflation, the current account deficit being under control, the consolidated public sector account recording a surplus for the first time in two decades and the M3/GNP ratio rising, the liberalization of the capital account in 1992 and the surge in global capital flows, however, significantly changed the parameters of macro policymaking and financial regulations in the country. Thus, it was ironically in this same period where the economic managers faced new threats to macroeconomic stability and simultaneously had to contend with old ones.

In terms of the performance of the fiscal sector in the period under review, a lot of fiscal adjustments were made, enabling the consolidated public sector position to reach a surplus in 1996. Still, the assessment team noted that the bulk of fiscal adjustments in recent years was due largely to the inflows of privatization proceeds. With the impending sharp fall in tariff revenue resulting from the tariff reduction program, the recurrence of a fiscal deficit is seen to be a problem.

Emphasis should therefore be placed on improving the revenue–generation capacity of the government especially in tax administration. Capital market deepening should also be promoted along with an improvement in the level of domestic savings. The latter should come mainly from the household and unincorporated sector.

**Infrastructure.** Within the period 1980–1990, the country may have made significant improvements in infrastructure but it nonetheless still lags behind its Asian neighbors. Neglect of infrastructure investments can be partly blamed on the country’s macroeconomic crisis and may be resolved by implementing “draconian” stabilization policies. Some of the problems facing the country’s infrastructure program include the following: the country having the most expensive electricity rates in Southeast Asia; slow increase in the...
number of main telephone lines and payphones; inadequate and unsatisfactory port facilities; and weak water supply planning and coordination.

**Microeconomic factors**

- **Slow pace in poverty alleviation and the deterioration in income distribution.** Although poverty incidence declined between 1985 and 1997 (Table 2), the actual number of poor families increased. This means that there remains “a core segment of the population that is marginalized and is affected very minimally by developments in the mainstream of society.” In terms of poverty alleviation, the country has not been successful in reducing the number of poor families. Moreover, the 1997 data from the *Family Income and Expenditure Survey* (FIES) showed a sharp deterioration in the equity of income. Based on the experiences of other high-performing Asian economies (HPAEs), poverty reduction and greater income equality improve social cohesion. Thus, the Social Reform Agenda (SRA) adopted by the Ramos administration is noteworthy since it aimed to lessen, if not eradicate, poverty by implementing government interventions which are directed toward the integration of the “society’s disadvantaged groups into the mainstream political and economic society.” However, with its institutional approach, it may take some time before the potential positive effects from the SRA can be realized.

- **Human resource development.** Health, nutrition and basic education have high significant impact on labor productivity and it is in these areas where the government still has much to do. To cite, infant mortality has only fallen slightly since the 1980s and access to health services is still relatively low. These conditions are attributed to the government’s inadequate response to changing policy and program environment such as the devolution of the health services to local government units. Likewise, there has been little progress in providing basic education due to the low level of expenditures for human development priorities.

- **Technology.** The country’s capabilities in second- and third-wave technologies are so insufficient that the government still depends on foreign firms for telecommunications, power generation, transportation, agricultural inputs and machinery, machine tools, pharmaceuticals, and consumer electronics. The science and technology (S&T) competence is weakly supported by the educational system and is seen as a cost to be minimized rather than as an investment. Thus, in the last decade, the country still lags behind its neighbors in terms of the ratio of R&D expenditures to GDP and the growth of total factor productivity. Even while there are programs to promote S&T, these have been poorly funded.

- **Environmental management.** Air and water pollution have brought damages similar to the depletion of the natural resources. For example, an increase in the number of respiratory tract illnesses in Metro Manila due to lead emissions from motor vehicles and transport fuels has been estimated to have cost the country approximately P2 billion in 1992. Thus, the Ramos government’s efforts to lessen emissions by promoting the use of unleaded gasoline and imposing high taxes on lowleaded gasoline are noteworthy. At the core of sustaining economic growth is the aspect of environmental management. However, a three percent decline in the genuine savings measure—which includes adjustments for both human and natural resources—reveals that the economy is leaning toward unsustainable growth. Data reveal that the country has the lowest rate of protection of natural resources. To cite, roughly six million hectares (20 percent) of land area are unprotected and unallocated. Of course, a number of programs have also been set up, aimed at promoting equitable access to both upland and coastal resources such as the Fisheries Code of 1998 or Republic Act 8550; however, they have to be pushed and implemented in earnest.

### Table 2: Poverty Indicators

<table>
<thead>
<tr>
<th></th>
<th>1985</th>
<th>1994</th>
<th>1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>Poverty incidence (%)</td>
<td>44.2</td>
<td>35.5</td>
<td>32.1</td>
</tr>
<tr>
<td>Number of poor families</td>
<td>4,355,052</td>
<td>4,531,170</td>
<td>4,553,387</td>
</tr>
<tr>
<td>Urban</td>
<td>1,250,398</td>
<td>1,521,882</td>
<td>1,246,173</td>
</tr>
</tbody>
</table>

Source: Economic and Social Statistics Office, NSCB
nomic programs that will carry the Philippines in the next century under the mantle of sustainable growth and development.

As such, the country must gear up for the increased integration of the world economy. The economy must be vigilantly monitored and its performance continuously assessed in an objective manner. Fundamental reforms must be implemented and, in certain cases, continued in order to achieve sustainable growth. The regional financial crisis notwithstanding, our policymakers should not allow it to distract them from focusing on and instituting fundamental reforms.

In this regard, Yap and the PIDS assessment team offers an economic agenda that will help the country push toward this goal. The agenda is grouped into four categories, namely, macroeconomic stability, productivity and efficiency, social cohesion, and environmental management.

Macroeconomic stability

Capital markets must be further developed to spur domestic resource mobilization. An increase in domestic resources will stimulate and further develop the capital markets. A developed financial system may bring about an increase in the savings rate and ultimately lead to higher economic growth. Invariably, economic growth causes savings to rise. This is the cycle of economic growth and economic managers should push the country toward this condition.

Fiscal prudence must be maintained to make monetary policy more flexible. One way to enhance the government’s revenue performance is to stop enacting new laws and instead focus on improving tax administration such as, among others, polishing the performance evaluation system for revenue officers and creating data centers (Manasan 1998). The government must also restore the levels of capital outlays and government expenditures on maintenance and operating costs to their pre-1984–1985 numbers. It must likewise put emphasis on the maintenance and operating expenditures since underspending for the upkeep of infrastructure creates disruptions and damages to the economy.

Monetary policy must continue to be prudent and an appropriate exchange rate policy must be implemented.

Financial reforms must be implemented to maintain investor confidence in the economy.

Productivity and efficiency

The government should aim to boost the manufacturing and agriculture sectors through the following interventions:

- Raise savings to encourage FDI;
- Refine infrastructure policies through a competitive environment, better-equipped agencies in the face of a market-oriented policy regime, organized infrastructure agencies, a sensible management of contingent liabilities by the government, and proper delineation of national-local government roles;
- Implement strategic human resource development (HRD) and science and technology (S&T) through technology transfers, a more focused and integrated research and development program, a productivity-oriented HRD plan, and a streamlined Department of Science and Technology (DOST);
- Continue trade liberalization and tariff reduction; and
- Reform the agriculture sector.

Social cohesion

The PIDS Assessment Team proposes the facilitation of access of the low-income groups to basic services and of the underprivileged groups to both physical and human capital so as to enhance their own productivity.

First, a reinvigorated Comprehensive Agrarian Reform Program (CARP) should be fully implemented to be able to push forward the agrarian reform. Second, government interventions to address poverty and equity issues must focus on the following:

- a broadbased economic growth that will benefit the rural areas through the generation of more gainful employment and livelihood projects,
- efficient basic social services programs targeted for poverty groups,
- institution of safety nets for the poor during the transition into a global economy, and
- a monitoring system for identifying proper beneficiaries.

In addition, a population management program must be seriously implemented since rapid population growth is one of the underlying factors in the problems on health and education. Moreover, the low-income groups’ access to housing should be remedied.

Environmental management

Three important issues need to be addressed in terms of environmental conservation and management. These are the correct pricing of the use of natural resources, reform of property rights, and strong monitoring and enforcement of prices and property rights. To do these, the DENR and the DAR have to work closely together. Adequate and timely information must also be ensured.

Conclusion

Summing up, it is evident from the analysis and assessment that many basic reforms still have to be designed and implemented. Moreover, it should be noted that to ensure a more sustain-
The Financial Crisis in East Asia

From Miracle to Debacle

The current financial turmoil in East Asia has sent shock waves across the global economy, even eliciting dire predictions of another Great Depression. A World Bank (1989) study lists three possible sources of a financial crisis: macroeconomic conditions, industrial and financial policy, and debtor and creditor behavior. The dominant view is that the present crisis was brought about by weaknesses in the financial system of the economies, bringing into focus specific financial policies, and debtor and creditor behavior.

Many of the East Asian economies implemented twin liberalizations. First is the opening up of the capital account which allowed foreign investment to flow in and out of an economy with very minimal regulation, and second is the liberalization of the domestic financial system. The first measure allowed domestic firms to gain access to foreign capital while the second increased competition among financial institutions operating locally.

One view of the crisis is that the existing regulatory framework could not cope with the new demands brought about by these structural changes. Prudential regulations and bank supervision were inadequate to cope with the more liberalized economic climate. The riskiness of loans was not evaluated thoroughly, financial institutions did not disclose enough information, and even if they did, the data were not timely.

The stance of the government, particularly the monetary authorities, also encouraged the expansion of the financial system and dollar borrowing. There are at least two elements to this aspect:

- By standing behind the viability of the domestic financial system, the government always gives an implicit guarantee to private debt. This guarantee encouraged bankers to take on riskier loans knowing that even if these fail, they will be bailed out eventually. Deposit insurance forms part of this guarantee, but in this case, it discouraged depositors to monitor the performance of the banks.
- Economic managers were not able to respond properly to the rapid inflow of foreign capital. Exchange rates appreciated in real terms and/or interest rates rose. The interest rate differential encouraged dollar-denominated borrowings. In the Philippines, instead of working to keep the exchange rate at a competitive level, the Bangko Sentral ng Pilipinas (BSP) gave a strong signal that the level of the exchange rate was not only appropriate but would remain stable for an extended period of time. This stance further encouraged foreign borrowing.

The increased access to funds and greater competition led to a rapid expansion in the assets of the domestic financial system, mainly in the form of loans to the private sector. An unhealthy mismatch of funds in terms of maturity and currency base developed. Banks would lend long-term loans based on deposits and borrowings that were short-term in nature; and banks would lend dollars to firms that earned revenue in domestic currency. Data show that 40–50 percent of foreign currency deposit loans in the Philippines went to nonexporters. Thailand, Indonesia and Korea, meanwhile, had a rapid build-up of short-term foreign debt.

It was inevitable that there would be some bad loans because of overinvestment in some sectors, particularly in real estate. As a result of the intense competition, profits were squeezed, projects failed and loans were not repaid. In the case of Thailand, the crisis in the financial sector was relatively widespread. This prompted foreign investors to start pulling out of the stock market. Because Thailand had a huge current account deficit at that time, the pullout of foreign money put tremendous pressure on the baht. There was no recourse but to allow the baht to depreciate sharply.

Neighboring countries were then drawn into the crisis, the so-called contagion effect. One reason was that the structure of the export sectors of Malaysia, Thailand, Indonesia and the Philippines is similar. Hence, to remain competitive with each other, their currencies must depreciate in tandem. It should be noted that when China experienced a sharp depreciation in 1994, it put competitive pressure on the Southeast Asian countries. This explanation, however, lost some of its strength when the crisis spread to Hong Kong and Korea.

The second reason for the contagion effect was that foreign investors acted like a herd in withdrawing their funds from the region. This is attributed to incomplete information on the part of the investors; they could not or did not bother to differentiate among the various economies. This type of behavior is the central theme of the literature on self-fulfilling crises.
Since many of the debts were dollar-denominated and did not carry a natural hedge against sharp deprecations, the fall in the value of domestic currencies weakened the financial viability of many projects. The situation was exacerbated by the rise in interest rates. The higher cost of money and the larger debt overhang in terms of local currency magnified the crisis and caused a downward spiral in the East Asian economies, especially Indonesia.

Some pundits contend that it was less a case of overinvestment than a case of unwise investment. This is another view of the cause of the weaknesses in the financial sector. They cite as examples the national car program of Tommy Suharto in Indonesia, the Petronas tower in Malaysia and the steel industry in Thailand. A Newsweek issue (26 January 1998) even revived the phenomenon of crony capitalism.

This analysis gives a distinct impression that some of the factors responsible for the rapid growth of East Asia were either absent or were themselves the cause of the problem. For example, promoting competition, especially through export-oriented policies, was hailed as one of the key ingredients of their rapid growth. Yet, lack of competition in the business conglomerates is seen as one of the critical failings that contributed to the crisis. Moreover, what were previously viewed as strong financial markets—able to mobilize huge flows of savings and allocate them efficiently—were then transformed into weak financial markets which sparked the economic debacle (Stiglitz 1998). And as a swipe against government intervention, some quarters contend that the close relationship forged between the bureaucracy and private sector in several of these economies to address information problems brought about political cronism and a general lack of transparency in credit allocation leading to the bad loans.

This sweeping analysis tends to gloss over the fact that similar crises have occurred in countries with sophisticated financial regulation (for example, the U.S. savings and loan debacle) and in places with high levels of transparency (for example, Scandinavia) [Stiglitz 1998]. Moreover, two-thirds of external bank lending in Indonesia were for the nonbank private sector, indicating that foreign lenders were willing to extend credit to Indonesian firms. The latter did not have to resort solely to behest loans from “friendly” domestic banks.

A third line of argument lays the blame squarely on the liberalization of the capital account and the liberalization of the banking sector as the cause of the weaknesses in the financial sector (Montes 1997). Ready access to international credit amplified existing market failures leading to the profligacy and excesses of the private sector. Both Stiglitz and Uy (1996) and Rodrik (1998) note that market failures arising from asymmetric information, incompleteness of contingent markets, and bounded rationality are endemic to financial markets.

Despite the seemingly consistent analysis, the framework rooted on financial sector weaknesses is still incomplete. The macroeconomic parameters of many of these economies (except perhaps for Thailand) did not warrant the excessive deterioration in their conditions, particularly the exchange rate. Thus, to put the entire blame on domestic policy mistakes, particularly in the financial sector, can lead to misleading policy prescriptions.

Krugman (1998) echoed this sentiment when he stated that “it is clearly wrong to blame all of overinvestment and overvaluation of assets in Asia on domestic financial intermediaries. After all, private individuals—and foreign institutional investors—did buy stocks and even real estate in all the economies now in crisis. This suggests that other kinds of market failure, notably ‘herding’ by investors, still have some role to play.” It is evident that contagion through the panic of fund managers had an impact on the economic performance of the East Asian economies.

The discussion on this subject reveals that there is still much to be learned about the present crisis before dismissing the East Asian miracle, particularly the idiosyncratic financial practices associated with some of the economies. What is clear is that the lessons from the experience of the high-performing Asian economies or HPAEs—Japan, Korea, Taiwan, Hong Kong, Singapore, Thailand, Malaysia, and Indonesia—are still valid. The crisis was caused by an aberration in the financial sector and had little to do with supply side fundamentals.

Policy Implications of the Crisis

Several lessons, however, could be drawn from the tumultuous experience during the past six months.

First, prudential regulations and supervision of financial institutions must be strengthened in order to prevent moral hazard problems. Intal and
Was the Peso Overvalued?

Despite the sharp appreciation of the peso in real terms and its adverse impact on the performance of the agriculture and manufacturing sectors, there is still an ongoing debate on whether the peso can be described as overvalued or not.

The argument against labeling the peso as overvalued revolves around the Balassa-Samuelson theorem which shows that the real appreciation of a currency can be caused by shifts in the relative prices of the tradable and nontradable sectors, which are in favor of the latter. In the Philippine case, the increase in investor confidence following the resolution of the energy crisis in 1992 and the liberalization of the capital account in that same year caused a rise in the price of nontradables. This was brought about by increased activity in this sector particularly in construction and real estate. The real appreciation could not have been brought about by a surge in portfolio capital flows as net portfolio investment was quite small even during the period after the capital account was liberalized. The only other major inflow of foreign exchange were the remittances of overseas workers but this was used to cover the trade deficit. The current account deficit was generally manageable, ranging from 3.0–4.5 percent of GDP. Hence, the appreciation in real terms was an equilibrium response to improved economic conditions.

On the other hand, movements in the nominal exchange rate show that the appreciation of the peso in real terms was directly related to its sharp appreciation in nominal terms from P29.2 in October 1993 to P24.1 in December 1994. Other Southeast Asian countries were able to prevent large changes in their nominal exchange rate. Real interest rates have always been on the high side during this period indicating that monetary policy was extremely tight. Lamberte (1995) cited the IMF-imposed ceilings on monetary variables as the culprit. Empirical evidence also shows that the Bangko Sentral ng Pilipinas was targeting the exchange rate (Gochoco 1992, Reyes and Yap 1993).

The notion that there was increased investor confidence in the Philippine economy because of major structural reforms hangs by a thin thread. As Krugman (1995) convincingly argued, the spectacular economic performance of some developing countries was based not on solid achievements, but on excessively optimistic expectations on the part of international and domestic investors or, using the terminology of Federal Reserve chairman Alan Greenspan, on their irrational exuberance. While Krugman was specifically referring to Mexico, his analysis can apply to Indonesia and the Philippines.

The initial successes that followed the implementation of economic reforms (note that the term “followed” and not “were caused by” was used deliberately) led to a speculative bubble. Krugman described this process as follows: “Markets poured money into developing countries, encouraged both by the capital gains they had already seen and by the belief that a wave of reform was unstoppable. Governments engaged in unprecedented liberalization, encouraged by the self-reinforcing conventional wisdom and the undeniable fact that reformers received instant gratification from enthusiastic investors.”

Figure 1: Equilibrium Real Exchange Rate, 1980–1997

Source: Author’s estimates
The bubble did burst for many developing countries, the major lesson being that the real currency appreciations that resulted from the apparent increase in investor confidence did not reflect changes in real exchange rate equilibria. Rather, the currency appreciations should have been interpreted as transitory in nature given the fact that they resulted from excessively optimistic expectations of international investors that were not warranted by structural economic change.

To give an empirical sense to the debate, an equilibrium real exchange rate was calculated with monthly data from 1980-1997 using the Hodrick-Prescott filter as applied by Goldfajn and Valdes (1997). The real effective exchange rate, based only on trade with major partners, was used to approximate a real exchange rate. The results are shown in Figure 1. The degree of overvaluation (undervaluation) is derived by taking the ratio of the actual value of the real exchange rate and its corresponding equilibrium value. Based on the definition of the real exchange rate index used, a ratio above 1 (below 1) indicates that the currency is overvalued (undervalued).

As shown in Figure 2, the ratio is above one for most of the sample period. The only times the ratio would dip below unity was when there was a sharp peso depreciation (October 1983, November 1990, and the second half of 1993). Thereafter, the ratio would climb back above 1 implying that the tendency is for an overvalued currency. The degree of overvaluation, however, is generally mild (in the order of 10 percent).

Given the weight of the theoretical arguments and the empirical evidence, the answer to the question posed in the title is definitely YES.

Finally, an economic blueprint can only go as far as the nation’s political will allows it. The new political administration should therefore commit itself fully to carrying the Philippine economy to new heights as it enters the 21st century.
June 12 as a Centennial Framework

Several writers and historians have forcefully argued that the Kawit Declaration of Philippine Independence on June 12 was not as politically significant as the Bacoor independence declaration by municipal presidents on August 1, 1898 or the Malolos ratification of the Kawit independence proclamation on September 29, 1898 or as internationally significant as the July 4, 1946 independence proclamation by United States High Commissioner Paul V. McNutt, the latter being duly accepted and recognized by no less than then Philippine President Manuel A. Roxas amidst a jubilant crowd and display of fireworks at the Luneta. While recognizing the circumstantial and especially the theoretical and linguistic imperfections of the June 12 declaration, I believe, however, that there is, to a significant extent, historical relevance in the said declaration in our search for a national point of reference from which centuries of numerous struggles for freedom by various ethnolinguistic groups comprising the Filipino national community may be viewed interrelatedly.

There are at least two reasons to support this tentative position.

First, the 333 years of Spanish rule (1565–1898) were marked by numerous uprisings and armed disturbances in various areas in Luzon, Visayas and Mindanao involving several, if not practically all, of the documented Christian and non-Christian ethnolinguistic groups. The outbreaks throughout Philippine history have common factors despite cultural diversity. That is, the natural love for liberty and the will to resist any external threat. This basic rationale of local and sectoral struggles was forcefully expressed in the dramatic and emotional declaration of national independence on June 12, 1898 in Kawit, Cavite by a council of revolutionaries who foresaw, and believed in what they perceived, a new nation emerging from a multicolored revolutionary past.

Second, the same people who witnessed the Kawit proclamation were also subsequently involved in perfecting the independence declaration and initiating a constitutional process through the Malolos Congress toward the establishment of a democratic republic. Thus, the revolutionary leadership assumed in theory and in spirit the existence of an independent Filipinas after June 12, 1898 that would include not just the dominant Christian majority but also the non-Christian minorities. This is shown by the designation of delegates to represent outlying communities as far as Bongao, Sulu in the South and Batanes in the North. Based on the Malolos documents, numerous areas of the archipelago were represented in the Congress with delegates—a majority of whom were Tagalogs, Pampangos, Ilocanos, and Visayans—either designated or elected. The Malolos Congress clearly envisioned an entire archipelago, from Batanes to Tawi-Tawi, that was represented in the entire process of nationbuilding and guided by the common imperative for freedom.

Thus, the national process toward the ultimate birth of a truly free Filipino nation formally and historically proceeded from the June 12 independence proclamation. The second logical landmark was the convening of the revolutionary Congress in Malolos on September 15 where two vital documents relevant to independence emerged: the ratification of the June 12 declaration of independence on September 29, and the promulgation of the Malolos documents, numerous areas of the archipelago were represented in the Congress with delegates—a majority of whom were Tagalogs, Pampangos, Ilocanos, and Visayans—either designated or elected. The Malolos Congress clearly envisioned an entire archipelago, from Batanes to Tawi-Tawi, that was represented in the entire process of nationbuilding and guided by the common imperative for freedom.

Roles of the Visayas and Mindanao in the Revolutionary Struggle

Samuel K. Tan

First, the 333 years of Spanish rule (1565–1898) were marked by numerous uprisings and armed disturbances in various areas in Luzon, Visayas and Mindanao involving several, if not practically all, of the documented Christian and non-Christian ethnolinguistic groups. The outbreaks throughout Philippine history have common factors despite cultural diversity. That is, the natural love for liberty and the will to resist any external threat. This basic rationale of local and sectoral struggles was forcefully expressed in the dramatic and emotional declaration of national independence on June 12, 1898 in Kawit, Cavite by a council of revolutionaries who foresaw, and believed in what they perceived, a new nation emerging from a multicolored revolutionary past.

Second, the same people who witnessed the Kawit proclamation were also subsequently involved in perfecting the independence declaration and initiating a constitutional process through the Malolos Congress toward the establishment of a democratic republic. Thus, the revolutionary leadership assumed in theory and in spirit the existence of an independent Filipinas after June 12, 1898 that would include not just the dominant Christian majority but also the non-Christian minorities. This is shown by the designation of delegates to represent outlying communities as far as Bongao, Sulu in the South and Batanes in the North. Based on the Malolos documents, numerous areas of the archipelago were represented in the Congress with delegates—a majority of whom were Tagalogs, Pampangos, Ilocanos, and Visayans—either designated or elected. The Malolos Congress clearly envisioned an entire archipelago, from Batanes to Tawi-Tawi, that was represented in the entire process of nationbuilding and guided by the common imperative for freedom.

Thus, the national process toward the ultimate birth of a truly free Filipino nation formally and historically proceeded from the June 12 independence proclamation. The second logical landmark was the convening of the revolutionary Congress in Malolos on September 15 where two vital documents relevant to independence emerged: the ratification of the June 12 declaration of independence on September 29, and the promulgation of the Malolos documents, numerous areas of the archipelago were represented in the Congress with delegates—a majority of whom were Tagalogs, Pampangos, Ilocanos, and Visayans—either designated or elected. The Malolos Congress clearly envisioned an entire archipelago, from Batanes to Tawi-Tawi, that was represented in the entire process of nationbuilding and guided by the common imperative for freedom.

*Director, National Historical Institute (NHI). This paper was presented in one of the sessions of the PIDS Centennial Lecture series, conducted to commemorate the observance of the centennial of the declaration of Philippine independence.

*The represented areas and their respective delegates to the Malolos Congress included the following: Zamboanga by Felipe Buencamino, Tomas Mascardo, and Lazaro Tanedo; Misamis by Teodoro Sandico, Apolinario Mercado, and Gracia Gonzaga; Calamianes by Narciso H. Resurreccion, Norberto Cruz Herrera, and S. Isidro; Batanes by Daniel Tirona and Vito Belarmino; Suring by Tomas G. Del Rosario and Timoteo Paez; Davao by Leon Guerrero and Ceferino Pantaoja; Cotabato by Jose M. Lemra and Pedro Layay Villaluz; Basilan by Juan Tuason and Jamiano Bautista; Dapitan and Lal-Lo by Jose Albert and Julio Ruiz; Paragua (Palawan) by Felipe Calderon and Domingo Colmenar; Amburayan by Mateo Gutierrez Y Ubaldio and Jose Coronel; Tagan by Lino Abaya and Fernando Ferrer, Jolo by Benito Legarda and Victor Papa; Balabac by Santiago Icasiano and Jose Zulueta; Palao by Isidro Tiongco and Alfonso Ramos; Laboc by Ramon Aviola and Manuel Aldegueza; Matti by Vicente Samosa and Urbano Morales; Malabang by Lorenzo del Rosario and Agapino Alienza; Tucuran by Telesforo Chuidian and Juan Santos; Siasi by Jose Hernandez and Alejandro Avecalla; Fatoan by Manuel Gomez Martinez and Luis Avesilla; Bongao by Sotero Laurel and Jacinto Vega; Baras by Arcadio del Rosario and Andres Tirona; Butuan by Santiago Barcelona, Alfonso and Ambrosio Delgado; and Bontoc by Fernando Canen and Mariano Noble Jose.
of a democratic constitution on January 22. Hence, the first democratic republic in Asia was introduced on January 23, 1899.

It is apparent that the political activities and decisions of the Aguinaldo leadership after the Kawit declaration were appropriate reactions of a freedom-seeking people. Said reactions refer to the resistance put up by the Filipinos against the United States’ acquisition of the Philippines following an easy American victory over the Spanish army in the battle of Manila Bay on May 1, 1898. The series of American decisions and activities were antithetical to Filipino aspirations and understandably confused and complicated the so-called Filipino–American alliance during the Spanish–American War in the Philippines.

What were these American actions that brought about the Filipinos’ resistance towards them?

"Even before the outbreak of the Revolution in 1896, Katipunan revolutionaries began arriving in the surrounding areas of Cebu and started the process of integrating the long Visayan revolutionary struggle into the Katipunan-led revolution in the Luzon area."

First, preparations for the American expeditionary forces for the conquest and occupation of the Philippines began soon after Commodore George Dewey’s victory in the Battle of Manila Bay. By the end of July, three contingents arrived in the Philippines equipped for military war.

Second, peace protocols of the Spanish–American war which started on August 10 began to end the Spanish–American conflict. One of the results of these peace protocols was the mock battle of Manila which, as noted earlier, easily led to the formal capitulation of the City by the Spaniards to the Americans on August 12 without the inclusion of the Aguinaldo government in the formalities. The more important result, however, was the conclusion of the Treaty of Paris on December 10, 1898 which provided for the Spanish secession of the Philippines to the United States for $20 million. For the second time, the Philippines was deliberately excluded despite the patriotic diplomatic efforts of Felipe Agoncillo in Paris.

Third, American military forces had begun moving by September 1898 to the Visayas while the Malolos Congress was laying down the Constitutional basis of independence and democratic government for the Philippines. The American military moves were sweetened by the oft-quoted “Policy of Benevolent Assimilation” as enunciated by President William McKinley on December 21, 1898, only to be followed immediately the next day by the American occupation of Iloilo.

On the basis of the foregoing historical observations, it appears that the June 12 declaration of independence—however imperfect it may be at that time—represented a clear, unequivocal, and strong desire of a war-torn and revolt-laden community to be free and emancipated from colonial rule. It inspired the revolutionary government of Aguinaldo to counter in a democratic manner the imperialist design of a new colonial power to weaken—internationally and domestically—the Filipino will to independence through a "carrot-and-stick" policy.

Throughout this process, what were the roles and participation of the Visayas and Mindanao?

The Visayan Freedom Struggle

Three historical landmarks determined the character and extent of the Visayan struggle for freedom during the Philippine Revolution.

The Katipunan in the Visayas

Even before the outbreak of the Revolution in 1896, Katipunan revolutionaries began arriving in the surrounding areas of Cebu and started the process of integrating the long Visayan revolutionary struggle into the Katipunan-led revolution in the Luzon area. In particular, the roles of revolutionaries such as Emilio Verdeflor of Cavite, Mateo Luga of Ilocos, Pantaleon del Rosario, Gil Domingo, and Hermogenes Peralta who became commanders of revolutionary units or factions in Cebu were crucial to the revolution in the Visayas. Especially significant was Pantaleon Villegas (Leon Kilat) of Oriental Negros who became a Katipunero in Manila while working as an acrobat in a circus company and subsequently commissioned by Emilio Aguinaldo in March 1898 to start the revolution in Cebu. The April 3, 1898 offensive in the city was impressive but was shortlived after Leon Kilat’s assassination by his own men on April 8, a Holy Friday, at about 2 a.m., as instigated by the local priest and the elite. What he began, however, spread to Carcar and other areas outside of the city and brought into the revolutionary circle all sectors of Cebu, including the ilustrado and elite.

After a series of rise-and-fall of leaders, who were plagued by multiple problems such as class interests, oppor-
tunism, personal rivalries, racial and ethnic prejudice, epidemics, fires, and criminality, took place, the revolutionary struggle crystallized along the pro-independence ideals of Arcadio Maxilom and Juan Climaco until their formal surrender between 1901 and 1902. Afterwards, only messianic and millenarian movements—sometimes labeled by colonial authorities as banditry—continued the freedom struggle, under leaders like Roberto Caballero, Petronilo Esmardo, Eugenio Alcachufas, Rafael Tagal, Mariano Abayan, Claudio Bakus, and mystic leaders such as Ponciano Elopre (Buhawi) and Papa Isio of Negros.

Meanwhile, Iloilo witnessed the ouster of Spanish rule shortly before the American occupation of the City in December 1898. Martin Delgado led the resistance against American rule. Samar and Leyte also had their share of anticolonial struggle against Spanish rule but their well-known chapter in revolutionary history was the armed struggle against the superior American military forces. Indelibly remembered is the battle of Balangiga in September 1899 wherein a dawn attack by bolomen surprised the Americans who were having breakfast in their detachments. Most of the more than 60 men were killed except a few who survived to report the most serious crack in American supremacy in the Visayas, if not in the entire archipelago. The well-known response to this massacre was the landmark American reprisal, on orders of Gen. Jacob Smith, to kill men, women, and children above 10 years of age in Samar.

Elsewhere in the Visayas, particularly Negros, the armed struggle against Spanish rule was eclipsed by the brief declaration of independence with the creation of a Negros Republic in 1899, only to be co-opted by the Negrense elite’s acceptance of American rule, the same way the elites in Iloilo and Cebu did.

**The masses in the struggle**

In the overall assessment of the Visayan freedom struggle, it is important to note that by the end of 1901, the virtually illustrado-led revolution had ended as a chapter in Philippine revolutionary history. But the freedom struggle, which antedated the Katipunan outbreak by almost three centuries, continued to plague American occupation and rule. These armed movements were led by charismatic personalities who regarded themselves as prophets, messiahs, and reincarnations of Rizal, the Holy Spirit, and Christ. The fanatical followers of these messianic movements were called in colonial reports as pulahanes, tulisanes, vagamundos, babaylanes, and other social identities. Their revival during the first decade of American rule was attributed to perceptions that the deterioration of social conditions including loss of lives due to epidemics, sickness, and destruction of the environment and properties were the result of the scorched-earth method used by the Americans in the war.

**The American factor**

The Treaty of Paris definitely gave American forces basis to claim sovereignty over the entire archipelago. The American occupation of Cebu and Iloilo by December 1898 brought superior military technology against the revolutionary government. By 1902, American control was established in the Visayas leaving the freedom struggle to the masses after the elite had been co-opted by colonialism.

**The Mindanao Freedom Struggle**

From historical, especially documentary sources, it was not until early 1897 that tangible indications of Katipunan-related activities began to appear in Mindanao although the presence of dissidents before that year could be implied from the lists of deportados from Luzon sent to various points in Mindanao, including even the remote islands of Jolo, Basilan, Siasi, Bongao, Tata’an and Cagayan de Jolo (Sulu). They formed part of the Spanish garrisons and were used to suppress local resistance and for other purposes.

**The Moro struggle**

By 1896, the profound effects of Spanish pressures and influence had not only been felt in the Christianized communities but also in the non-Christian areas including that of the Muslims. In Lanao, the Spanish military campaigns mounted by Governor General Valariano Weyler against Maranao resistance led to the final destruction of Amay Pakpak’s fort, the symbol of Maranao steadfast struggle, in Marawi and the diffusion of local resistance. The inertia of the Maguindanao armed struggle initiated by Datu Utto of Buayan had virtually dissipated by 1890. After Datu Utto retired into the security of his home in Bakat. His capitulation in 1887 led to the rise of at least two datus: Datu Piang and Datu Alunan. In several kirim manuscripts correspondences, the Maguindanao as well as the Maranao leadership was coopted politically by colonial rule. Sulu, which suffered from political erosion following the unilateral proclamation of Datu Harun Alracid (or Narassid) of Palawan as Sultan of Sulu in 1884, continued to lose leverage in foreign relations until 1893 when this Datu abdicated. Amirul Kiram, leader of the anticolonial resistance during the last decade of Spanish rule, assumed the throne as Sultan Jamalul Kiram II.

**The Indio response**

There were no radical differences or disagreements over the 1896 revolution in Mindanao. First, the repercu-
sion of the Katipunan-led revolution was not significantly felt until early 1897 mainly because of the mode and extent of communication then which was dependent on slow interisland shipping between Mindanao and Luzon and the old riverine routes and mountain trails used in internal travel. Second, the Spanish presence and impact in Mindanao were profoundly religious despite the establishment of forts in strategic points in Mindanao including Jolo, Siasi, Bongao, and Tata’an. Consequently, the withdrawal of Spanish presence after 1896 did not necessarily reduce the Spanish influence in the region. It merely entrusted the defense of Spanish interests to the religious assigned in the region, particularly the Jesuits, whose role had become crucial in the response of the Christian populace to the 1896 outbreak. Understandably, the reaction was divided and the local people were confused between choosing the Papal Flag or that of the local people were confused between choosing the Papal Flag or that of the Revolution as a rallying emblem. This was demonstrated in late 1896 in Surigao and Butuan where the Gonzales patriarch “Jantoy” and his two sons, Simon and Wenceslao, had established themselves as leaders of the revolution in Mindanao. They were supported by contingents of deportados and by mutinous members of the Spanish Army.

The Lumad reaction

There were no written records in the Lumad sector that can best describe their condition in 1896 or their role in the revolutionary struggle. From scanty sources, only the Bukidnons appeared to have been identified as being limitedly involved in the revolutionary activities. The involvement of the Manobos was not that clear either except during the time of Sultan Kudarat when the Manobo Chieftain Manakior and his warriors supported the Maguindanao overlord against Spanish troops. What seems to be clear based on some scanty accounts from travel-

“...lies in what it can offer for the present and the future...”

ers was the system of ethnic withdrawal from conflict with either Spanish forces or the Moros.

The lists of inhabitants or naturales as early as the 1850s in the archival records are clear indication of Spanish presence in the area. However, sources did not indicate if the Subanuns had been organized into government units headed by gobernadoresillos or cabezas similar to those in Dapitan, Misamis, Surigao, and Zamboanga. The organization of the Subanun homeland would not appear in Spanish records until the successful probe into the Sibuguey area by Alejo Alvarez and a companion to bring a Spanish official message to the tribal leaders. One result of the determined efforts of the Spaniards to restructure the Zamboanga peninsula in accordance with Spanish policy was the Treaty of 1896.

Conclusion: History and Destiny

The Philippine centennial brings together the past and the future in nationbuilding. It links history and destiny as interrelated and, in a sense, interdependent concepts. History, by the nature of its academic focus, provides insights into the past as early as historical sources allow. It portrays people, events, and realities far beyond the reach of human memory. The value of the past to man, however, lies in what it can offer for the present and the future. The activities of the centennial anniversary are the means to achieve this end.

Necessarily, the centennial story begins from the last decade of the 19th century when Philippine history took a dramatic turn with significant changes altering the patterns of development in the archipelago and paving the way for the outbreak of the Revolution in 1896. It was from this focal point of history that makes the centennial consciousness the motive force behind nationbuilding.

The colonial era is long gone but colonialism still continues, not in Spanish nor American forms, but in a Filipino neocolonial raiment that is more subtle and difficult to deal with. In a sense, a new frailocracy is emerging, a new form of exploitation and oppression of the poor and marginalized sectors. It is in this context where we see the relevance of our centennial activities and the need to remind the Filipino people of the unfinished reform movement.

The same reality applied to the Revolution from 1896 to 1913 which brought together the social classes to fight for a common cause to attain complete national independence, from Batanes to the Muslim South, by overthrowing the colonizers through armed struggles. The love for freedom and the determination and will to achieve it, regardless of the loss of lives and resources, is one of the enduring legacies of the Revolution and the most valuable element in our centennial celebration.

Undoubtedly, the contributions of the Visayas and Mindanao areas to the freedom struggle were impressive and cannot be ignored. There might be no colonial power to overthrow anymore but there are many manifestations of neocolonial structures and forces that threaten the freedom we are currently enjoying. It is in the protection and preservation of our freedom where the centennial celebration derives its meaning and importance. This should be the motivation for the future that we, as Filipinos, want.
Officials come and go. This is a reality in government organizations where leaders have fixed terms of office. Thus, with the entry of a new administration under President Joseph Ejercito Estrada, two economists who are closely linked with the Philippine Institute for Development Studies (PIDS) took on new directions and faced new challenges.

The Institute recently bid farewell to Dr. Cielito Habito and Dr. Benjamin Diokno. Dr. Habito ended his term of office as Secretary for Socioeconomic Planning and Director-General of the National Economic and Development Authority (NEDA). As NEDA Chief, he was appointed by President Estrada as Secretary of the Department of Budget and Management (DBM).

Dr. Habito had a relatively short yet distinguished service in the government. After being in the academe for 15 years, teaching at the University of the Philippines–Los Baños, he joined the NEDA in 1990 as Assistant Director-General. He was promoted the next year to Deputy Director-General and, after another year, was named by then President Fidel Ramos as Secretary of Socioeconomic Planning and NEDA Director-General. The appointment made Dr. Habito the youngest member of President Ramos’ Cabinet. Concurrently, Dr. Habito was the Chairman of the Commission on Population and the Philippine Council for Sustainable Development.

Even as a student, Dr. Habito already showed great promise—he graduated with honors at the Philippine Science High School, a *summa cum laude* at UP Los Baños, and received masters and doctorate degrees from the Harvard University. After his Cabinet stint, Dr. Habito is taking it easy: he reads a lot and does some research occasionally.

Dr. Diokno, on the other hand, has been serving in various government positions for the past 12 years. He is already familiar with the Budget and Management portfolio since he was the Department’s Undersecretary from 1986 to 1991. In addition, he was the Director of the Board of the Philippine National Oil Company (PNOC) from 1988 to 1991 and subsequently its Chairman and CEO in 1991, Chairman of the Local Water Utilities Administration (LWUA) from 1988 to 1991, Vice-Chairman of the National Statistical Coordination Board (NSCB), and Fiscal Adviser in the Office of the Senate President from 1993 to 1995. He was also a member of the PIDS Board of Trustees for 10 years (1988–1998). Dr. Diokno earned his bachelor and masteral degrees in economics from the University of the Philippines. He obtained another masteral degree in Political Economy from Johns Hopkins University in Maryland and a doctorate in Economics from the Maxwell School of Citizenship and Public Affairs of Syracuse University in New York.

With their new assignments in and out of government, these two distinguished economists will surely be missed not only by their respective staff in their previous organizations but the whole Institute as well who have looked up to them for being two of the more dedicated and brilliant economists in the Philippine government. BFG
Llanto (1998) list some specific recommendations:

- Strengthen prudential regulation and supervision by implementing comprehensive risk-based assessment and supervision instead of focusing primarily on credit risk. In addition, there is a need for more stringent information disclosure requirements, adequate accounting and auditing standards, as well as clearer rules and greater transparency in asset classification and provisioning.

- Review the policy on capital accounts and foreign borrowing. It would be useful to look into the Chilean case which entailed stricter rules on domestic firms’ borrowing directly abroad (such as the minimum credit rating rule), the imposition of reserves on short-term foreign currency deposits by nonresidents and other short-term portfolio flows, and a one-year residency requirement on foreign direct investment. Furthermore, dollar lending from FCDs to unhedged borrowers must not be allowed.

Second, the timing, extent, and pace of the twin liberalizations, including trade liberalization, should be reviewed. It is not surprising that since 1980 when financial liberalization was begun in earnest around the world, the number of BOP crises associated with banking crises increased (Kaminsky and Reinhart 1996). Public authorities would do well not to let the ideology of liberalization obstruct the specific objectives of monetary policy—the sound development of the financial system and the increase in the productivity of investment (Montes 1997). In this regard, measures should be implemented to regulate the flow of short-term capital although this is closely related to the second recommendation of Intal and Llanto (1998).

Finally, the behavior of the international private sector should be examined. First, international lenders must be more prudent and not be swayed by herds nor be afflicted with disaster myopia. Second, foreign investors should be encouraged to hedge at least the currency risk of their investments to prevent sudden withdrawals from domestic capital markets (Montes 1997). But beyond this, the current situation where there is simply too much liquidity in the global system should be corrected. This situation encourages very short-term investment and fuels speculative activity which generates the volatility that makes globalization a threat instead of a challenge and an opportunity.

References


After the recent devaluation of the Russian ruble, there is a growing agitation among Southeast Asian countries over the possibility of China’s currency, the renminbi, to follow suit. If and when the Chinese finally decides to devalue the renminbi, the consequential effects of a contagion would most likely bring about additional jitters to the already shaken financial landscape of the region.

In a study presented at the Philippine Institute for Development Studies (PIDS) by Dr. Johanna Ruivivar, an economist from PARIBAS (a New York-based investment consultancy firm), the possibility and scenario of the renminbi’s devaluation and its effects on the region’s financial status were discussed.

Dr. Ruivivar said that in a worst-case scenario, Chinese devaluation might bring about the depreciation of the peso from between P45 to P55 to the U.S. dollar while the Indonesian rupiah may plunge down to a staggering R20,870 the U.S. dollar.

During her presentation, Ruivivar delved on the current overvaluation of the Chinese renminbi, a concern where most of the apprehension for an impending renminbi devaluation is rooted. Dr. Ruivivar noted that an analysis of the data shows how the renminbi is currently overvalued by as much as 15 percent of its real exchange rate.

“From January 1994 to December 1997, the renminbi remained undervalued relative to its equilibrium value by an average of 15 percent. However, the renminbi has since become overvalued. Today the degree of overvaluation has increased from 15 to 9 percent in January 1998,” she illustrated.

Nevertheless, she said that there is no immediate cause for alarm. While the renminbi overvaluation is indeed placed at 15 percent, Ruivivar defined a level of 25 percent as the threshold degree of overvaluation. To effect a worst-case scenario for a possible devaluation of the renminbi, two alternative prerequisites are necessary. One is if the Japanese yen is devalued to Y222 to the U.S. dollar, or another is where all Asian currencies depreciate at the same rate as the yen, from U.S.$1:Y137 to U.S.$1:Y185.

Moreover, she noted that the renminbi’s overvaluation is not necessarily the only consideration for the Chinese to effect a devaluation. “The ultimate decision to devalue the renminbi will involve a political dimension and be driven by the prospects for export market growth and capital inflows as well as export competitiveness,” Ruivivar explained.

At present, competitiveness of the renminbi has not yet hampered Chinese exports significantly. The U.S. import growth from China, while down, nevertheless remains robust. Figures show a marked increase of 18 percent in the first five months of 1998. Comparatively speaking, U.S. import growth from problem economies in Asia is low and in some cases negative, as in the case of Indonesia.

In conclusion, however, Dr. Ruivivar acknowledged the limitations of the study. “The paper limits its focus (largely) to measuring renminbi overvaluation. The broader question of whether or not China will devalue is based upon parameters beyond the (actual) scope of this analysis.”

Will China Devalue its Currency?