The Politics of Economic Reform in the Philippines: The Case of Banking Sector Reform between 1986 and 1995

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Abstract

This thesis is about the political economy of the Philippines in the process of recovery from the ruin of economic crisis in the early 1980s. It examines the dynamics of Philippine politics by focussing on banking sector reform between 1986 and 1995. After the economic turmoil of the early 1980s, the economy recovered between 1986 and 1996 under the Aquino and Ramos governments, although the country is still facing numerous economic challenges. After the "Asian currency crisis" of 1997, the economy inevitably decelerated again. However, the Philippines was seen as one of the economies least adversely affected by the rapid depreciation of its currency.

The existing literature tends to stress the roles played by international financial structures, the policy preferences of the IMF, the World Bank and the US government and the interests of the dominant social force as decisive factors underlying economic and banking reform policy-making in the Philippines. However, the excessive focus on these factors limits our ability to examine economic reform policy-making since they depict Philippine politics as a process in which policy outcomes are determined by relatively immediate expressions of either foreign-rooted or socially-rooted demands.

This thesis will offer an alternative view, by seeking to show the merits of an approach which locates "policy elites and institutions" at the centre of the analysis of banking reform policy-making. It will be argued that the decisions of policy elites, including the President, legislators and state officials (Central Bank officials), and the interactions among them, which are affected by changing political institutions, are vital to explanations of the success or failure of banking reform. Political institutions strengthen or weaken the interests and capacities of presidents, the centre of Philippine government, in promoting reforms in the banking sector.

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List of Abbreviations

ADB	Asian Development Bank
ADFU	Apex Development Finance Unit
APEC	Asia-Pacific Economic Cooperation
AFTA	ASEAN Free Trade Area
APT	Asset Privatisation Trust
ASEAN	Association of Southeast Asian Nations
BF	Banco Filipino
Bancom	Bancom Development Corporation
BAP	Bankers Association of the Philippines
BOI	Board of Investments
BIR	Bureau of Internal Revenue
BPI	Bank of the Philippine Islands
BSP	Bangko Sentral ng Pilipinas
CB, CBP	Central Bank of the Philippines
CDCP	Construction Development Corporation of the Philippines
CMA	Central Monetary Authority
Combank	Commercial Bank of Manila
DBP	Development Bank of the Philippines
DOSRI	Directors, officers, stockholders and related interests
ECB	expanded commercial bank (universal bank)
E.O.	Executive Order
FEBT	Far East Bank and Trust Company
GATT	General Agreement on Trade and Tariffs
GDP	Gross Domestic Product
GNP	Gross National Product
Genbank	General Bank and Trust Company
GSIS	Government Service Insurance System
Herdis group	the diversified conglomerate of Herminio Disini
IBAA	Insular Bank of Asia and America
IBP	Interim Batasang Pambansa

IMF	International Monetary Fund
Interbank	International Corporate Bank
ISI	import-substitution industrialisation
KBL	Kilusang Bagong Lipunan (New Society Movement)
KKK	Kilusang Kabuhayan at Kaunlaran (Movement for Livelihood and Progress)
LBP	Land Bank of the Philippines
LCs	Letter of Credits
L.O.I.	Letter of Instruction
LP	Liberal Party
Manilabank	Manila Banking Corporation
Metrobank	Metropolitan Bank and Trust Company
MHS	Ministry of Human Settlements
Overseas, OBM	Overseas Bank of Manila
NISA	National Intelligence Security Agency
NDC	National Development Corporation
NEDA	National Economic Development Authority
NICs	newly industrialising countries
NP	Nationalista Party
OBU	Overseas Banking Units
PBC or PBCommerce	Philippine Bank of Commerce
PCA	Philippine Coconut Authority
PCIB or PCIBank	Philippine Commercial and Industrial Bank, after 1983, Philippine Commercial and International Bank
PCCI	Philippine Chamber of Commerce and Industry
PCGG	Philippine Commission on Good Government
P.D.	Presidential Decree
PDIC	Philippine Deposit Insurance Corporation
PDCP	Private Development Corporation of the Philippines

Philexport	Philippine Exporters Confederation
Philfinance	Philippine Underwriters Finance Corporation
Philsucom	Philippine Sugar Commission
Philtrust or PTC	Philippine Trust Company
PISO	Philippine Investments Systems Organisation
PNB	Philippine National Bank
R.A.	Republic Act
RCBC	Rizal Commercial Banking Corporation
SEC	Securities and Exchange Commission
SGV	Sycip, Gorres & Velayo (a prominent Manila accounting and business consulting firm)
SSS	Social Security System
UCPB	United Coconut Planters Bank
unibank	universal bank (expanded commercial bank)
USAID	U.S. Agency for International Development

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Chapter 1.
Introduction:
The Recovery and Reform of the Philippine Banking Sector

Introduction

This thesis examines banking sector reform in the Philippines between 1986 and 1995, the period of economic recovery after the economic and banking crisis of the early 1980s. By the late 1990s, the Philippines was seen as the "sick man of Asia", left behind by countries such as Singapore, Korea, Taiwan, Thailand, Malaysia and Indonesia. The failure of the Philippine economy in comparison with other Asian countries has been discussed by many observers.[1] However, there are still very few studies devoted to the recovery of the mid-1990s and the relative stability of the economy after the currency crisis.[2]

After the serious economic turmoil of the early 1980s, the economy recovered between 1986 and 1996 under the Aquino and Ramos governments, although the country is still facing numerous economic challenges. "Crony Capitalism", the word originally created to describe presidential cronyism under the Marcos dictatorship in the Philippines, is more often used as a general word to refer to Asian (or developing) countries in the late 1990s (see Kang, 2002). In the Philippines, various market-oriented reforms have been implemented and the state regulatory framework has been improved since the economic and banking crisis of the early 1980s. The Philippines is seen as a country which vigorously implemented liberalisation reforms in the 1990s.[3]

After the "Asian currency crisis" of 1997, the economy inevitably decelerated again. However, the Philippines was seen as one of the economies least adversely affected by

[1] For example, see Hutchcroft (1998), Haggard (1998), Bowie and Unger (1997), Jayasuriya (1995), Lindsey (1995), Rivera (1994), Yoshihara (1994), Broad (1988), and Hawes (1987).

[2] For example, see MacIntyre (2001), Haggard (2000), Noland (2000) and Kang (2002).

[3] According to a new index by A.T. Kearney, a consulting firm, the Philippines had the most rapidly "globalising" economy in 1993-1997 (cited in *The Economist* April 8th 2000:144). This is measured by variables such as openness to trade and investment, credit-worthiness and the importance of tourism and transfers from foreign workers.

the rapid depreciation of its currency.[4] In terms of economic growth, the Philippines has never recorded a high growth rate continuously. Poverty and unemployment are still a serious cause for concern. There are still many examples of favouritism, corruption and ineffectual state regulation in the banking sector.[5] In early 2001, President Estrada was forced to leave the palace after misconduct was revealed.[6] Yet, in spite of the dramatic political events fuelled by the financial scandal, the Central Bank was able to maintain relative monetary and banking stability although the political turmoil damaged a big commercial bank which had close links with the scandal. In this context, this thesis examines the politics of banking reform in the process of economic recovery after the economic crisis of the early 1980s.

In the last two decades, the existing literature on the Philippine political economy has been obsessed with one question: why was the Philippine economy left behind by other Asian countries including Korea, Taiwan, Singapore, Thailand, Malaysia and Indonesia? In order to understand the continuing failure of the economy and related policy reform in the Philippines, the existing literature tends to stress the roles played by international financial structures, the policy preferences of the IMF, the World Bank and the US government[7] and the interests of the dominant social force as decisive factors underlying policy-making in the Philippines. With regard to the Philippine state, most studies have focused on the "weakness" of the state and the "strength" of the dominant social force (or oligarchy).[8] International influences and the effects of social forces are important variables when explaining economic policy reform. However, the excessive focus on these factors limits our ability to examine economic reform policy-making since they depict Philippine politics as a process in which policy outcomes are determined by relatively immediate expressions of either foreign-rooted or socially-

[4] See, for example, Sicat (1999), Intal (1998) and Lim (1998).

[5] For the Estrada cronyism, see, for example, Coronel (ed.) (2000).

[6] For a report on the impeachment, see, for example, Hutchinson and Tordesillas (2001).

[7] See Payer (1974), Bello, Kinley and Elinson (1982) and Broad (1988).

[8] See, for example, May (1998), Hutchcroft (1998), Haggard (1998), Bowie and Unger (1997), Jayasuriya (1995), Lindsey (1995), Rivera (1994), Yoshihara (1994), Broad (1988), and Hawes (1987). Doronila (1992), which draws more attention to the state in the process of industrialisation, is a notable exception, although it recognises the "weakness" of the state.

rooted demands.[9]

This thesis will offer an alternative view, by seeking to show the merits of an approach which locates "policy elites and institutions" at the centre of the analysis of banking reform policy-making. It will be argued that the decisions of policy elites, including the President, legislators and state officials (Central Bank officials), and the interactions among them, which are affected by changing political institutions, are vital to explanations of the success or failure of banking reform. Political institutions strengthen or weaken the interests and capacities of presidents, the centre of Philippine government, in promoting reforms in the banking sector. Both foreign-rooted and socially-rooted demands are influential in banking reform policy-making, but these are mediated by political institutions and influence the decision of policy elites.

The main focus of this study is the commercial banking sector, the largest segment of the banking sector and the financial sector as a whole in the Philippines. The restoration of relative stability in the banking sector alone cannot lead to high economic growth rates. Economic development is obviously a more complicated process than banking sector development. Banking sector reform is only one example of economic reform. Each area of economic reform whether it be agrarian, budget, tax, trade or infrastructure reform, is closely associated with its own unique set of economic and political factors. However, in the Philippines banking sector reform especially is critical to any attempt to understand economic reform and politics. The stability and performance of the banking sector is closely connected with the macro-economy (see Bautista, Ybañez and Agulto, Jr.,1995:16-22). Banks have close connections with all businesses and their lending decisions have a strong impact on businesses (see Gochoco-Bautista and Reside,

[9] Studies which depart from this dominant trend in an attempt to understand the dynamic changes in state and society and the complexity of their interaction in the policy-making process, have just started to emerge. See, for example, Magadia (1999), Eaton (2002) and Montojo (1998). For studies which focus more on the process of policy-making, see Ateneo Centre for Social Policy & Public Affairs (1997) and Third World Studies Centre (1994). de Guzman (ed.) (1963) is a pioneering work on the decision-making of policy choice in the Philippines. Interesting studies which are more concerned about societal actors are also emerging. For example, the important role of NGOs in Philippine politics is examined by Clarke (1998) and a critical social movement in elections is analysed by Hedman (1998). For a recent study of political leadership in local politics, see Kawanaka (2002).

2000). As creditors, banks play an important role in corporate governance. Importantly, during the period in question banking reforms were guided by two key principles of economic reform: liberalisation and the strengthening of the state regulatory framework.

In its analysis of banking reform policy-making, this thesis distinguishes between two types of reform: structural and regulatory reform. The working definition of structural reform is reform which entails changes in the existing laws through the legislative process. In particular, amendments of two key laws, namely the Central Bank Act (R.A. 265) and the General Banking Act (R.A. 337) which had provided the legislation necessary for the monetary and banking sector regulation from 1949, can be seen as critical structural reforms. Regulatory reform is defined as reform which can be implemented by the Central Bank within the existing legal framework.

The following section of this introductory chapter will examine the developments and reforms of the banking sector after the economic and banking crisis of the early 1980s. Although weaknesses remain, the banking sector has successfully undergone various changes facilitated by reforms. After reviewing the existing literature on economic and banking reform policy-making, issues relating to "policy elites and institutions" will be explored. The final section will provide an overview of changing political institutions and banking reform in the Philippines.

Developments and Reforms in the Banking Sector since the Early 1980s

The Philippine banking sector has long been seen as a symbol of the country's failed economy. Banking frauds, including behest loans and DOSRI (directors, officers, stockholders and related interests) loans, and the cartel-like behaviour of the big banks have been identified as the main obstacles to effective financial intermediation in the Philippines. For example, in his influential study, Hutchcroft (1998) stresses the continuing role of "rampant favouritism" and "ineffectual state regulation" in the Philippine banking sector as typical of the failed economy. As many studies suggest, however, despite the remaining weakness, the Philippine banking sector was showing

visible improvements by the mid-1990s. Although banking frauds remained a potential threat to financial stability, as in other developing and developed economies, the level of fraudulent loans and financial distortion which had reached a peak in the late Marcos dictatorship, fell in the 1990s. After the economic and banking crisis of the early 1980s, the banking sector underwent radical changes facilitated by various policy reforms, although the relatively successful implementation of reforms in the 1990s has not guaranteed the development of a stable and effective banking sector in the following decades.

Although the level of financial development in the Philippines was not impressive in comparison with Korea, Singapore, Thailand and Malaysia, the financial sector showed strong growth in the mid-1990s. Various monetary and financial indicators improved. The ratio of M3 to GNP increased from 0.25 in 1986 to 0.41 in 1998 (Gochoco-Bautista,1999:39-40,Table 3). The share of deposits to GNP rose rapidly between 1986 and 1995, from 27.95 per cent to 52.46 per cent (Intal and Llant,1998:Table 3). It is true that Gross Domestic Saving (GDP minus consumption by both private and public sectors) is still low in comparison with other ASEAN countries such as Singapore, Malaysia and Thailand. However, as Ravalo (1998) points out, the relatively low Gross Domestic Saving, which is closely connected with the level of the GDP, cannot be seen as a simple indicator of the inefficiency of the banking sector. The relatively low level of GDP growth cannot be explained by the inefficiency of the banking sector alone.

All the assets, domestic credits and deposits of the financial system steadily increased between 1987 and 1997 (see Table 1-2). As the economy recovered, the size of the banking sector expanded. The total assets of the commercial banks increased from 264,635 million pesos in 1986 to 1,347,362 million pesos in 1995 (see Table 1-3). The number of branches also expanded. In 1986, 33 commercial banks had 1,589 branches and in 1995, 48 commercial banks had 3,152 branches (see Table 1-4). Increases in bank profits can be seen as a sign of recovery from the brink of collapse. Between 1983 and 1986, huge losses and non-performing assets were registered in the banking sector, mainly due to the problems of the state-owned Philippine National Bank (PNB) and Development Bank of the Philippines (DBP), which occupied a large share of the

banking sector. In 1986, the commercial banks recorded 2,607 million pesos in total losses. By contrast, in 1995 the total profits of the commercial banks amounted to 25,906 million pesos (see Table 1-5). The asset quality of the banking sector had also improved by 1997. The proportion of non-performing loans (NPLs) decreased to 2.8 per cent in 1996 from 22.6 per cent in 1985 (see Table 1-6), although asset quality declined after the currency crisis. In commercial banks, NPLs had risen to 12.3 per cent by 1999 and to 15.1 per cent by the end of 2000 due to slower economic growth and market instability, although some part of the deterioration reflected tighter reporting standards.[10] Private commercial banks have become less reliant on credit from the state. Recent studies on the banking sector reveal a significant shift in the liability structure of the commercial banking system towards much greater reliance on deposits and less dependence on borrowings.[11]

The banking sector was seen as typical of a Philippine business sector dominated by a small number of elite families (oligarchy) who made large profits at low risk due to close familial ties with power holders in the state and other businesses (see Hutchcroft,1998). However, by the 1990s the banking business was no longer an easy business in a highly-protected environment. The structure of the banking sector changed rapidly as a consequence of policy reforms. Under the Aquino government, the role of state banks, which had been predominant under the Marcos dictatorship, became much smaller, although they are still large players in the banking sector. In the early 1990s, the Central Bank started to facilitate competition among banks by easing the tight regulation on the opening of new domestic banks and branches of banks, while it maintained the conservative prudential regulations. Under the Ramos government, competition among banks was further encouraged by the entry of new foreign banks, a development which would have been unthinkable in previous decades.

In the 1990s, the banking sector was forced into a more competitive environment by changes in regulation, although excessive competition became a potential threat to the stability of the financial system. Under the more liberalised environment, increasing

[10] For the analysis of the banking sector, see World Bank (document) (2002:34-37).

[11] See Bautista, Ybañez and Agulto, Jr., (1995:26) and Intal and Llant (1998:16-17).

competition among banks, in particular among big commercial banks, was observed.[12] Although the entry of new foreign banks was allowed under the terms of the restrictive guidelines, the effect of this was to facilitate competition among the top domestic banks, which were supposed to be dominated by the "oligarchy". Big commercial banks were forced to extend their business to middle markets and to consumer markets such as car and home loans. Smaller banks also tried hard to acquire more savings and to expand their business. Philippine banks faced fierce competition to gain larger market shares in diverse business activities and to acquire deposits (cheap funds).

In the 1990s, the structure of the banking sector differed significantly from that of the first half of the 1980s (see Table 1-7). The large profits of the top private commercial banks during the economic recession of the early 1980s clearly showed the distortion of the banking sector. By the late 1990s, in a more competitive business environment, further mergers among big commercial banks such as Philippine Commercial and International Bank (PCIBank) and Equitable Bank, and Bank of the Philippine Islands (BPI) and Far East Bank and Trust Company (FEBT) showed that a new era had dawned in the banking industry. Today, there is no single expanded commercial bank which serves entirely the needs of a particular business group, although business connections through large shareholders play an important role in the banking business. The banking business is still profitable for well managed banks, but there is no indicator which shows the continuation of the structure which secured "enormous profits" for banks in the 1990s. After the currency crisis of the late 1990s, the ROE (Return on Equity) of banks rapidly decreased in response to the low economic growth. The ROE of the Philippine banking system declined from 12.42 per cent in 1997 to 5.81 per cent in 1998 (see Gochoco-Bautista,1999:44, Table 5).

The question of the high intermediation costs is a contentious issue among economists. However, there is little evidence to show that the high level of intermediation costs in the 1990s can simply be seen as a "powerful testimonial to oligopolistic power" (Hutchcroft,1998:230). The slow process of reducing intermediation costs should be understood in conjunction with other regulatory policies such as relatively high reserve requirements and tax policy, and macro economic policy, especially foreign exchange

[12] See Hapitan (2001), Unite and Sullivan (2001) and Manzano and Neri (2001).

policy (see Manzano and Neri, 2001). Expanding client base in retail banking potentially increased lending rates since new borrowers of car and home loans inevitably brought higher risks in comparison with the traditional borrowers of big commercial banks such as big corporations and very rich individuals.

With regard to the development of the banking sector, it should also be noted that the banking sector now has a more reliable regulator, namely the Bangko Sentral ng Pilipinas (BSP). In 1993, the huge debts of the old Central Bank were finally liquidated by the establishment of this new monetary authority. The new Central Bank has greater regulatory powers and independence as a monetary authority through the new legislation, although coordination between fiscal and monetary policy is still a contentious area. In addition to reducing its role in development finance by changing the composition of the Monetary Board, its core decision-making body, the new BSP has more successfully distanced itself from political affairs than its predecessor. Better protection of bank officials from legal action has also been provided. In terms of handling insolvent banks, the heavy burden of the Central Bank has been reduced as the role of the Philippine Deposit and Insurance Corporation (PDIC) has been enhanced. The Central Bank was streamlined by the organisational reforms, and the salaries of Bank officials were increased. The reform of the Central Bank can be seen as a critical factor in maintaining macro-economic stability after the currency crisis.

The BSP has maintained a good reputation as a regulator among the business community both inside and outside the Philippines. According to the surveys of the Makati Business Club (MBC) and the Philippine Chamber of Commerce and Industry (PCCI), the BSP was the best performing government institution in 1996. A business magazine, *Asiamoney,* chose BSP governor Gabriel C. Singson as the "Central Bank Governor of the Year 1996". The BSP maintained its good reputation after the currency crisis. In the Philippines, it is often said that corruption is widespread, but in terms of the monetary authority, there have been few specific charges of (or rumours about) corruption in the late 1990s. Although the notion of "reputation" is changing in nature, particularly in the Philippines, the restoration of the Central Bank's reputation as a monetary authority in the mid-1990s was a critical step towards monetary and banking

stability.

After the currency crisis , as is broadly recognised, the Philippines had a more stable banking sector than Korea, Thailand, Malaysia or Indonesia. Although the public was burdened with the huge costs of the failure of the banking sector under the Marcos dictatorship, the Philippines was one of the countries in the region which was able to avoid the use of large public funds to restore financial stability after the currency crisis. Since the economic crisis of the early 1980s, the Central Bank has adopted a more assertive attitude towards regulating the banking sector. The minimum capital requirement for banks has been steadily increased to improve the stability of the banking sector. Every commercial bank must also maintain a high capital adequacy ratio, defined by the Central Bank as the ratio of net worth (capital account) to risk assets. In 1992-1997, the capital adequacy ratio stayed within the range of 16.9 per cent to 20.2 per cent (Intal and Llant,1998:18, Table 5). This is twice as high as the Bank for International Settlements (BIS) requirement of 8 per cent. After the foreign exchange liberalisation, the risks which the public sector might shoulder have largely been reduced. Foreign exchange losses were one of the main causes of the enormous cost of maintaining the financial system. Learning from past experience, the new Central Bank has cautiously maintained the foreign currency accounts in surplus.

Another critical development was that of the 1998 Presidential election which was the first not to seriously damage monetary stability in the Philippines, although there had been some positive signs in the previous election. Although election-related murders and fraud are still serious threats to Philippine democracy, maintaining macro-economic stability in an election year had been a long-term "dream" for the monetary authority after repeated experiences throughout post-war history of macroeconomic instability caused by excessive spending during presidential elections. In this context, this thesis seeks to solve one of the puzzles of the Philippine political economy: why were the Aquino and, more importantly, Ramos governments able to implement important banking reforms which contributed to the restoration of monetary and banking stability?

Explaining Economic and Banking Reform Policy-Making

Banking policy reforms have been mainly examined by economists.[13] These studies provide valuable insights into the developments, reforms and problems of the banking sector. Obviously, this thesis has also drawn a great deal on these insights. There are still problems in the banking sector and in the macro economy, most notably the relatively high banking spreads (intermediation costs) and the low level of Gross Domestic Saving (GDS). The Central Bank continues to face difficult challenges in its efforts to develop a stable and effective banking sector in the context of unstable international financial markets. However, the recovery of the banking sector after the economic crisis, the important shift toward liberalisation and the significant improvement of regulatory policy have been largely recognised and discussed by economists. In particular, after the currency crisis, the various banking reforms of the second half of the 1980s and the early 1990s have been seen as an important factor contributing to the relative stability of the banking sector despite the economic shocks.[14]

However, the main concern of economic literature is banking policy review, and the effects of various liberalisation measures and regulatory reforms.[15] In these analyses, banking reform policy-making is largely seen as a matter of technical choice, although there is a recognition of the importance of political factors in monetary and banking stability.

With respect to the liberalisation of the banking sector, the main concern of economists is the effect of liberalisation measures on the domestic banking sector. The causes of liberal reform and the process of forming and implementing reform have been rarely

[13] See, especially, Intal and Llanto (1998), Lamberte and Llanto (1995), Paderanga (1996) and Bautista, Ybañez and Agulto (1995). For the growing literature on the Philippine banking sector after the currency crisis, see Gochoco-Bautista (1999), Gochoco-Bautista and Reside (2000), Canlas (2000), Intal, et al. (1998), Lim (1998), Noland (2000) and Sicat (1999).

[14] For example, see Gochoco-Bautista (1999:32), Canlas (2000:37), Intal, et al. (1998:154), Sicat (1999:44) and Intal and Llanto (1998:2).

[15] For debates on the effects of the entry of new foreign banks, see Hapitan (2001), Unite and Sullivan (2001) and Manzano and Neri (2001). For recent studies on banking regulation, see Lamberte (2002), Milo (2001) and Milo (2002).

discussed by economists.[16] Since the early 1980s, the importance of liberal reform has been recognised by local economists and encouraged by the IMF, the World Bank and the US government, but the implementation of liberal reforms has never been smooth. To understand the successes or failures of liberal reforms, changing political factors need to be placed at the centre of the analysis.

With regard to regulatory reform, for example, Lamberte (2002) has examined extensively the significant changes in the role of the Central Bank, in particular after the establishment of the new Central Bank, Bangko Sentral ng Pilipinas (BSP). However, with respect to the causes of the Central Bank reform, the study simply points out the important contribution of the Legislature under the Ramos government in establishing the new Central Bank, without examining the policy-making process (see Lamberte,2002:8). The urgency of the Central Bank reform had been recognised since the mid-1980s. Yet, the implementation of the Central Bank reform was a turbulent process. As Lamberte notes, the leadership and commitments of legislators, particularly senators, were crucial in the successful implementation of the Central Bank reform, but these should be understood in the broader context of changing political institutions. The commitment of legislators to the reform of the banking sector in cooperation with the President was strengthened by changing electoral rules under the 1987 Constitution.

Despite the significant contribution they make to our understanding of banking policy, the studies published by economists leave one important question unanswered: how and why was critical banking reform implemented under the Aquino and, more seriously, the Ramos government? Unlike the economic literature, this thesis aims essentially to examine the politics of economic and banking reform policy-making.

In his influential study, Hutchcroft (1998) examines the politics of the banking sector and uses evidence drawn from the commercial banking sector to show how the major obstacles to economic development in the Philippines lie in the political sphere. Essentially, he sees the Philippine banking sector as a typical case of rampant favouritism and ineffectual state regulation, and stresses the historical continuity of

[16] For notable exceptions, see de Dios (2000) and Alburo (1993).

these factors. He argues that the "rampant favouritism" and "ineffectual state regulation", which impede economic growth, can be understood in the context of the structure of Philippine society and the state, viewed as "a predatory oligarchy and a patrimonial state" (see Hutchcroft,1998:1-12).[17] He also claims that "[T]he favour or disfavour of those oligarchs currently holding state office is a major determinant of the relative success or failure of particular banks" (Hutchcroft,1998:8). This perspective is consistent with a broad trend in debates on Philippine politics: the stress on interpersonal relationships and their strong continuity through history (see Kerkvliet, 1995:401). Hutchcroft rightly addresses the importance of political factors in economic development but his approach leads to a limited understanding of the development, reforms and problems of the Philippine banking sector in the process of economic recovery.

First of all, the limitations of his analysis stem from a reliance on too broad a typology to explain the politics of the banking sector in the Philippines. The primary goal of his study is to "explain the Philippines' longstanding 'developmental bog'" (Hutchcroft,1998:1). Hutchcroft attempts to explain the continuing economic problems of the Philippines by employing a broad categorisation of capitalist systems. He notes that:

> "Economies are commonly expected to fall somewhere along a continuum between laissez-faire and statist models. The Philippines highlights the basic inadequacy of this popular typology, precisely because its economy does not exhibit key characteristics of either laissez-faire or statist capitalism" (Hutchcroft,1998:19).

In order to find an adequate place for the Philippines and other developing countries, he adds one more category ("rent capitalism"). He insists that:

> "The laissez-faire versus statist continuum generally highlights only one vital dimension of intra-capitalist variation: the relative strengths of state apparatuses and business interests. A second dimension, however, is just as vital: variation among state apparatuses, many of which exhibit strong patrimonial features" (Hutchcroft,1998:19).

[17] The "patrimonial framework" originated in Weber's work (1978, Vol.2, Chapter 12). For an analysis of the Philippines in the context of this framework, see also Hutchcroft (1991).

He names this second dimension "rent capitalism", which is identical with "patrimonial polity". There are two types of "patrimonial polity (rent capitalism)": "the patrimonial administrative state (bureaucratic capitalism)" and "the patrimonial oligarchic state (booty capitalism)". The Philippines is categorised as "a patrimonial oligarchic state (booty capitalism)" while Thailand and Indonesia are classified as "patrimonial administrative states (bureaucratic capitalism)".

When he comes to consider the differences between the two types, Hutchcroft notes that: "[I]n the patrimonial administrative state, the dominant social force is a bureaucratic elite - based within the state apparatus". "In the patrimonial oligarchic state, on the other hand, the dominant social force - an oligarchy - has an economic base quite independent of the state apparatus, but access to the state is nonetheless the major avenue to private accumulation". He asserts that "over the long term, obstacles to change will tend to be far more problematic in the patrimonial oligarchic state" (booty capitalism) "than in the patrimonial administrative state, or bureaucratic polity" (bureaucratic capitalism) (Hutchcroft,1998:234).

These categories of the patrimonial oligarchic state (booty capitalism) and patrimonial administrative state (bureaucratic capitalism) are offered in order to explain the failure of the Philippine banking sector in comparison with other Asian countries such as Thailand and Indonesia. However, an analysis based on this broad categorisation limits our ability to understand banking reform policy-making in the process of economic recovery in the Philippines. Despite the remaining weaknesses of the banking sector, the "patrimonial oligarchic state (booty capitalism)" was able to restore banking stability in the 1990s. The "patrimonial administrative states" of Thailand and Indonesia (Hutchcroft,1998:5), on the other hand, showed serious weakness in banking regulation in the 1990s.

Secondly, in addition to the weakness inherent in an analysis relying on such a broad typology, Hutchcroft's assertion that the Philippine elite is the most influential force in state decision-making is problematic. Essentially, Hutchcroft sees the Philippine elite as a unified social force which shares the same interests and policy preferences. He notes

that "the Philippine elite has displayed a remarkable degree of consensus on major issues of national policy, even as it fights with passion (and often violence) over the division of spoils" (Hutchcroft,1998:250). However, as he notes, throughout its history there have always been fierce conflicts among Philippine elites both in and out of the state over key policy issues. These conflicts have been an important factor facilitating (or decelerating) banking reform. In the 1950s, a fierce conflict among Philippine elites emerged over monetary policy ("the monetary policy debate") in which the most powerful faction in the country's history, namely the "sugar bloc", failed to enforce monetary policy to serve its business interests. In the 1960s, the controversy over decontrol policy witnessed a continuing struggle among Philippine elites pursuing its own business interests. As Marcos gained political power, he was at the centre of conflicts among Philippine elites in the 1960s and 1970s. Under Marcos's authoritarian rule, as the tight control of the dictatorship started to loosen in the late 1970s, fierce conflicts among Philippine elites were again revealed. As the economy decelerated, there were fierce battles among Philippine elites over fiscal, monetary and banking policy. Anti-Marcos movements among business and religious elites clearly showed the fragmentation of Philippine elites. Under the Aquino government, conflicts among Philippine elites continued. There were intense debates over key policy including foreign debt, social reform and the US bases issues. There was strong opposition to liberal reforms under the Aquino and Ramos governments.

The assumption that the Philippine elite is a powerful and uniform entity becomes problematic in the analysis of liberalisation. Since economic liberalisation potentially leads to more competition among businesses, it is very unlikely to occur if the economy is dominated by a powerful and uniform oligarchy. Thus, in Hutchcroft's study (1998), although the promotion of liberal reform as a broad policy trend under the Ramos government is acknowledged, the implementation of liberalisation in the banking sector, such as the entry of new foreign banks, is treated as a very limited measure in spite of its obvious significance. In Hutchcroft's view, the promotion of liberal reform was largely prevented by the strong interests of the oligarchy, despite the trend towards economic liberalisation in the 1990s. Yet, as noted earlier, since the mid-1980s, changes in the structure of the banking sector due to liberalisation were evident even liberal

reforms are not always helpful in developing an effective and stable banking sector.

Thirdly, Hutchcroft's excessive stress on the continuing "weakness" of the Philippine state apparatus is also problematic in terms of the analysis of the banking sector during the period of economic recovery. The establishment of the new Central Bank and the financial restructuring of the bank are simply seen as cases in which the financial mess at the Central Bank led to huge costs for the public. With regard to regulatory power and the role of the Central Bank, Hutchcroft observes "little change in the overall character of the monetary authority" (Hutchcroft,1998:211). Thus, the successful passage of the new Central Bank Act is seen as having little impact on the banking sector in Hutchcroft's study.

However, it must be noted that his assessment of the reforms stands in sharp contrast to those of other leading economists.[18] There is no economic literature which stresses the importance of the strong continuity in the banking sector and the Central Bank under the Marcos, Aquino and Ramos governments, although all observers agree that there are weaknesses remaining in the banking sector.[19] Contrary to Hutchcroft's observation, as a regulatory authority, the Central Bank has experienced radical changes in terms of its role and regulatory power since the early 1980s. The process of economic and banking recovery has been associated with the improvements of the regulatory authority under changing political institutions. In the early 1980s, under the Marcos dictatorship, the Central Bank had been very vulnerable to the direct intervention of the President. The Central Bank, which played a critical role in development finance, allocation of foreign exchange and rescue of ailing banks, was unable to maintain its autonomy from the President and political affairs. During the economic crisis, the President intervened directly in the decisions of the Central Bank to rescue ailing banks. Election-related spending reemerged as a serious threat to monetary stability. Under the Marcos government, the Central Bank was unable to restore public confidence in the banking sector. After President Aquino took power, banking reform was initiated in order to

[18] See, particularly Lamberte (2002).

[19] See, for example, Intal and Llanto (1998), Lamberte and Llanto (1995), Paderanga (1996), Bautista, Ybañez and Agulto (1995), Gochoco-Bautista (1999), Gochoco-Bautista and Reside (2000), Canlas (2000), Intal, et al. (1998), Lim (1998), Noland (2000) and Sicat (1999).

redirect policy and to eradicate the effects of Marcos's influence. Redirecting state intervention, the Central Bank facilitated the reduction of its own role in development finance. The Central Bank was able to regulate banks more independently under the new President. President Aquino, unlike her predecessor, did not intervene directly in the Central Bank's decisions. With support from the President, the Central Bank implemented liberalisation measures through regulatory reforms in the early 1990s. Under the Ramos government, the Central Bank further improved its regulatory powers through the enactment of the New Central Bank Act. The Bangko Sentral ng Pilipinas (BSP) is still facing numerous challenges under changing economic conditions, but it has secured more distance from political affairs than before due to the reduction of its role in development finance and the Monetary Board reform.

Hutchcroft (1998:208) stresses the importance of the Ramos administration's skill in allocating discretionary funds to legislators and the financial support of the World Bank in the enactment of the New Central Bank Act. However, the Central Bank reform cannot be fully understood in terms of the "old tactics" (use of discretionary funds) and the financial support of the World Bank alone. As a means to reforming the banking sector, the "old tactics" had not worked at all under the "old" Legislature between 1949 and 1972 under the 1935 Constitution. The Central Bank was established in 1949, but there was no key structural reform in the banking sector through the legislative process until the Legislature was closed in 1972, although the urgency of banking reform was evident by the late 1960s. As noted, despite generous support from the World Bank, the Aquino government failed to implement the Central Bank reform. In order to understand why the "old tactics" were effective under the Ramos government and why the government adopted the policy recommended by the World Bank, the decisions of the policy elites and the interaction among them need to be examined in the light of the changes occurring in the political institutions as a result of the 1987 Constitution, which strengthened the interests and capacities of the President in promoting banking reform.

As economists point out, there are still many weaknesses in the Philippine economy and in the banking sector.[20] Improving regulatory policy is a continuing process. In a more globalised and liberalised policy environment, maintaining banking stability

[20] See, for example, Gochoco-Bautista (1999:55-73).

becomes more difficult. The Central Bank has always been on a tightrope in terms of regulating the banking sector. The relatively successful restoration of banking stability after the financial crisis will not secure continuing stability and the further development of the banking sector. However, the key events associated with the Philippine banking sector in the process of economic recovery, including the overall restoration of relative banking stability, changes to the banking sector structure, significant changes in the role of the Central Bank, the facilitation of competition among banks through liberalisation measures and the enhancement of the Central Bank's regulatory power, can hardly be understood simply as the effects of personal favours bestowed by a dominant oligarchy.

While in Hutchcroft's study (1998), liberalisation in the banking sector is treated as a very limited measure, other observers view liberalisation as the underlying cause of the problems in the economy and the banking sector.[21] According to the studies of Bello, Kinley and Elinson (1982) and Broad (1988), the promotion of liberalisation in the 1980s has been linked to the strong influence of the IMF, the World Bank and the US government and to the close ties between these entities and technocrats in the Philippine state. In the 1990s, the strong influence of international factors on Central Bank reform was also observed by Maxfield (1997). After the end of the "Cold War" and the departure of the US military, there was a change in US security interests which was seen as an important factor mitigating the pressures from the IMF and World Bank for liberal reform during the early years of the Aquino government. Along with the global trend towards liberalisation, some observers stress this change in US security concern as a decisive factor in the promotion of liberal reform in the Philippines in the 1990s (see Hutchcroft,1998:245).

As the Philippine experience shows, foreign support has been an important factor in activating the interests of policy elites in promoting economic and banking reform. Nevertheless, the promotion of liberal policy reform in the banking sector and other sectors in the Philippines can hardly be seen simply as a response to policies enforced by foreign governments and financial institutions. The successes and failures of

[21] See, for example, Bello (2000). For the negative impact of liberalising the banking sector on employment, see IBON Facts & Figures, 15 & 31 December 2000, "Philippine Financial System".

banking reform in the Philippines cannot be wholly explained by reference to foreign pressures centred on US interests. It is important to recognise that the policy elite, including the President, legislators and state officials, have not simply served foreign interests. Despite a strong trend towards financial liberalisation in the 1990s, banking regulation, foreign exchange policy, the structure of the banking sector and the level of financial stability varied across Asian economies, as many studies of the Asian economic crisis show.[22]

During the economic crisis of the early 1980s, in spite of strong pressure from the IMF and the World Bank, the Marcos government repeatedly delayed the implementation of stabilisation measures based on economic orthodoxy due to an internal political factor, namely the 1984 legislative elections. The government did not implement liberal reforms in the coconut and sugar industries during the Marcos Presidency despite enormous pressure from the IMF and the World Bank because the President was determined to protect the interests of his close allies. The US seemed to be supportive of the Marcos government, but the IMF and the World Bank largely maintained their stance in terms of policy conditionality. Lack of foreign funds due to the strict position of the IMF and the World Bank further weakened the US-backed President Marcos. The restructuring of state banks was eventually to become the first step towards liberal reform in the banking sector. However, the Marcos government blocked such reform, ignoring the advice of the governor of the Central Bank, the Minister of Finance, the IMF and World Bank.

The Aquino government, on the other hand, selectively implemented the economic reforms recommended by the IMF and the World Bank. With foreign support, the Aquino government implemented some economic and banking reforms but not others. The success and failures of banking reform can only be fully understood by examining internal political factors. The monopolies in the coconut and sugar industries were terminated and the state banks were finally rehabilitated. But these measures were not simply the result of increasing pressure from foreign actors. The absolute power of the President during the transitional period and the urgent necessity to reform economic policy and eradicate Marcos's influence immediately after Aquino took power were also

[22] See, for example, Asian Development Bank (1999) and Haggard (2000).

critical factors.

After the Aquino government failed to convince the Senate to postpone the termination of the US bases agreement and the immediate Communist threat had greatly faded, further reduction of US support was expected in the last years of the Aquino government. Some liberal reforms were implemented in the early 1990s, but the Aquino government was less successful in promoting economic reform during this period. In spite of generous offers of urgently needed funds from the World Bank, the Aquino government failed to reform the Central Bank due to internal political factors, namely the deadlock between the Executive and Legislature on reform. As a result, the Aquino government lost an opportunity to receive generous financial support from the World Bank.

After the closure of the US bases, there was no change in the World Bank's commitment to the Central Bank reform. The Ramos government was able to implement reform by overcoming the obstacles which had thwarted the Aquino government. The promotion of liberal reform and regulatory reform under the Ramos government cannot be explained by reference to strengthening foreign pressures alone, as previous economic and banking reform experiences showed. For example, the Ramos government lifted the tight restrictions on the entry of foreign banks without strong financial incentives (or pressure) from the World Bank through conditional lending or from other lenders. The successful promotion of banking reform under the Ramos government should be examined in the context of the changing political institutions which strengthened the interests and capacities of the President in promoting economic and banking reform.

The Policy Elites-Institutions Centred Approach

As Haggard and Kaufman (1995:5) argue, economic policy-making is ultimately determined by the choices of key actors as constrained by economic circumstances and existing institutions. The demands of social and foreign actors are important variables when explaining the outcomes of economic policy reform. However, an excessive focus on these factors often constrains our ability to examine economic reform policy-making since this approach depicts Philippine politics as a process by which policy outcomes are determined by relatively immediate expressions of either foreign-rooted or socially-rooted demands. For many years, scholars have explored the critical issue of how institutions affect political behaviour and policy outcomes.[23]

This thesis will argue that in the Philippine context "policy elites and institutions" must be at the centre of the analysis of banking reform policy-making. This approach, which draws attention to the decisions of policy elites and the interactions among them which are affected by changing political institutions, provides a systematic explanation for the successes and failures of economic and banking reform. Social and foreign factors are important in economic and banking reform but these are mediated by the political institutions which influence the decisions of policy elites. As defined by Grindle and Thomas (1991), the term policy elites refers to "those who have official positions in government and whose responsibilities include making or participating in making and implementing authoritative decisions for society" (Ibid:59). In terms of banking reform policy-making in the Philippines, the policy elites include Presidents, legislators, and non-elected state officials (Central Bank officials, Monetary Board members of the Central Bank and cabinet members).

The basic idea underlying this approach is fittingly expressed by Geddes (1994:6) in terms of policy choice and the "autonomy of the state". "Since state decisions are made

[23] The literature concerned with interactions between institutions and policy outcomes in developing countries has grown considerably in recent years. See, for example, Haggard and Kaufman (1995:5) Harris, Hunter and Lewis (eds.) (1995), Haggard and McCubbins (eds.) (2001), and World Bank (2001). For the case of the Philippines in a comparative perspective, see, particularly, MacIntyre (2003) and Eaton (2002).

by these human beings, the content of their decisions -including decisions that contribute to reforming the state itself- will reflect their interests. Political leaders' interests centre on their careers".[24] As Geddes (1994:8) argues, this approach leads to an explanation of autonomous state actions vis-à-vis powerful societal and foreign actors grounded in the behaviour of individual political actors: Presidents, legislators and state officials will only serve the interests of dominant social forces (oligarchy) and foreign actors in so far as it serves their own interests, which are centred on their careers.

Changing political institutions crucially affect the ways in which policy elites pursue their own interests and facilitate (or decelerate) cooperation among policy elites to form and implement policy reform. As North (1995:23) observes, "[I]institutions are the rules of the game of a society".[25] Institutions are composed of both formal and informal rules. Formal rules are composed of statute law and regulations. Informal rules (or constraints) include customs, social norms and self-imposed codes of conduct. These are often closely related to the cultural and historical context of a society. Lessons from past experience and historical events are influential in constraining individual behaviour and encouraging conformity to a code of conduct.

The Constitution, which defines the power of the State, Executive, Legislature and the electoral rules of the President and legislators (members of the House and the Senate), can be seen as being at the centre of formal political institutions in the Philippines. With respect to legislative politics, the political party system is also a set of important political institutions and organisations, but it is still underdeveloped in the Philippines. The lack of a responsible political party system or of any effective party rule which can

[24] Geddes cites Schumpeter (1975:285) who views politics as a career in modern democracy.

[25] North stresses that it is essential to distinguish clearly between institutions and organisations. "Organisations are the players: groups of individuals bound by a common purpose to achieve objectives. They include political bodies (political parties, the senate, a city council, a regulatory agency); economic bodies (firms, trade unions, family farms, cooperatives); social bodies (churches, clubs, athletic associations); and educational bodies (schools, colleges, vocational training centres)" (North,1995:23). According to North (1995:23), institutions are composed of both "formal rules (statute law, common law, regulations)" and "informal constraints (conventions, norms of behaviour and self-imposed codes of conduct)".

discipline individual legislators' behaviour is an important feature of the political institutions of the Philippines.

The attempt to examine the interactions between political institutions and policy reform in the Philippines context has only just begun. The writings of Eaton (2002) and MacIntyre (2003) are pioneering studies. Eaton (2002) examines a piece of failed tax legislation (EVAT) under the Ramos government which he compares with the success of tax legislation in a Latin American Presidential system (Argentine). He points out the importance of electoral rules and revenue distribution rules as explanatory factors underlying the failure of the Philippines and the success of Argentina in terms of tax reform. In MacIntyre's (2003) comparative study of four ASEAN countries (Thailand, Indonesia, Malaysia and the Philippines) the Philippine polity is treated as relatively successful in terms of policy reform (responses to the 1997-98 financial crisis). Both studies make important contributions to our understanding of the complicated interactions between political institutions and policy reform in the Philippines. On the other hand, the limitations in the approaches of Eaton and MacIntyre are due to their lack of attention to policy reforms and the changing institutions of the Philippines in their historical context. These are ambitious comparative studies but their breadth leads to weaknesses in the understanding of the interactions between political institutions and policy reform in the Philippines.

Eaton's study (2002) is an important contribution to the study of political institutions and policy reform in the Philippines since it focuses on political institutions as an explanatory factor underlying economic policy-making, unlike the existing literature which tends to stress social or foreign actors. In fact, tax reform is a controversial issue that shows how domestic political factors played an important role in policy-making in the 1990s. Eaton (2002) shows how the electoral rules of the House and revenue redistribution rules served as obstacles to cooperation between the President and the members of the House on the tax reform measure (EVAT). However, this ambitious comparative study is too narrowly focused on the failed VAT reform under the Ramos government. Although the Ramos government failed to implement VAT reform, it later successfully enacted another critical tax reform measure, namely the Comprehensive

Tax Reform Package (CTRP). This implementation of tax reform cannot be explained by the "institutional factors" which Eaton (2002) effectively views as the cause of the failed VAT reforms under the Ramos government. It is also arguable that the Ramos economic reform was less successful than that implemented by the Argentine government, which faced a very serious economic crisis. To understand economic reform in the Philippines, it would be more helpful if economic reform was examined in its historical context with more detailed reference to the changing political institutions.

MacIntyre (2003) attempts to resolve "the power concentration paradox" using a comparative analysis based on the number of veto players. In brief, the fragmented political institutions of Thailand, with six veto players, caused policy volatility, while the concentrated political institutions of Malaysia and Indonesia, with one veto player, led to policy rigidity. Both policy volatility and rigidity highlight distinctive problematic governance syndromes which prevented these countries from responding effectively to the 1997-1998 financial crisis. In comparison with these countries, the Philippines, with three veto players, was able to avoid such problematic governance syndromes (neither policy volatility nor rigidity) in the financial crisis.

For the purpose of comparative study, the classification of political institutions by a simple number of veto players is highly convenient. Yet, as MacIntyre recognises, this approach limits the examination of complicated interactions between political institutions and policy reforms. The varying economic policy reform experiences of the Philippines suggest the limitations of an analysis based on the simple number of veto players. In MacIntyre's analysis, Philippine political institutions under the Ramos government, which did not suffer from serious defects of governance, had three veto players (the President, the House and the Senate) due to a presidential system of government with a bicameral legislature without a stable majority of disciplined parties. Although these basic features of Philippine political institutions were the same in the pre-Marcos dictatorship era (1946-1972), which supposedly had three veto players, the Philippine government of the pre-dictatorship era, particularly the second Marcos government (1969-1972) experienced serious problems of governance leading to policy rigidity. In the face of macro-economic instability in the early 1970s, economic reform

was urgently needed but economic reform measures were seldom implemented due to the deadlock between the President and the Legislature. After martial law was declared and the Legislature was closed, the authoritarian government, with one veto player, implemented economic policy measures relatively smoothly avoided policy rigidity during the first half of the 1970s. However, faced with the economic crisis of the early 1980s, the authoritarian government with its one veto player experienced serious problems of governance similar to policy rigidity syndrome. These experiences of policy reform and responses to economic crisis under various forms of government show the necessity of further detailed analysis of the political institutions.

Any attempt to construct a general theory by which to understand the systematic effects of institutions on policy-making, will be limited in a single-country study. Yet, there are advantages to studying the complicated interactions between institutions and policy reform outcomes in a given country. Institutions and institutional changes are essentially incremental and path dependent (North,1995:23). Thus, the interactions between institutions and policy reform can only be understood in the unique historical setting of each country and policy area. As Haggard and McCubbins (2001:4) argue, explaining political outcomes often requires a more detailed focus on specific institutions. In particular, this observation is applicable to developing countries, which often experience radical changes in formal political institutions. A single-country case study also has the merit of leading to a better understanding of how informal political institutions are connected to a particular society and its historical context.

Between 1986 and 1995 banking reforms have been guided by two key principles: facilitating competition among banks through liberalisation measures and strengthening the state regulatory framework. As noted earlier, in order to analyse banking reform policy-making, this thesis distinguishes between two types of reform: structural and regulatory reform. The working definition of structural reform is reform which entails changes in the existing laws through the legislative process. In particular, amendments of two key laws, namely the Central Bank Act (R.A. 265) and the General Banking Act (R.A. 337), which provided laws for monetary and banking sector regulation from 1949, can be seen as critical structural reforms. Policy coordination between policy

elites including Presidents, legislators and state officials, are crucial to the design and implementation of structural reform. Political institutions essentially facilitate or impede policy coordination by offering incentives to individual actors.

Regulatory reform is defined as the reform which can be implemented by the Central Bank within the existing legal framework. The Central Bank officials engage daily in improving regulation under a given authority. However, the Central Bank is not entirely autonomous vis-à-vis other actors.[26] The autonomy of the Central Bank vis-à-vis politicians, especially Presidents, and regulated banks is influenced by political institutions. Political institutions constrain the interactions among policy elites and the autonomy of the Central Bank officials vis-à-vis Presidents and others. The failures and successes of banking reform under the Marcos, Aquino and Ramos governments are closely connected with the facilitation and deceleration of policy coordination among policy elites and the level of the Central Bank's autonomy, which are factors constrained by changing political institutions.

Political institutions have crucially strengthened or weakened the interests and capacities of presidents, the centre of Philippine government, in reforming the economy and banking sector. In brief, this thesis argues that the successful enactment and implementation of banking reform in the Philippines during the process of economic recovery after the economic crisis of the early 1980s was contingent on a new constellation of political institutions emerging as a consequence of the establishment of the 1987 Constitution. This new constellation strengthened the interests and capacities of Philippine Presidents in advancing economic and banking reform and weakened the proclivity and potential for resistance among legislators and a faction of social actors who had benefitted from the existing system. The following section will provide an overview of the decisions of policy elites, the interactions among them, and the outcomes of banking reform by examining how their interests are affected by changing political institutions.

[26] The definition and measurement of Central Bank autonomy (or independence) is still a contentious issue. For the controversy, see Maxfield (1997); Fry, Goodhart and Almedia (1996); and Cukierman (1992).

The Interests of Policy Elites, Changing Political Institutions and Banking Reform

Economic and banking reform is a continuous process and always a controversial issue in developing economies. Presidents have potentially a motive to reform the economy and banking sector to generate broad support. Improving the economy and banking sector advantages presidents who seek to stay in power. All Presidents have stressed the importance of economic reform. Yet, Presidents have often faced conflicting choices between the amount of support they can expect to generate by implementing reform and that which is likely to result from protecting vested interests within the existing system. The careers of legislators depend on reelection. Their ability to influence how people will vote in the next elections is always a crucial factor in their policy decisions. Legislators thus share the same motives and face the same dilemmas as Presidents. In addition, legislative leaders seeking to be elected to the next Presidential seat face a particularly difficult choice in that they have to decide whether it will be more beneficial for their career to support or oppose the reform agenda of the President since the reforming the economy and banking sector potentially benefits the incumbent President who is often the main rival to legislative leaders. State officials (or Central Bank officials) also have a motive to reform the banking sector since developing a stable and effective banking sector secures them in office and thus advances their careers. Nevertheless, their policy decisions are often constrained by their relationships with politicians, in particular with the President who is at the centre of government. It should also be noted that they might become involved in misconduct which will maximise their material benefits in the short term.

With respect to formal political institutions, the Philippines has had three forms of government (see Table 1-8): a Presidential system with bicameral Legislature under the 1935 Constitution (1946-1972); a Presidential dictatorship (Marcos authoritarian regime) under the 1973 Constitution; and a Presidential system with bicameral Legislature under the 1987 Constitution (1987 - present).

The Presidential dictatorship is subdivided into two periods: the first half (1972-77) and the second half (1978-1986). While the first half was a period of consolidated dictatorship, the second half witnessed changes in the character of the State. In 1978, elections to the Interim Batasang Pambansa (National Assembly) were first held under the dictatorship. In 1981, martial law was lifted, although the dictatorship under President Marcos maintained absolute power over law-making.

It should be noted that the Aquino period (1986-1992) is also seen as the transitional period of the 1987 Constitution. After President Aquino took power by extra-ordinary means (the "EDSA revolution") she held absolute power over law-making until the new Legislature was opened in July 1987. Moreover, after the May 1987 legislative elections, there were no legislative elections held between 1987 and 1992 due to the transitional provisions of the 1987 Constitution. Under the 1987 Constitution, the Philippines restored the Presidential system with a bicameral Legislature. However, the 1987 Constitution set different electoral rules for the President and legislators from the previous 1935 Constitution. Importantly, it prohibited the reelection of the President by limiting Presidential terms to one term (6 year) only.

The interests and capacities of Presidents in implementing banking reform measures have been constrained by these changing political institutions. The key events of banking reform in the Philippines, including the monetary instability and the failure of banking reform in the early 1970s, the first implementation of structural reform under the Marcos dictatorship, the rise of Presidential cronyism in the banking sector, the disastrous failure of banking reform in the early 1980s, the mixed results of banking reform under the Aquino government, the newly restored democracy, and the relatively successful banking reform under the Ramos government, can be understood by examining how the decisions of policy elites and the interactions among them are linked to career interests which are affected by changing political institutions.

The Presidential System under the 1935 Constitution: Monetary Instability and Failed Banking Reform in the early 1970s

After independence, the Philippines adopted a democratic form of government under the 1935 Constitution, which was a Presidential system with a bicameral legislature until 1972. The Central Bank Act and General Banking Act, which were enacted in 1948 and became effective in the following year, provided the banking sector with a regulatory structure. The Philippine banking sector started to play an important role in economic recovery from the devastation of the Japanese occupation, although the roots of the banking sector are to be found in pre-War history. The Central Bank was expected to play a critical role in developing the monetary and banking system of the country.

In a changing economy, the Philippine banking sector developed and regulatory policy was altered. During the 1950s, foreign exchange control had been the main concern of the monetary authority in order to stabilise the economy and to allocate financial resources. In the 1960s, the focus of monetary policy shifted from foreign exchange control as decontrol was instituted. In the 1960s, the Central Bank began to promote economic development intensively by active use of the rediscount window.[27]

However, between 1949 and 1972 under the 1935 Constitution, no key structural reform in the banking sector was enacted through the legislative process. This period was also characterised by frequent monetary instability. Under the 1935 Constitution, the frequent legislative elections, in particular the Presidential elections, which allowed reelection of the incumbent President, inevitably facilitated election related spending and discouraged the Central Bank from tightening monetary policy. Furthermore, the fierce rivalry between the President and legislative leaders, particularly the senators who were standing for the next Presidential election, was a serious obstacle to the implementation of banking sector reform through the legislative process.

[27] See Lamberte (1988:211) and Laya (1982:131). For changes in monetary policy, see Tan (1971).

It should also be noted that the Central Bank had not held decisive power as a monetary authority. On the first Monetary Board before the 1972 reform, the decision-making body of the Central Bank was chaired by the Minister of Finance, and the Central Bank governor was one of the seven members along with representatives from two state banks, namely the Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP).[28]

In the late 1960s, faced with banking instability, the Central Bank started to advocate structural reform in the banking sector to strengthen the Bank's powers of supervision and examination.[29] Under the second Marcos government, as the amount of credit allocated by the state banks expanded, favouritism in credit allocation became a public concern. The media was active in reporting on the problem of a "favoured" few who benefitted from public funds allocation.[30]

After the elections of 1969 led to monetary instability due to massive election related spending, the urgency of banking reform became clearer. The reelected President showed his willingness to respond to public demands and to improve the banking sector. The President keenly backed the banking reform advocated by the Central Bank. Yet, the government was unable to enact important legislation because of its failure to cooperate with the House and Senate. Importantly, there were few formal or informal institutions which facilitated cooperation between the President and the Legislature on policy reform priority. The lack of a strong political party system to discipline the legislative behaviour of legislators and the fierce rivalry between the President and the legislative leaders, particularly senators, was a distinctive feature of Philippine political institutions and this often became a serious obstacle to economic reform.

[28] The DBP was established by reorganising the Rehabilitation Finance Corporation (RFC) in 1958.

[29] Key reform measures include making the governor of the Central Bank the Chairman of the Monetary Board, the upgrading of the position of Superintendent of Banks to Deputy Governor, an increase in the basic pay of bank examiners and more rigid training in bank examination (see BSP,1998:56-57).

[30] For example, the case of the Iligan Integrated Steel Mills was enthusiastically investigated by the Philippine Free Press. See 6 March 1971; 13 March 1971; 18 March 1971; 27 March 1971; 3 April 1971; 17 April 1971; 24 April 1971; 22 May 1971; 5 June 1971; 19 June 1971; 10 July 1971; 24 July 1971; 31 July 1971 and 5 August 1971.

In addition to the absence of a responsible party system, the powerful Senate added to the difficulties of the Philippine president in pursuing his legislative agenda (see Grossholtz,1970:100). Each senator was elected by the national constituency in the same way as the President himself and, as sometimes happened, possibly with a larger number of votes. Senators had longer electoral terms (six years) than the President (four years). The conflicts between presidents and senators were often fuelled by tactical considerations for the next presidential elections because leading senators were serious challengers to an incumbent President seeking reelect for another term. President Marcos was also a former senator. In particular, during his second term (only President Marcos was reelected), it was very difficult for the President to push through his legislative agenda because of a refusal to cooperate on the part of the Legislature. The legislative infighting became fiercer during the second and supposedly the last term of President Marcos. In June 1971, the Constitutional Convention, which started to discuss amendments to the 1935 constitution, including the legislative system and presidential term, fuelled the controversy.[31] Legislative leaders who harboured presidential ambitions had little incentive to cooperate with their main rival, the incumbent President, who it was supposed would attempt to stay in power by amending the Constitution and enacting economic reform measures. The banking sector, like industry and agriculture, was central to national development, but was not reformed through the legislative process provided under the 1935 Constitution.[32]

The Consolidated Presidential Dictatorship: Implemented Banking Reform and Expanded Presidential Cronyism

In 1972, President Marcos declared martial law and closed the Legislature. Under the Presidential Dictatorship, the President dominated the law-making process and was

[31] See, for example, FEER, 5 June, 1971:18; FEER, 12 June 1971:14 and FEER Supplement , 12 June 1971, "Philippines 1971". For the debate on changes to the legislative system, see, for example, "On the Unicameral System" by Napoleon G. Rama, in Philippines Free Press, 27 November 1971.

[32] For the ineffectiveness of the Congress, see Stauffer (1975:26), Pattoco (1972:185), M.A. Caoili (1989:1-35) and Olivia Caoili (1994:13). For a study which emphasises the important role of Congress, see Emmert (1983). For the passage of some important pieces of legislation, see de Guzman (1963).

located at the centre of political institutions. This transformation of the political institutions strengthened the interests and capacities of the President with respect to economic and banking reform. However, the concentration of power provided fertile ground for Presidential cronyism as the dictatorship consolidated itself by promoting active state intervention in the economy. The banking sector experienced unprecedented levels of presidential cronyism and favouritism under Marcos' authoritarian rule, which severely eroded the stability of the banking sector.

The concentration of power overcame the problem of policy coordination in the early years of the dictatorship. The martial law regime allowed the implementation of the first structural reform, which included amendments to existing key laws in the Philippine financial system. The banking reform was one of a set of key economic reforms which the government claimed as evidence of the positive impact on the economy of the martial law regime. Soon after the declaration of martial law, in order to improve the regulatory framework of the banking sector, President Marcos issued two important Presidential Decrees: P.D. No. 71, which amended the General Banking Act,[33] and P.D. No.72, which amended the Central Bank Act[34] .

During the 1970s the Philippines achieved a relatively high economic growth rate averaging 6.4 per cent between 1971 and 1980 (Lamberte,1989:36). The banking sector steadily grew during the 1970s under favourable economic conditions and an expansionary monetary policy. However, under Marcos's authoritarian regime, the

[33] The revisions in the General Banking Act included: (1) "putting non-banks engaged in quasi-banking (borrowing from the general public) under the Central Bank's regulation and supervision"; (2) authorising the Monetary Board to judge the qualification of bank directors and officers; (3) "reducing the required capital-to-risk assets ratio from 15 per cent to 10 per cent to enable banks to expand their lending and investing capacity"; and (4) "authorising banks to invest in allied undertaking" (BSP,1998:69-70).

[34] The revisions included the following major changes in the Central Bank Act: (1) making the governor of the Central Bank the chairman of the Monetary Board, a post previously held by the Minister of Finance; (2) replacing the PNB and DBP representatives to the Monetary Board with those from the National Economic and Development Authority and Board of Investments; (3) subjecting deposit substitutes to reserve requirements; and (4) increasing the number of Central Bank deputy governors, paving the way for the conversion of the position of superintendent of banks to deputy governor (See BSP,1998:69-70 and Suleik,1989:36-37).

vulnerability of the economy and the banking sector was soon revealed. Active state intervention in the economy under the martial law regime provided massive "opportunities" for Presidential cronies, the most "successful" plunderers of public resources. The bases of the economic and banking sector were eroded by Presidential cronyism under conditions of active state intervention in the economy. Presidential cronyism was not unusual in Philippine politics. Presidents consolidated their political power by using state resources. Presidential supporters (or cronies) could benefit through inexpensive credits, allocation of foreign exchange, various industrial incentives including tax exemption, public works contracts and government procurement. But Marcos's cronyism was clearly anomalous in the country's history. The banking sector became one of the main industries which experienced an unprecedented level of Presidential cronyism under the Marcos dictatorship. The state banks expanded rapidly, as did behest loans under this new pattern of state activism. The Central Bank provided the state banks with substantial credits through foreign loans, rediscount windows and government deposits. The growth of crony-owned banks proceeded at a rate unprecedented in the history of banking in the Philippines during the last half of the 1970s.[35]

Importantly, under Marcos authoritarianism, the Central Bank played a critical role in promoting active state interventionism. Thus, the role of the monetary authority in maintaining monetary stability was severely undermined. In the early years of martial law, through the amendments to banking laws the Central Bank's legal position was strengthened enabling it to be more effective in regulating the financial system. The Central Bank's authority was also enhanced by making the governor the chairman of the monetary board, the policy-making body of the Central Bank. To strengthen coordination of development efforts by other state organisations, the Director General

[35] The list of commercial banks for 1973 and 1980 indicates that some banks expanded their businesses at an unusual speed. Four of the top ten "private" banks achieved this status due to rapid growth in a very short period of time. Allied Bank which was owned by Lucio Tan, the biggest private bank of 1980, was the most remarkable example. Other banks included Republic Planters Bank (fourth largest) which was owned by Roberto Benedicto, United Coconut Planters Bank (sixth largest) which was owned by Eduardo Cojuangco, Jr. and Traders Royal Bank (eighth largest) which was also owned by Roberto Benedicto. All the banks had unusual access to Central Bank credit or other sources of public funds. Their owners were seen as being the core of the President's cronies.

of the NEDA and the Chairman of the Board of Investments became members of the Monetary Board, replacing the representatives of the PNB and the DBP. The entire financial and credit system was placed under the Central Bank's supervision. These were positive steps towards enhancing the regulatory authority of the Central Bank.

Nevertheless, under the Presidential Dictatorship, the autonomy of the Central Bank as a monetary authority was significantly weakened as it was subordinated to the developmental efforts of the State, which was dominated by the President. The Central Bank played a critical role in development finance which largely benefitted the President and his cronies. The role of monetary authority in maintaining monetary stability and regulating banks was severely undermined as Presidential cronyism increased.

The Presidential Dictatorship in Decline: Failed Banking Reform

After changes in international economic conditions, the Philippines had to face its most serious economic and banking crisis in the early 1980s. In the early 1980s, the highly indebted Philippine economy was very vulnerable to macro economic shocks including oil price increases, low commodity prices, rapid rises in interest rates and recession in developed countries. Faced with crisis, the Presidential dictatorship in decline showed its inability to reform the economy and banking sector.

The weakness of the financial sector was revealed after Dewey Dee, a Filipino-Chinese textile based manufacturer, fled the country leaving behind nearly $85 million in debt in January 1981. Faced with economic turmoil and political uncertainty, the banking sector had failed to regain its stability in spite of a massive rescue operation mounted by the Central Bank. In October 1983, the Philippines was forced to declare a moratorium on external debt payments. During 1984 and 1985, draconian economic stabilisation measures led to the worst economic recession in the country's history. For these two consecutive years, GDP declined more than 7 per cent. The rate of inflation soared more than 50 per cent in 1984. Many banks collapsed during the economic crisis in spite of massive rescue operations. The huge non-performing assets of the

state banks were a clear indication of the failed economy. Despite the urgent need for banking reforms, no reforms were implemented by the Marcos government. The government failed to restore public confidence in the banking sector.

In its early years, the martial law regime was relatively effective with regard to the implementation of reforms. However, in the late 1970s, the authoritarian regime fragmented after favourable macro economic conditions changed for the worse. Serious problems of policy coordination among policy elites emerged as the dictatorship began to lose control. The creation of the Ministry of the Human Settlement by the first lady, Imelda Marcos, triggered the loss of the government's control over the economy (see Sicat,1985:59). In the early 1980s, under strict budget constraints, conflicts between policy elites (in particular, Gerardo Sicat and Cesar Virata), who were in favour of macro economic stabilisation measures, and Imelda Marcos and close Marcos cronies, who opposed austerity measures, were exacerbated. Marcos authoritarianism in decline was characterised by fragmenting policy elites within the state, activating opposition from business and social elites, and declining external support.[36]

The implementation of stabilisation measures and reforms in the monopolistic coconut and sugar industries was vital to the securing of external funds from the IMF and the World Bank. However, the implementation of stabilisation measures was repeatedly delayed due to the 1984 elections and reforms of the coconut and sugar industries were not implemented until the end of the Marcos era. These industries were dominated by close Marcos cronies, namely Eduardo Cojuangco (the coconut industry) and Roberto Benedicto (the sugar industry), who also owned big banks. They occupied important positions in the ruling Marcos party, Kilusang Bagong Lipunan (KBL).

During this period, the weakness of the Central Bank as monetary authority and banking regulator was clearly revealed. The Central Bank underestimated the volatility of the money markets, which grew rapidly in the late 1970s and contributed to the fragility of the banking sector. The Central Bank, which played a critical role in

[36] Haggard (1990b) classifies the regime as a "weak authoritarian regime". He explains the failure of economic adjustment in the Philippines in terms of the characteristics of a "weak authoritarian regime".

development finance, allocation of foreign exchange and the rescue of ailing companies, including banks, was unable to maintain its autonomy from the President or to resist political pressures. Due to the restoration of elections (legislative elections in 1978, local elections in 1980 and legislative elections in 1984), even if they were unfair, it became much harder for the Central Bank to maintain monetary stability. After repeated delay due to the 1984 elections, the new Central Bank governor, Jose Fernandez implemented radical stabilisation measures, but they caused further recession in the economy. The vulnerability of the Central Bank vis-à-vis the President's intervention was exposed by the crisis. The Central Bank initiatives, which aimed to strengthen the banking sector and to restore public confidence by implementing tough measures against insolvent banks, were undermined by the President. The close allies of the President, including Eduardo Cojuangco and Roberto Benedicto, who also headed big banks, were more influential over state decisions than the regulator of the banking sector, since the President was more supportive of his cronies than he was of the Central Bank governor.

The insolvent state banks, with their huge non-performing assets, exemplified the failure of economic and banking management under the authoritarian government. In spite of the deepening crisis, structural reform to rehabilitate the state banks was not implemented by the Marcos government. No consensus emerged on the controversial reform among policy elites. There were fierce conflicts among policy elites over fiscal, monetary and banking policy. Above all, the President was in favour of the opposition to the Finance Minister and the Central Bank governor, who supported implementation of macro-economic stabilisation measures, tight budgets and banking reform. Faced with growing opposition, the President was unable to implement the restructuring of the state banks, which would potentially have led to large lay-offs, further deterioration of public confidence in the banking sector and the termination of credit allocation to his close cronies under severe economic conditions. For Marcos, the need to consolidate the political support he received from his cronies, who controlled a large share of the economy, in the short run overwhelmed the need for adequate economic and banking reform.

The Presidential System under the 1987 Constitution in Transition: Implemented and Failed Banking Reforms under the Aquino Government

In 1986, when Aquino established a new government, it faced a serious economic recession with $28 billion of external debt. In the late 1980s, payments on this inherited debt absorbed some $3.5 billion per year, or about ten per cent of the country's GDP (Boyce,1993:245). The deep problems of the Philippine economy, including low economic growth rates, large inequity of wealth and an ineffectual state apparatus remained unresolved. In electoral politics, the importance of familial ties remained evident. However, the effect of the various policy reforms in the banking sector under the Aquino government, in particular the rehabilitation of the state banks, should not be underestimated. The establishment of the Aquino government triggered a change in banking policy.

In 1986, President Aquino terminated the dictatorship and called for the Constitutional Convention to write the new 1987 Constitution. In terms of the Constitution, the Aquino Presidency was seen as a transitional period. Until the Legislature was reopened after the May 1987 elections, the President held absolute law-making power. Due to these transitional provisions, legislative elections were not held between 1987 and 1992.

After President Aquino took power, economic and banking reform became an urgent task for the new government. The insolvent state banks left by the former dictator were soon restructured before the Legislature was reopened. Due to their rehabilitation, the presence of state banks in the banking sector became much smaller than before.

The transition also triggered a change in the relationship between the Central Bank and the President, although the Central Bank governor Jose Fernandez retained his position. President Aquino added another cabinet member (Budget Secretary) to the Monetary Board to facilitate economic policy coordination. However, unlike the former dictator, President Aquino did not intervene directly in the Central Bank's decisions regarding banking policy. President Aquino backed the Central Bank's position on foreign debt

policy, which was the most controversial issue in the early years of the Aquino government, despite severe criticism from other cabinet members and legislators. Despite continuing political uncertainty, the Central Bank, which was backed by the President, started to restore public confidence in the banking sector.

However, the Aquino government failed to implement further structural reform in the banking sector through the legislative process. Although some important legislation, including the Foreign Investment Act, was passed in the early 1990s, the Aquino government's performance in terms of pursuing its legislative agenda was not impressive. Despite strong support from the World Bank and businesses, including banks, the establishment of an independent Central Bank became one of the key reforms which were not implemented by the Aquino government.

The failure of the Central Bank reform bill exemplified Aquino's failure to implement key economic reform due to the slow legislative process and the lack of cooperation between the President and the Legislature. The newly restored Legislature suffered from many inefficiencies. Inexperienced legislators were keen to participate in policy debates, but the passage of legislation was often delayed. After serious delay, the House passed the Central Bank reform bill. However, since the Senate bill was not finalised, the bill was not enacted.

A responsible party system which facilitates policy-coordination between the President and the Legislature had not yet developed in the Philippines. There were no effective institutions and organisations to coordinate policy priority between the President and the Legislature. In addition, since there were no legislative elections between 1987 and 1992, due to the transitional provisions of the new Constitution, legislators secured their seats for at least five years and were not keen to cooperate with the President since they did not need to ask her for support in elections in the early years of the new government. President Aquino was not keen to create a formal body to solve the problem since she was committed to a strict separation of powers between the Executive and the Legislature under the newly restored democracy. For a President who enjoyed popular support due to her anti-authoritarian stance, "intervention" in the legislative

process by creating a policy coordination body was best avoided since it would potentially have damaged her popularity as a respected champion of "democracy".

In brief, immediately after Aquino came to power, the interests and capacities of the President in advancing reforms in the banking sector were enhanced by broad support from businesses and foreign lenders and her continuing domination of a policy-making power until the Legislature was restored. During this period, an important banking reform, the rehabilitation of state banks, was implemented. Under the Aquino government, with support from the President, the Central Bank implemented regulatory reforms in the banking sector more successfully than under the Marcos government in the early 1980s. However, after the Legislature was restored, the lack of policy coordination between the President and Legislature and the fierce conflicts between the President and the legislative leaders, particularly senators, on important policy issues, including foreign debt policy and the US bases issue, became a serious obstacle to the reform of the economy and the banking sector through the legislative process.

The Presidential System under the 1987 Constitution: Implemented Banking Reform under the Ramos Government

Under the Ramos government, the Philippine economy recovered and recorded a relatively high growth rate. Between 1994 and 1997, the annual growth of the GDP was a continuous 4-5 per cent. Relatively high economic growth rates were supported by the expansion of exports. After the currency crisis of 1997, the economy decelerated, but the government was able to manage the macro economic shocks relatively well. In spite of the currency crisis, the banking sector remained relatively stable.

The Ramos government became the first administration to implement key structural reforms in the banking sector through the legislative process. The establishment of the New Central Bank, the Bangko Sentral ng Pilipinas, and the entry of new foreign banks can be seen as critical structural reforms which reflected the successful promotion of key principles of banking reform: the enhancement of the Central Bank's regulatory powers and the liberalisation of the banking sector.

Although the Ramos government inherited its economic strategy from the Aquino government, the transition from Aquino to Ramos was associated with changes in political institutions which influenced the decisions and interests of policy elites and the interactions among them. Under a new constellation of political institutions emerging as a result of the 1987 Constitution, the interests and capacities of the President in promoting banking reforms were expanded. The establishment of a cooperative relationship between the President and the legislative leaders provided the basis for successful structural reforms in the banking sector under the Ramos government.

New political institutions under the 1987 Constitution provided legislative leaders with stronger incentives to cooperate with the President than under the 1935 Constitution. The 1987 Constitution replaced the basic framework of the previous 1935 Constitution, including the Presidential system and the bicameral Legislature. There were significant changes in terms of electoral rules. Importantly, the Presidential term was now to be limited to only one term of six years and reelection of the President was banned under the new Constitution. This term limit removed a serious obstacle to building cooperative relationships between Legislative leaders, in particular senators, and the President. Under the previous 1935 Constitution, the Senate posed a peculiar difficulty to the Philippine President. The conflicts between a President and senators were often fuelled by tactical considerations for the next Presidential election because leading senators were serious challengers to an incumbent President who sought reelection for a consecutive term as allowed by the 1935 Constitution. Senators who harboured ambitions for the Presidential seat had no incentive to cooperate with the current President. Under the 1987 Constitution, however, for legislative leaders who harboured ambitions for the next Presidential seat, the incumbent President was no longer a rival in the next Presidential elections.

It should also be noted that the 1992 elections, the first Presidential elections under the 1987 Constitution provided an important lesson for legislative leaders that support from the President was an important asset in the next Presidential elections. In addition, the popularity of a particular candidate, Miriam Defensor-Santiago, who did not have a

strong political machine but appealed to the public as a clean reformer, also made an impression on legislative leaders who harboured ambitions for the Presidency. Having popular appeal as a reformer was a significant advantage in Presidential elections. Legislative leaders, including the House Speaker, Jose de Venecia, the Senate President, Edgardo Angara, and Chairman of the Senate Committee on Banks, Raul Roco, harboured presidential ambitions. Thus, they had an incentive to cooperate with the President's initiatives in economic and banking reform, especially in the period before President Ramos had decided which candidate he intended to endorse as the next President.

The Ramos government also took its own initiatives in building a cooperative relationship with legislative leaders. The government articulated the problem of close links between political instability and economic failure. The government stressed the importance of political stability and national unity for economic development. In the Philippine context, along with internal armed conflicts, the conflict between the Executive and the Legislature was seen as a key obstacle to national unity and political stability.

Amicable relations were encouraged by the newly-elected President's leadership. For instance, the formation of the Legislative and Executive Development Advisory Council (LEDAC) played a critical role in creating a consensus between the President and legislative leaders on priority bills. Under the Ramos government, the LEDAC meeting was held once a week for many years. Ramos also encouraged legislators to participate in forming economic development plans. In addition, in 1993, a People's Summit on Social Pact for Empowered Economic Development (SPEED) was organised through collaboration between the President and Legislative leaders to mobilise public support for the government's economic and social agenda.

In the Philippines, the lack of a responsible party system has been viewed by many observers as an obstacle to economic reform because of the resulting poor policy coordination between the President and legislative leaders (see Lande,1965:3). Overall, the Philippine experiences of banking reform add another example to studies of Latin

American countries that show that a lack of party discipline weakens a President's capacity to reform state and economy.[37] However, under the 1987 Constitution, with the President's own initiative to build cooperative relations with the Legislature, the Ramos government was able to pursue its legislative agenda more successfully than previous Presidents had and became the first government to implement key structural reforms in the banking sector through the legislative process.

Conclusion

Economic and banking reform has always been a controversial issue in the Philippines. The economy has repeatedly faced economic turmoil or crises which have fuelled demands for economic and banking reforms. The responses of governments have been varied and they have often failed to implement banking reform in a prompt way. As outlined above, to understand the successes or failures of banking reform, this thesis will show the advantages of an approach which draws serious attention to the decisions of policy elites and to the way in which the interactions among them are affected by changing political institutions. Demands from foreign and social actors are influential, but they are mediated by political institutions which shape the decision-making of policy elites. In brief, this thesis will argue that the successful enactment and implementation of banking reform in the Philippines between 1986 and 1995 was contingent on a new constellation of political institutions emerging after the end of the Marcos dictatorship as a consequence of the 1987 Constitution. This new constellation strengthened the interests and capacities of Philippine presidents in advancing banking reform and weakened the resistance of legislators.

In the following chapters, key events in banking reform will be further explored by examining the decisions of policy elites and the interactions among them in the context of changing political institutions. The focus of this thesis is the period of economic recovery between 1986 and 1995. However, the analysis will begin with the last years of the Marcos era, since changing political institutions and banking reforms are essentially historical path dependent. The issues of banking reform and political institutions were inherited from the previous period. The key events of banking reform

[37] See, in particular, Geddes (1994) and Eaton (2002).

include the failures of banking reform during the economic and banking crisis in the early 1980s; the successes and failures of reforms under the Aquino government between 1986 and 1992; and the successful implementation of important structural reforms, namely the establishment of the new Central Bank and the entry of new foreign banks, under the Ramos government.

Table 1-1. Key Macro Indicators of the Philippine Economy

Year	(1) Real GDP (Billion Peso, 1985 prices)	(2) Real GNP (Billion Peso, 1985 prices)	(3) Growth Rate of Real GDP (per cent)	(4) Unemployment Rate	(5) Inflation Rate
1980	609.8	608.6	5.15	-	14.2
1981	630.6	628.3	3.42	-	11.7
1982	653.5	646.2	3.62	9.4	8.7
1983	665.7	655.5	1.87	7.9	14.2
1984	617.0	598.3	-7.32	10.6	53.3
1985	571.9	556.1	-7.31	11.1	23.4
1986	591.4	579.2	3.42	11.1	-0.4
1987	619.7	608.7	4.78	9.1	3.0
1988	658.5	652.3	6.25	8.3	12.2
1989	698.4	689.7	6.06	8.4	11.5
1990	720.7	716.9	3.04	8.1	13.2
1991	716.5	720.2	-0.58	9.0	18.5
1992	718.9	731.4	0.34	8.6	8.6
1993	734.1	746.9	2.12	8.9	7.0
1994	766.4	786.1	4.39	8.4	8.3
1995	802.9	825.2	4.76	8.4	8.0
1996	849.1	884.2	5.85	7.4	9.1
1997	893.1	930.6	5.19	7.9	5.9
1998	888.0	934.4	-0.58	9.6	9.7
1999	918.1	969.3	3.40	9.6	6.7
2000	958.4	1016.1	4.38	10.1	4.4
2001	989.2	1051.1	3.22	9.8	6.1

Sources: NSCB, NSO
BSP(Selected Philippine Economic Indicators, Various years)
Asian Development Bank (2003),
Key Indicators of Developing Asian and Pacific Countries

Table 1-1. Key Macro Indicators of the Philippine Economy

Year	(6) Foreign Debt Stock (Million $)	(7) Foreign Debt Stock / GNP (%)	(8) Gross International Reserves (Million $)	(9) Total Exports (Million $)	(10) Exchange Rates Pesos per US Dollar End of Period
1980	17252	49.5	3155.40	-	7.60
1981	20893	54.3	2574.00	5722	8.20
1982	24677	62.3	1711.40	5021	9.17
1983	24816	71.3	864.70	5005	14.00
1984	25418	76.8	886.10	5391	19.76
1985	26252	83.4	1061.10	4629	19.03
1986	28256	94.0	2459.98	4842	20.53
1987	28649	87.2	1958.69	5720	20.80
1988	27915	72.9	2058.88	7074	21.34
1989	27616	68.0	2324.16	7821	22.44
1990	28549	68.6	2048.35	8186	28.00
1991	29956	70.5	4525.94	8840	26.65
1992	30934	60.7	5337.87	9824	25.10
1993	34282	64.9	5922.03	11375	27.70
1994	37079	60.8	7121.78	13483	24.42
1995	37778	51.8	7762.17	17447	26.21
1996	41875	47.3	11745.08	20543	26.29
1997	45433	52.7	8767.67	25228	39.98
1998	47818	69.4	10806.25	29496	39.06
1999	52210	65.1	15107.32	35037	40.31
2000	52060	65.8	15024.20	38078	50.00
2001	52355	69.3	15658.39	32149	51.40

Sources: NSCB, NSO
BSP(Selected Philippine Economic Indicators, Various years)
Asian Development Bank (2003),
Key Indicators of Developing Asian and Pacific Countries

Table 1-2. Total Assets, Credits and Deposits of the Financial System
(in Million Pesos)

	Total Assets (excluding CB)	Growth Rate	Domestic Credits*	Growth Rate	Total Deposits**	Growth Rate	GNP Growth Rate
1981	289,802	-	112,898	18.2%	176,587	-	3.4%
1982	339,772	17.2%	130,310	15.4%	91,747	-48.0%	2.4%
1983	431,575	27.0%	171,482	31.6%	106,750	16.4%	1.7%
1984	487,906	13.1%	174,678	1.9%	112,481	5.4%	-9.1%
1985	503,156	3.1%	161,351	-7.6%	131,515	16.9%	-7.0%
1986	418,740	-16.8%	135,871	-15.8%	143,577	9.2%	3.6%
1987	452,336	8.0%	150,795	11.0%	153,855	7.2%	5.2%
1988	523,756	15.8%	185,096	22.7%	194,113	26.2%	7.2%
1989	638,713	21.9%	234,018	26.4%	240,202	23.7%	6.2%
1990	800,230	25.3%	291,024	24.4%	279,451	16.3%	4.8%
1991	926,668	15.8%	330,555	13.6%	336,688	20.5%	0.5%
1992	1,087,449	17.4%	396,428	19.9%	386,755	14.9%	1.6%
1993	1,359,407	25.0%	525,204	32.5%	489,237	26.5%	2.8%
1994	1,645,716	21.1%	684,526	30.3%	608,185	24.3%	4.6%
1995	2,049,375	24.5%	939,244	37.2%	767,893	26.3%	4.9%
1996	2,637,320	28.7%	1,384,976	47.5%	898,356	17.0%	7.2%
1997	3,389,280	28.5%	1,785,741	28.9%	1,068,425	18.9%	5.3%
1998	3,444,785	1.6%	1,747,009	-2.2%	1,145,172	7.2%	0.4%
1999	3,741,292	8.6%	1,772,586	1.5%	1,285,548	12.3%	3.7%
2000	4,065,520	8.7%	1,998,999	12.8%	1,387,253	7.9%	4.8%
2001	4,096,701	0.8%	2,085,483	4.3%	1,510,707	8.9%	3.4%
2002	4,312,300	5.3%	2,150,991	3.1%	-	-	4.5%

* Gross Domestic Credits including Domestic Securities, Loans and Advances

** Peso Deposit Liabilities excluding Deposit Substitutes

Sources: Philippine Statistical Year Book 2002, BSP
BSP (www.bsp.gov.ph/statistics)

Table 1-3. Total Assets of the Financial System
(in Million Pesos)

	Financial System	Banking System	Commercial Banks	KBs /FS	Thrift Banks	Rural Banks	Specialised Government Banks*	Non-Banks	NBs /FS
1981	289,802	226,057	171,705	59.2%	11,631	6,631	36,090	63,745	22.0%
1982	339,772	265,015	198,865	58.5%	12,586	8,136	45,428	74,757	22.0%
1983	431,575	338,903	256,459	59.4%	16,150	9,500	56,794	92,672	21.5%
1984	487,906	391,757	299,227	61.3%	14,967	9,023	68,540	96,149	19.7%
1985	503,156	395,141	296,564	58.9%	15,082	8,822	74,673	108,015	21.5%
1986	418,740	304,086	264,635	63.2%	17,653	9,351	12,447	114,654	27.4%
1987	452,336	330,305	287,465	63.6%	19,557	9,961	13,322	122,031	27.0%
1988	523,756	392,054	342,312	65.4%	24,993	11,018	13,791	131,702	25.1%
1989	638,713	479,011	420,410	65.8%	32,390	12,522	13,689	159,702	25.0%
1990	800,230	609,697	539,708	67.4%	37,623	13,862	18,504	190,533	23.8%
1991	926,668	691,099	599,122	64.7%	47,480	15,936	28,561	235,569	25.4%
1992	1,087,449	811,958	691,099	63.6%	60,234	18,641	41,984	275,491	25.3%
1993	1,359,407	1,019,065	864,350	63.6%	74,607	22,667	57,441	340,342	25.0%
1994	1,645,716	1,253,912	1,058,820	64.3%	106,646	28,191	60,255	391,804	23.8%
1995	2,049,375	1,595,483	1,347,362	65.7%	143,307	36,653	68,161	453,892	22.1%
1996	2,637,320	2,109,635	1,876,217	71.1%	185,138	48,039	241	527,685	20.0%
1997	3,389,280	2,779,006	2,512,975	74.1%	208,395	57,636	-	610,274	18.0%
1998	3,444,785	2,788,633	2,512,223	72.9%	216,441	59,969	-	656,152	19.0%
1999	3,741,292	3,007,728	2,722,288	72.8%	223,588	61,852	-	733,564	19.6%
2000	4,065,520	3,326,729	3,013,561	74.1%	245,807	67,361	-	738,791	18.2%
2001	4,096,701	3,403,067	3,070,474	74.9%	258,834	73,759	-	693,634	16.9%
2002	4,312,300	3,606,700	3,250,200	75.4%	273,000	83,500	-	705,600	16.4%

* Starting February 1996, specialised government banks consist of AAIIBP only.
Starting 1997, specialised government banks were consolidated with commercial banks.
Sources: BSP (www.bsp.gov.ph/statistics)

Table 1-4. Number of Offices

	Total	Commercial Banks*			Foreign Banks			Thrift Banks			Rural Banks		
		Total	Head	Branch	Total	Head	Branch	Total	Head	Branch	Total	Head	Branch
1986	3,616	1,866	33	1,589	9	4	4	665	116	372	1,083	875	107
1987	3,547	1,831	32	1,617	9	4	4	658	112	369	1,058	850	109
1988	3,562	1,850	32	1,638	9	4	4	664	110	378	1,048	840	109
1989	3,588	1,870	32	1,660	9	4	4	675	106	403	1,043	824	118
1990	3,638	1,940	33	1,733	9	4	4	653	103	396	1,045	804	142
1991	3,791	2,065	34	1,889	9	4	4	663	101	433	1,063	784	182
1992	4,296	2,438	35	2,289	9	4	4	718	98	505	1,140	787	253
1993	4,657	2,682	35	2,553	9	4	4	780	97	573	1,195	780	319
1994	5,096	3,001	36	2,878	9	4	4	821	100	612	1,274	784	395
1995	5,569	3,298	48	3,152	20	14	5	925	99	718	1,346	790	462
1996	6,332	3,647	49	3,478	22	13	8	1,171	108	941	1,514	804	616
1997	7,182	4,078	54	3,880	23	13	9	1,389	117	1,171	1,715	832	788
1998	7,646	4,230	53	4,025	23	12	10	1,474	117	1,262	1,942	826	1,021
1999	7,689	4,326	52	4,118	22	11	10	1,478	118	1,277	1,885	806	989

* including Foreign Banks and Specialised Government Banks

Sources: BSP, The Philippine Financial System Fact Book 1999,1995

Table 1-5. Total Commercial Banks, Statement of Income and Expense
(in Million Pesos)

Year	Net Income / (Loss) Before Tax	Total Operating Income	Net Interest Income	Total Operating Expenses	Extra Ordinary Credits
1986	(2,607)	7,892	1,487	11,101	602
1987	4,164	13,476	7,387	10,143	831
1988	7,072	17,438	9,862	11,792	1,426
1989	9,822	23,415	13,953	15,451	1,858
1990	15,021	34,681	17,964	21,747	2,087
1991	15,706	36,680	23,788	23,385	2,411
1992	15,240	38,800	21,784	25,967	2,407
1993	15,840	43,274	24,806	30,781	3,347
1994	19,654	51,145	33,948	35,709	4,218
1995	25,906	65,348	42,760	45,087	5,645
1996	40,728	96,924	70,845	67,493	11,297
1997	41,992	134,602	98,194	98,765	6,155
1998	23,534	140,553	106,411	125,656	8,637
1999	12,028	127,214	84,858	123,468	8,282

Sources: BSP, The Philippine Financial System Fact Book, 1995 and 1999

Table 1-6. Non-Performing Loans of Commercial Banks
(in Million Pesos)

	Total Loans	NPL	Loan Loss Provisions	NPL/ Loans	Provisions / Loans
1981	127,842	17,182	1,193	13.4%	0.9%
1982	152,793	23,457	1,940	15.4%	1.3%
1983	189,284	22,851	2,512	12.1%	1.3%
1984	198,929	41,801	5,046	21.0%	2.5%
1985	166,660	37,726	5,753	22.6%	3.5%
1986	183,476	37,506	40,783	20.4%	22.2%
1987	138,885	19,047	11,160	13.7%	8.0%
1988	162,684	17,565	9,705	10.8%	6.0%
1989	208,042	17,135	11,284	8.2%	5.4%
1990	270,760	19,426	12,679	7.2%	4.7%
1991	306,171	20,245	12,270	6.6%	4.0%
1992	366,809	22,494	12,453	6.1%	3.4%
1993	506,425	23,840	13,311	4.7%	2.6%
1994	637,179	25,050	11,995	3.9%	1.9%
1995	866,330	28,008	13,781	3.2%	1.6%
1996	1,221,763	34,206	15,149	2.8%	1.2%
1997	1,573,140	73,602	34,780	4.7%	2.2%
1998	1,542,487	160,001	61,333	10.4%	4.0%
1999	1,582,894	195,389	91,038	12.3%	5.8%
2000	1,628,214	245,813	107,206	15.1%	6.6%
2001	1,625,052	281,908	127,412	17.3%	7.8%

Sources: BSP Selected Philippine Economic Indicator, May 1998
BSP Selected Philippine Economic Indicator, 2003
(www.bsp.gov.ph/statistics)

Table 1-7. Philippine Commercial Banks (1983-2002)
at the end of Period

(in Million Pesos)	2002			1996			1993			1983		
		Total Assets	Share %		Total Assets	Share %		Total Assets	Share %		Total Assets	Share %
Metropolitan Bank	1	473,812	14.2	1	200,089	11.1	3	78,719	9.2	3	11,505	4.6
Solidbank Corp.				15	38,886	2.2	13	18,173	2.1			
Consolidated Bank										18	3,995	1.6
Global Bank												
Asian Bank Corp.				22	20,246	1.1	20	10,305	1.2			
Philippine Banking Corp.				26	14,212	0.8	25	7,040	0.8	25	2,931	1.2
Bank of the Philippines Island	2	386,583	11.6	3	138,437	7.7	4	65,444	7.7	5	10,642	4.3
Far East Bank & Trust Co.				5	120,877	6.7	6	51,067	6.0	8	7,149	2.9
Pacific Banking Corp.										17	4,083	1.6
City Trust Banking Group							15	16,142	1.9	21	3,355	1.4
DBS Bank												
Bank of Southeast Asia (DBS)				32	8,084	0.4						
Development Bank of Singapore				36	5,752	0.3						
Equitable PCI Bank	3	268,151	8.0	11	59,854	3.3	11	26,158	3.1	23	3,099	1.2
PCI Bank				6	119,143	6.6	5	52,061	6.1	7	8,070	3.3
Insular Bank of Asia & America										19	3,699	1.5
Land Bank of the Philippines*	4	249,094	7.5	4	129,333	7.2	2	89,432	10.5			
Citibank N.A.	5	216,911	6.5	7	85,450	4.8	7	47,325	5.6	2	26,590	10.7
Rizal Commercial Banking Corp	6	206,010	6.2	8	78,466	4.4	8	39,869	4.7	13	5,445	2.2
Philippine National Bank	7	184,642	5.5	2	189,306	10.5	1	123,070	14.4	1	70,502	28.4
Republic Planters Bank										9	6,829	2.8
Development Bank of the Philippines*	8	151,004	4.5									
Allied Banking Corp	9	129,020	3.9	10	60,609	3.4	10	29,519	3.5	10	6,857	2.8
Banco de Oro	10	120,042	3.6	16	35,544	2.0						
Dao Heng Bank				42	4,244	0.2						
China Banking Corp	11	106,381	3.2	12	47,156	2.6	12	21,372	2.5	15	4,584	1.8
United Coconut Planters Bank	12	105,008	3.1	9	74,639	4.2	9	38,805	4.6	4	10,739	4.3
HK&Shanghai Banking Corp	13	77,567	2.3	19	23,988	1.3	17	15,166	1.8	27	2,574	1.0
Union Bank of the Philippines	14	73,299	2.2	13	45,916	2.6	18	14,215	1.7	31	2,227	0.9
International Corporate Bank							22	8,330	1.0	24	3,004	1.2
Security Bank Corp	15	64,681	1.9	14	40,243	2.2	16	15,310	1.8	16	4,266	1.7
Prudential Bank	16	48,129	1.4	20	22,200	1.2	14	16,203	1.9	20	3,625	1.5
Pilipinas Bank				25	14,601	0.8	27	5,220	0.6	32	1,357	0.5
Philippine Bank of Communications	17	46,675	1.4	17	24,533	1.4	19	11,240	1.3	22	3,313	1.3
Standard Chartered Bank	18	40,009	1.2	29	12,783	0.7	28	5,052	0.6	30	2,290	0.9
International Exchange Bank	19	39,259	1.2	27	13,966	0.8						
Bank of Commerce	20	38,386	1.1	31	10,497	0.6	26	6,503	0.8			
Panasia Bank												
Traders Royal Bank				28	13,134	0.7	24	7,896	0.9	14	4,639	1.9
Commercial Bank of Manila										34	800	0.3
Philippine Trust Co.	21	33,439	1.0	24	15,669	0.9	21	9,332	1.1	33	1,285	0.5
Export and Industry Bank	22	26,742	0.8									
Urban Bank				34	7,379	0.4	30	4,666	0.5			
Int'l Commercial Bank of China	23	22,540	0.7									
Deutsche Bank AG	24	22,138	0.7	30	10,858	0.6						
Bank of Tokyo-Mitsubishi, Ltd	25	20,194	0.6	35	6,487	0.4						
China Trust (Phils.)	26	16,250	0.5	43	3,979	0.2						
United Overseas Bank Philippines	27	15,367	0.5									
Westmont Bank				23	17,093	1.0						
Associated Bank							32	2,476	0.3	29	2,379	1.0
ING Bank	28	15,082	0.5	21	22,042	1.2						
East-West Banking Corp.	29	14,985	0.4	41	4,684	0.3						
Asia United Bank	30	14,653	0.4			0.0						

Philippine Veterans Bank	31	13,987	0.4	33	7,753	0.4	29	4,675	0.5	28	2,555	1.0
Mizuho Corporate Bank, Ltd	32	12,368	0.4									
Fuji Bank, Ltd				44	3,281	0.2						
Maybank	33	11,280	0.3									
J.P.Morgan Chase Bank	34	10,869	0.3									
Chase Manhattan Bank				45	1,128	0.1						
ABN Amro Bank, Inc.	35	10,408	0.3									
Australia & New Zealand Banking	36	10,018	0.3	40	5,001	0.3						
Bank of America NT & SA	37	8,418	0.3	18	24,041	1.3	23	7,971	0.9	6	9,004	3.6
Korean Exchange Bank	38	6,296	0.2	38	5,320	0.3						
Banco Stander Phils., Inc	39	6,201	0.2	39	5,233	0.3						
Bangkok Bank Public Co., Ltd	40	4,274	0.1	37	5,328	0.3						
Al-Amanah Islamic Bank	41	96	0.0									
(Manila Bank Corp.)**										11	6,486	2.6
TA Bank of the Philippines, Inc												
(PDCP Bank)**												
First Philippine International Bank							31	3,871	0.5			
Producers Bank of the Philippines										26	2,630	1.1
(BPI Family Bank)**												
Family Bank & Trust										12	5,655	2.3
Total		3,342,807	100		1,798,472	100		852,625	100		248,165	100

Note:

Foreign Banks

* LBP is not classified as commercial banks in 1983.

DBP is not classified as commercial banks in 1996, 1993 and 1983.

** (Thrift Banks)

Sources: Business Day, Business World, Fourth Quarter Banking Report, various issues

Table 1-8. Key Characteristics of Political Institutions, Policy Coordination and Banking Reform

Political Institutions (Constitution)	Presidential System under 1935 Con.	Presidential Dictatorship (the first half)	Presidential Dictatorship* (the second half)	Presidential System under 1987 Con. (in transition)	Presidential System under 1987 Con.
Electoral Rules					
President					
Term	4 Years	-	-	6 Years	6 Years
Constituency	National (Direct Vote)	-	-	National (Direct Vote)	National (Direct Vote)
Reelection	Once	-	-	None	None
Senate					
Number	24	-	-	24	24
Term	6 Years 1/3 (every two years)	-	-	5 Years (1987-1992)	6 Years** 1/2 (every three years)
Constituency	National (Direct Vote)	-	-	National (Direct Vote)	National (Direct Vote)
Reelection	Unlimited	-	-	Once	Once
House					
Number	120	-	-	200+(50***)	200+(50***)
Term	4 Years	-	-	5 Years (1987-1992)	3 Years
Constituency	Single Member	-	-	Single Member	Single Member
Reelection	Unlimited	-	-	Twice	Twice
President	Marcos (1969-1972)	Marcos (1972-1977)	Marcos (1978-1986)	Aquino (1986-1992)	Ramos (1992-1998)
Policy Coordination					
Executive-Legislative	Fail	-	-	Fail (1987-1992)	Good/Fair
Executive-CB	Fair	Good	Fair/Fail	Good	Good
Monetary Stability	Fail	Good/Fair	Fail	Fair	Good/Fair
Banking Reform	Fail	Fair	Fair/Fail	Fair	Good/Fair
Structural Reform	Fail	Good	Fair/Fail	Fair/Fail	Good/Fair
Regulatory Reform	Fair/Fail	Good/Fair	Fair/Fail	Good/Fair	Good/Fair

* Elections for National Assembly (Batasang Pambansa) were held in 1978 and 1984.

** The electoral term for the 12 lower-ranking senators in the 1992 elections was three years under the transitional provision.

*** The 50 members have been elected by party list system for minority representation since 1998.

Chapter 2.
The Economic Crisis and the Banking Sector between 1980 and 1986

Introduction

The period of the most serious economic turmoil in the Philippines was the worst era for the Philippine banking sector. After a relatively high growth period, the economic climate started to change in 1979 when the second oil shock in the 1970s led to a prolonged deceleration in economic growth. The 1980s began with structural reform of the banking sector which aimed to increase long-term finance in the economy. However, soon after the reform was initiated, the banking sector was shaken by a collapse of the money market triggered by a financial scandal. Between 1981 and 1983, the Central Bank had tried to prevent bank closures to avoid further deterioration of public confidence both in the banking system and the government. Massive rescue funds were provided through the Central Bank and state financial institutions to rescue ailing companies, including financial institutions.

However, in spite of the massive rescue operation, the government was unable to salvage the economy and banking sector. The Philippines faced its most serious economic and financial crisis between 1983 and 1985 and became the only Asian country to declare a moratorium on repayments of foreign debt in 1983. High inflation, negative economic growth rates and huge amounts of foreign debt were a reflection of the economic crisis. Massive public funds to rescue ailing banks and the huge non-performing assets of the banking sector indicated clearly the depth of the financial crisis. The government acquired six banks through the rescue operation. Between 1981 and 1987, the Central Bank closed 173 banks, although the majority were small rural banks. The state banks, namely PNB and DBP, which had occupied a large share of the banking sector, recorded huge losses between 1984 and 1986. Non-performing loans in the banking sector reached the highest level in banking history.

Despite some reform attempts, the government failed to improve the economy. After repeated delay, the Central Bank implemented stabilisation measures to curb high

inflation, but these led to further economic recession. Under the Marcos dictatorship, public confidence in the banking sector was never restored.

International economic factors including high interest rates, a slump in commodity markets and the economic recession of the leading trading partners adversely affected the economy and the banking sector. Nevertheless, as Filipino economists argue, the economic and banking crisis cannot be explained by external economic factors alone since some countries managed to minimise the economic shocks.[1]

In terms of economic policy choice, some stress the influence of International Financial Institutions, namely the IMF and the World Bank. In fact, the availability of foreign credit was an influential factor in terminating the unlimited rescue operation for ailing companies including banks. However, the IMF and the World Bank pressures had not always been seen as a decisive and solitary factor in policy choice. Careful studies of the policy conditionality of the IMF and the World Bank revealed that their conditionality had not been burdensome for the country until 1983.[2] During the severe balance of payments crisis, the Philippines repeatedly delayed the implementation of a stabilisation programme endorsed by the IMF and the World Bank due to an internal political factor, namely the 1984 elections. After the election, the Central Bank adopted a stabilisation programme, but its detailed policies and the timing of its implementation were decided by the Philippine government. It should be noted that even during the severe balance of payments crisis, in spite of massive pressure from the IMF and the World Bank, the Marcos government did not accept their recommended reforms in the coconut and sugar industries which directly affected Marcos's power base. The reform of the state banks, which was also endorsed by the IMF and the World Bank, was also not implemented. The loss of US support was a significant factor in ending Marcos's rule. However, in terms of economic policy choice, the influence of US policy preferences was not very clear. The President seemed to believe that US support for his regime was solid due to its security interests and that the US would not enforce economic reform.

[1] See de Dios, et al. (1984) and Sicat (1985:25).

[2] See Mosley (1991) and Thompson and Slayton(1985).

This chapter examines the failure of banking reform during the economic crisis by focusing on the decisions of policy elites and the interactions among them in the context of changing political institutions. After martial law was declared in 1972, the problems of policy coordination between the Executive and Legislature, which was a serious obstacle to structural reform in the banking sector, was resolved due to the closure of the Legislature. The first key structural reforms in the banking sector were implemented by presidential decrees. During the early years of the Marcos dictatorship, the Central Bank, which was backed by the President, strengthened its regulatory power. The governor of the Central Bank became the chairman of the Monetary Board. In terms of monetary and banking policy, economic policy coordination was improved, since representatives from National Economic Development Authority and Board of Investments joined the Board. The Central Bank coped with the first oil price hike in 1973 relatively well.

However, during the early 1980s, the various changes in political institutions centred upon the dictatorship were clearly revealed. Essentially, the Central Bank was losing support from the President. The tight control of the dictatorship began to change in the mid-1970s (Thompson,1995:102). Marcos resumed elections in 1978 and officially lifted martial law in January 1981. The President continued to have a decisive influence on policy-making, due to his unlimited power to issue decrees. Nevertheless, even if they were not fair, the resumption of elections led to a new era for the authoritarian regime. Having increased the importance of electoral contests for the regime's survival, the leaders of Marcos ruling party and close Presidential cronies, who also owned big banks, obtained more influence over economic policy-making. During the economic downturn, the dictatorship, which was at the centre of the political institutions, was declining as a result of fragmenting policy elites, giving rise to opposition movements from various groups, including business and Catholic churches and a loss of support from foreign creditors. Under an authoritarian regime in decline, the interests and capacities of the President in advancing economic and banking reforms were severely undermined.

Faced by this crisis, the policy elites found themselves divided over policy choices relating to economic reform. Monetary Board members, including Prime Minister (and

Finance Minister) Cesar Virata, were supportive of economic stabilisation measures to secure foreign credit. However, the leaders of the Marcos ruling party and its close associates, including Imelda Marcos, Eduardo Cojuangco and Roberto Benedicto, were keen to avoid the structural reform which might cause further economic recession, lose support for the government and deprive them of their privileges. As international support from the IMF, the World Bank and then the US government had been fading and the government was not able to improve the economy, this prompted critical voices from business elites who opposed the Marcos cronies' domination of the economy. Various opposition movements to the regime, including religious leaders and left wing movements, were energised during the economic crisis. Importantly, electoral politics reemerged as a serious threat to monetary stability. The Central Bank, which played a critical role in helping the authoritarian regime through massive public spending, was very vulnerable to political interference and lost its control over monetary and banking policy.

This chapter is divided into three sections. In the first section, the 1980 banking reform is analysed. The structural reform, which included amendments to existing laws by presidential decree, was potentially influential since it altered the structure of the banking sector. For example, the expanded commercial banks (universal banks), which could undertake investment house operations were introduced to facilitate investment activities. However, the effects of reform were not clear because the banking sector was shaken by the collapse of the money market soon after the reform initiatives. In the second section, the responses of the government to the instability of the banking sector and its consequences are reviewed. Until 1983, the Central Bank tried to rescue all banks. Nevertheless, the massive rescue operation did not improve the economy and the banking sector. The government had to face further deterioration of the economy. In the third section, the Central Bank's attempts to alter the previous policy are examined. During this period, the new Central Bank governor, Jose "Jobo" Fernandez, took drastic measures to stabilise the economy and to restructure the banking sector. However, the reform efforts were undermined by lack of support from the President. The most serious issue in the banking sector, the rehabilitation of the state banks, was left unsolved until the end of regime.

The 1980 Structural Reform in the Banking Sector

In the late 1970s, the Central Bank was concerned about the effectiveness of the financial system. Since the middle of the 1970s, the Central Bank had tried to mobilise more savings for long-term finance through various measures. As a key policy measure, the Central Bank had started to liberalise interest rates in the middle of the 1970s. Laya (1982:163) explains that

> "While it was recognised that the economy was responsive to the mobilisation of savings in financial forms as a result of interest rates, tax and other fiscal and monetary reforms, the increase in deposits had not been translated into long-term financial assets. Much of the outstanding credits of the financial system, of which the banking system was the dominant sector, still remained short-term oriented".[3]

The initiatives for the 1980 reform stemmed from the concern of the Central Bank over ineffective financial resource mobilisation through the financial system. The main objectives of the reform were (1) to promote greater efficiency by increasing competitive conditions and (2) to increase the availability of, and access to, longer term funds.[4] To achieve these goals, the government implemented the following reforms in 1980 and 1981: (1) changing the financial structure; (2) floating interest rates; and (3) improving the Central Bank policy instruments.

The IMF and the World Bank played an important role as technical advisors in designing the reform of the financial structure. In March 1979, a joint IMF/World Bank Mission was invited to study the financial system in the Philippines. It must be noted that this mission had a specific issue to address. The IMF/World Bank clarified the objectives of the mission as follows:

> "In particular, the mission looked at the present situation of the sector in light of the need to increase the flow of longer-term savings and make such

[3] See, also Lamberte and Remolona (1986:103).

[4] See World Bank/IMF (document) (1979), Laya (1982:164), Suleik (1991:37) and Lamberte and Remolona (1986:103).

> flows available for priority uses. There was concern about the shortage of medium and longer-term finance, especially for industry. The authorities requested that the mission pay special attention to the possibilities and consequences of changing the range of functions performed by financial institutions and the impact this might have upon the supply of finance" (World Bank/IMF,1979:i).

The main recommendation of the study was that the commercial banks should be given "powers to invest in equities and engage in underwriting" (World Bank/IMF,1979:i), since the existing legislated specialisation of financial institutions prevented them from responding to the needs of their clientele and from operating on the basis of comparative advantage.

Following this recommendation, the reform programme included the following major changes in the banking structure: (1) the introduction of universal banks (or expanded commercial banks);[5] and (2) simplification of domestic bank categories by reducing differentiations among thrift banks, savings and mortgage banks, private development banks and stock savings and loan associations.

In short, expanded commercial banks can be defined as the combination of commercial banking (full domestic and international banking) with the functions of an investment house (underwriting, securities dealership, and equity investment) (see Laya,1982:166). Investment house operations can be pursued by an expanded commercial bank either (1) through the establishment of a separate department in the banks or (2) through a separate subsidiary. The introduction of the expanded commercial banks was expected to have the effect of making competition in the system, more vibrant and credit-orientation longer-term.

By simplifying the domestic bank category, thrift banks, including savings and mortgage banks, private development banks and stock savings and loan associations, were allowed to offer the full range of "domestic banking" services, including demand

[5] The model for the universal bank was the German universal bank. For a detailed discussion of German universal banks, see Krummel (1980).

deposit accounts and NOW accounts, and other additional services with prior Monetary Board approval. Thus, thrift banks came to be defined as commercial banks which did not engage in international banking. Through this reform, other banks were expected to be energised, since the removal of their legislated areas of specialisation and the capability to "move up" to the level of the higher ranking financial institutions were thought to be good incentives to enhance their operations. The Central Bank raised the minimum capital requirement: P500 million for expanded commercial banks, P300 million for commercial banks, P20 million for thrift banks located in Metro Manila and P0.5 million for rural banks.

The second component of the reform in the early 1980s was the liberalisation of interest rates. Since the middle of the 1970s, interest rates had been gradually liberalised. In July 1981, except for short term loans, all interest rates on deposits, deposit substitutes and loans were freed from administrative ceilings. Then, in January 1983, the ceiling on the short-term loan rate, the last remaining ceiling, was lifted. The institution of floating interest rates, in conjunction with the other financial reforms of 1980, was expected to give financial institutions a greater flexibility with respect to the mobilisation of funds .

To strengthen the regulatory power of the Central Bank, a Presidential Decree granted the Monetary Board the power to authorise special examinations of affiliates of non-bank financial intermediaries with quasi-banking functions and to inspect deposits during bank examination in order to detect bank fraud or serious irregularity (see Suleik,1991:37).[6]

Within the Monetary Board, there was a conflict over the introduction of expanded commercial banks. The reform of the financial structure was controversial, since the existing financial structure had been established less than a decade before as a result of recommendations made by the joint IMF-CBP (Central Bank of the Philippines)

[6] The Central Bank's capital base was to be enhanced from P10 million to P10 billion through an additional revision to R.A. 265 by means of P.D. 1771 dated January 4, 1981. However, the additional capital was not provided by the government.

commission.[7] Some Central Bank officials, including Arnulfo Aurellano (a special assistant to Governor Licaros), had serious doubts about the merits of the expanded commercial banks (see Broad,1988:144-145). Also, governor Licaros himself did not support the reform initially. They were afraid of the consequences of economic concentration and domination by the big banks of the banking sector. However, Virata, the Ministry of Finance and a member of the Monetary Board, was a key proponent of the reform.[8] The proponents believed that expanded commercial banking could take advantage of scale economies. Bigger and more diversified banks are more stable, more capable and more efficient in pursuing various financial activities. The leaders of the banking sector and other financial institutions were also convinced by the proponents with regard to the merits of the banking reform.[9] The BAP (Bankers Association of the Philippines) issued an official statement supporting the reform.

Despite Chairman Licaros's doubts about their merits, the Monetary Board approved amendments to laws aimed at reforming the financial structure, including the introduction of expanded commercial banks. It should be noted that the Monetary Board's decision was unusual since the Central Bank governor, the Chairman of the Monetary Board, had normally played a decisive role in decision-making. By the late 1970s, in terms of decision-making in the Monetary Board, the decisive influence of Licaros, who had served as Central Bank governor since 1970, had started to fade as Virata had became a more prominent figure in the Marcos government. In early 1981, Licaros was replaced by Jaime Laya, deputy governor for supervision and examination and a close ally of Virata. There was strong evidence that Licaros's involvement in irregularities forced him to resign,[10] although they were not officially uncovered.[11] The direct involvement of the Governor in misconduct relating to foreign currency allocation

[7] For the controversy, see Broad (1988:137-148).

[8] See FEER,23 January 1981:38-39; Business Day, 26 September 1979; Asian Wall Street Journal, 26 February 1980, cited Broad, 1988:148.

[9] See Times Journal, 16 January 1980, p.10.

[10] Virata, who played a leading role in Licaros's resignation, admitted the "unfortunate" incident (Interview, Virata, 19 June 1998). See, also, Hutchcroft (1998:140) and Patrick and Moreno (1985:322).

[11] It is reported that Governor Licaros asked to be retired after fifty years of service in the government, eleven of them as Central Bank Governor (Bulletin Today, 14 January 1981, p.10 and Times Journal 13 January 1981).

may have been the most serious crime which the Central Bank had ever committed.

Under the authoritarian regime, the process of structural reform through amendments to laws had been very smooth. Following approval from the Monetary Board, the President enforced the decisions of the Monetary Board. Then, the "Batasang Pambansa", the legislative body which was established in 1978 under the martial law regime, immediately amended the existing banking law without any serious discussion in the legislative body.[12] These reforms consisted of seven amendments which were passed into law in April 1980.

The essence of the 1980 reform was to liberalise the financial system to facilitate financial resource mobilisation, particularly with regard to long term funds. The introduction of the expanded commercial banks was expected to mobilise more long-term funds and to activate capital markets. The flotation of interest rates was supposed to attract more deposits. In fact, Lamberte and Remolona's study (1986:101) suggests that the reform achieved some of these goals in the short run. The reform led to substantial increases in the growth rates of savings and time deposits.[13] However, the effects of the reform on the banking system were not so clear,[14] as an era of financial and economic crisis resulting from political upheaval followed immediately afterwards. It was impossible to mobilise longer term funds and to activate capital markets during the economic and political crisis. Despite the flotation of interest rates, the Central Bank opened various rediscounting windows to provide credits at lower interest rates.

In terms of banking policy-making, the 1980 reform suggests that the President still supported the decision of the Monetary Board at that time. Under the dictatorship, with Presidential support, banking reform was implemented smoothly. However, as the economic crisis deepened, conflicts over economic policy were revealed between the Monetary Board members and the leaders of Marcos' ruling party, including influential

[12] See Bulletin Today, 25 March 1980, p.1 and 28 March 1980, p.1.

[13] Lamberte and Remolona (1986:138) find that the reform caused higher interest rates on deposits and borrowed funds and low returns on loans and investments which squeeze bank profits. They claim that "This had made banks more vulnerable to the balance of payments crisis" in 1983.

[14] See Business Day, 30 April 1984 (Supplement: "Unibanking: Adjustment period needed").

Marcos cronies. During the economic and political crisis, the Central Bank lost the support of the President.

Saving for All Banks: The Rescue Operations and Their Failures between 1981 and 1983

Since the economic climate started to change in 1979 and the Philippines entered an era of worldwide recession and high interest rates, the government attempted to maintain high growth through high investments (Lim,1996:11). In January 1981, the Dewey Dee scandal revealed the fragility of the financial system. Dewey Dee was a leading businessman who headed a business group centred on textile manufacturing. He left the country on 9 January 1981, leaving behind unpaid debts of about P635 million, mostly to 16 commercial banks, three offshore banking units and 11 investment houses (Lamberte,1989:48). This scandal led to the collapse of the money market and seriously hurt public confidence in the financial system. Laya, the governor of the Central Bank, notes that "in retrospect, Dewey Dee's flight had a far greater impact than might have been expected with the amount of money that he took with him" (Laya:1982:46). Big businesses and financial institutions, including commercial banks, investment houses and finance companies, which depended heavily on the money market, were hit by the scandal.

Assuming that the economic downturn and the financial crisis was temporary, the government and the Central Bank became involved in rescue operations on a scale which the country had never experienced before. Governor Laya announced that the Central Bank was empowered to extend appropriate financial assistance to both banks and non-bank financial institutions.[15] For the first time, the Central Bank made advances to quasi banks, reaching P1.5 billion (about US$187 million), the largest such advance in the history of the Central Bank (Laya,1982:29). Yet, this was only the first step in rescuing the financial system.

During previous economic recessions, increasing government spending to stimulate the economy had been the conventional response. However, the policy choices of the

[15] See Times Journal, 21 January 1981.

government in response to the recession, including the massive rescue operation and the prolonged delay of adjustment efforts, should be understood in conjunction with the changing political institutions centred on the Marcos dictatorship in decline. President Marcos resumed elections in 1978 and officially lifted martial law in January 1981. The opening of the National Assembly, the interim Batasang Pambansa (IBP), did not cause a significant change in Presidential power with respect to policy-making, since the President held unlimited power to issue decrees.[16] The President also maintained a tight control over the ruling party (KBL: Kilusang Bagong Lipunan), which dominated the Assembly. Nevertheless, the resumption of elections, no matter how unfair, opened a new era of the Marcos dictatorship. Surrounded by a constellation of political institutions, contingent on the resumption of elections, and with the legitimacy of the dictatorship in decline, the President was unable to implement economic and banking reform measures promptly enough to avoid an economic and banking crisis.

By the late 1970s, the legitimacy of the martial law regime had started to fade, due to the economic downturn, presidential cronyism, bureaucratic inefficiency, internal conflicts among state elites, including economic ministers and military leaders, opposition from business and religious leaders and an increase in political unrest. In terms of economic policy-making, the leaders of Marcos ruling party who were most concerned about immediate electoral contests and their business interests became more influential. Having restored the electoral contest and with its legitimacy declining, the government did not stop providing massive funds through foreign borrowing to avoid the further economic recession and to shore up support for the regime. The Central Bank had played a critical role in helping the regime survive through this massive spending. Until the foreign credit line was shut down and available funds were exhausted, the government could not stop spending. Election-related spending reemerged as a serious threat to monetary stability. A deep cleavage among policy elites over economic policy was revealed during the economic crisis. Monetary Board members of the Central Bank, including the Central Bank governor, Finance Minister and the Director General of the NEDA, recognised the importance of economic adjustment, including tight monetary and fiscal policy. However, the leaders of KBL (Marcos's political party), including Imelda Marcos and close Marcos cronies, opposed the economic

[16] See Olivia Caoili (1989); Canoy (1980:178-186); and Wurfel (1988:234).

adjustments. Finally, President Marcos did not support the Monetary Board's policy and delayed economic adjustments.

In the wake of the 1981 liquidity crisis, financial companies which had been heavily involved in the money market were the first group of companies to fall. These included Filmanbank and Philfinance of the Silverio Group; Atrium, Apcor, Interbank and Combank of the Herdis Group; and Bancom Development Corporations of the Bancom Group, which was long owned by Rolando Gaput.[17] Apart from their own affiliates, Atrium and Apcor were known to have lent large amounts to and to have underwritten several commercial papers of Dewey Dee's Continental Manufacturing Corporation (see Lamberte,1989:47). Many companies of the Silverio Group and the Herdis Group, which had close financial relationships with these financial companies were severely damaged. During the liquidity crisis, some small banks, which were poorly managed, also revealed their financial weakness. Philippine Veterans Bank (PVB), a state-owned commercial bank, was one of the weakest banks. The bank's financial position deteriorated due to uncollected loans incurred by some of its officers. In spite of its mounting losses, the bank was allowed to operate until 1985. Associated Bank was another bank which received generous financial assistance. After a rescue operation, the bank was acquired by the DBP.

To restore public confidence in the financial system, the government decided to rescue financial institutions. Until 1983, the Central Bank did not allow the closure of a single bank. The Central Bank arranged to merge and consolidate financial institutions within the same conglomerate. Apart from the Central Bank credits, the government provided ailing banks with financial assistance through state financial institutions, including the Philippine National Bank (PNB), Development Bank of the Philippines (DBP), Land Bank of the Philippines (LBP), Government Service Insurance System (GSIS), Social Security System (SSS) and National Development Corporation (NDC). Generous financial assistance through state financial institutions led to the government's takeover of rescued banks. Due to the massive rescue operation, the presence of the state in the financial sector was further expanded. The state banks, namely the PNB and the DBP,

[17] Rolando Gaput, who was seen as Marcos's financial advisor, worked for the Bancom between 1965 and 1980 and left the bank to head the Security Bank in July 1980.

occupied nearly half of the entire banking sector's assets in 1983.

Filmanbank of the Silverio Group faced a continuing decline in its liquidity position due to the expansion of unsecured loans in the past. To rescue the bank, PNB infused more than P200 million worth of equity and then took control of the ownership and management of the bank. The bank was renamed Pilipinas Bank in 1980. Philfinance, a finance company of the Silverio Group, which also faced a severe liquidity problem, was closed after revealing serious violations against financial regulation.[18]

Financial companies and a bank of the Herdis Group were merged by the Central Bank's rescue packages. Atrium Capital Corporation (Atrium), the largest investment house in the country with P1.6 billion assets in 1980, and Asia Pacific Capital Corporation (APCOR) merged to form Interbank. Atrium obtained an emergency loan from the Central Bank to pay off their investors, although their placements were based on a without-recourse basis. When they merged, the DBP provided P420 million capital infusion. Furthermore, National Development Corporation, a state-owned holding company, acquired a 20 per cent ownership share of the Herdis Group. As a consequence, Interbank became a state-owned commercial bank. The DBP owned 70 per cent of the capital stock of the bank and played a key role in managing the bank.[19]

Bancom Development Corporation, headed by Sixto Roxas, the fourth largest investment house in the country, was another of the biggest companies which suffered severely from the liquidity crisis. Accepting the Central Bank's rescue plan, it merged with three other financial institutions of the Bancom Group and then converted to a commercial bank, Union Bank of the Philippines (UBP).[20] To meet the P300 million minimum capital requirement for a new commercial bank, LBP infused P140 million and SSS did P100 million.

[18] Lamberte (1989:25) explains the typical fraud. The finance company engaged in "Kiting", which means borrowing from the money market using the same commercial papers of reputable firms three or four times for different sets of investors.

[19] See Bulletin Today, 13 September 1981.

[20] See Bulletin Today, 3 September 1981.

Associated Bank was another bank which was rescued by government assistance, including the CB advances, capital infusion by the DBP and deposits from the DBP. Later, the DBP acquired the bank, since the bank was not able to pay back its debt.

These five state-acquired banks had combined assets of P12 billion, about 8 per cent of the total domestic commercial banks' assets (see FEER, 13 September 1984:56). The various forms of financial assistance by state institutions to acquired banks amounted to more than P6 billion at the end of February 1984.[21] Central Bank assistance to financial institutions also increased rapidly. The ratio of the assistance divided by the total of the reserve money jumped from 7.7 per cent in the first quarter of 1984 to 47.3 per cent in the same period of 1986 (see Table 2-1).

Apart from assistance to financial institutions, the government set up a P1.5 billion Industrial Fund using the national budget and the proceeds of Central Bank Certificates of Indebtedness (CBCIs) in 1981 (see, Laya,1982:30-34). The Fund aimed to rescue commercial paper issuers and quasi-banks from the collapsed money markets. The resources of the Industrial Fund were to be channelled through lead banks to the commercial paper issuers. Thus they could pay back the troubled quasi-banks and these in turn could repay the Central Bank. The first recipients of assistance from the Industrial Fund were Continental Manufacturing Company, Alfa Integrated Textiles and the Construction and Development Corporation of the Philippines (CDCP).[22] Continental Manufacturing Corporation was the company which Dewey Dee abandoned. This company and Redson Textile Manufacturing Corporation, another Dewey Dee's company were taken over by the DBP.[23] Alfa Integrated Textiles was damaged by the Dee scandal during the recession, since the company had close relations with Dee's company. CDCP, which was owned by Rodolfo Cuenca, a Marcos crony, was the largest construction company with 13,878 employees (at year end 1980). The following year, the Industrial Fund was replaced by a new P2 billion rediscounting facility.

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[21] See Business Day, 4 May 1984, p.2.

[22] It is reported that 10 more firms asked the government for assistance (Bulletin Today, 1 September 1980,p.20).

[23] See, for example, Bulletin Today, 31 January 1981, p.11.

To restore financial stability, the Central Bank also provided large amounts of credit through its rediscount windows, particularly in the late 1970s and early 1980s. Between 1980 and 1983, a lot of rediscount windows had been opened with preferential rates significantly below the market rates. In fact, the Central Bank's selective credit programme lost its selectiveness, since many economic activities could qualify for rediscounting.[24] Massive rescue operations to ailing companies which were owned by close Marcos cronies fuelled criticism against the Marcos government. For example, Jaime Ongpin, a leading critic of the business community against the government, severely criticised the CDCP rescue by the government.[25]

The Central Bank was also keen to attract foreign credits to stimulate the economy during this period. Foreign swaps (Forward Exchange Cover) began in 1972 and became particularly important in the late 1970s and early 1980s. In the early 1980s, the Central Bank encouraged private banks to acquire foreign credits through foreign swaps which generously transferred currency risks from the private banks to the Central Bank (Dohner and Intal, Jr.,1989:174). Between 1983 and 1984, total swaps increased both in absolute terms and as a proportion of total commercial bank assets and 1984 devaluations caused Central Bank losses.[26] Huge losses from foreign swaps contributed to the financial collapse of the Central Bank.

Until 1983, the Philippines could manage to generate foreign loans, although investors became more cautious and the terms and conditions tended to be less favourable for the country. Despite the financial instability and serious economic problems, the World Bank and IMF did not encourage structural reforms in the banking sector until the economy and banking sector was faced with a deep crisis. They did not recognise properly the vulnerability of the economy and banking sector in the country. The World Bank had continued to provide loans to the country. The first $200 million Structural Adjustment Loan (SAL) was approved in September 1980 and the second $200 million SAL was approved in April 1983. In addition, in May 1981 the World

[24] For the lists of preferential rediscount rates, see Lamberte (1988, Table 7, 1949-1973 and Table 21, 1981-1983); and World Bank (1988, Table 6.1, 1979-1986).

[25] See, for example, Times Journal, 1, 3 and 4 March 1983.

[26] From 1985 the Central Bank stopped using foreign exchange swaps to facilitate foreign borrowing.

Bank approved a $250 million APEX loan for relending to the private sector through Philippine Investments Systems Organisation (PISO), Private Development Corporation of the Philippines (PDCP), and the Development Bank of the Philippines (DBP), including a $100 million co-financing syndicated by Lloyds Bank International (see Laya,1982:61). In 1981 the Central Bank also borrowed $250 million for the private sector as part of the Consolidated Foreign Borrowing Programme (Jumbo Loan) (Laya,1982:61). This consisted of $200 million syndicated by Manufacturers Hanover Trust in the US and $50 million syndicated in Bahrain by Allied Bank.

In 1980, the World Bank recognised that the balance of payments deficit of the country was already over 5 per cent of GNP. The economy had a very high ratio of investment, due to the extremely high capital-output ratio, but the return on public investment was low. In fact, the first SAL was granted to attack two basic problems: the uneven structure of protection and the low return on public investment (see Mosley,1991:45). Nevertheless, the World Bank did not impose the strict conditions needed to achieve these two goals. As Mosley's study revealed, the conditions of the lending were not burdensome for the country (see Mosley,1991:50).

The World Bank was particularly concerned about the eleven major industrial projects which had been announced in late 1979, just after the oil price shock, by the Ministry of Trade and Industry, headed by Roberto Ongpin, who was also a member of the Monetary Board.[27] These very ambitious projects aimed to transform the basis of the economy from light (labour intensive) to heavy (capital intensive) industry. Their estimated cost was more than $3 billion. Of the eleven major industrial projects, the World Bank succeeded in persuading the Philippine government to cancel four projects including the steel mill, the aluminium smelter, the paper mill and the petrochemical

[27] For the projects, see Ministry of Industry (1980) "Philippine Industry in the 1980s". The eleven major projects comprised: the Copper Smelter Project (an estimated cost of $350 million), the Phosphatic Fertiliser Project (an estimated cost of $370 million), the Aluminium Smelter Project (an estimated cost of $580 million), the Diesel Engine Manufacturing Project (an estimated cost of $100 million), the Cement Industry Rationalisation Programme, the Coconut Industry Rationalisation Project, the Integrated Pulp and Paper Project, the Petrochemical Complex Project (an estimated cost of $187 million), the Heavy Engineering Industries Project (an estimated cost of $100 million), the Steel Mill Project (an estimated cost of $700 million), and the Alcogas Programme (an estimated cost of $900 million).

complex (see Mosley,1991:51). However, the Bank allowed the others to go ahead if they were justified by rigorous economic appraisal. The Ministry had kept the plan of the industrial projects until 1983. The government failed to improve the macro economy for two years after the first SAL. However it implemented some of the trade liberalisation measures and this was enough to satisfy the World Bank. The second SAL was approved in April 1983.

The IMF's assessment of the economy was also not very critical until late 1983, although the year 1982 was only the second year since 1962 when there was no Stand-by Credit Arrangement between the Philippines and the IMF. The IMF rejected the government's request to secure an IMF credit for 1982, since the Philippine government nearly doubled the rescue funds for 1981 to $400 million from the $193 million which had previously been agreed with the IMF (see, Bello,1985:192). In the following year, although the country's debt had reached an unsustainable level, the Stand-by Credit Arrangement became effective in February 1983. The IMF showed its support for the Marcos government.[28] Later that year, the IMF changed its attitude. In spite of the peso devaluation, the IMF cancelled the last two tranches of the Credit programme for the year, since the government did not achieve the monetary targets for the 1983 credit. However, it was reported that an IMF official gave foreign creditors assurances concerning the Philippine economy as late as August 1983 (see Thompson and Slayton,1985:76).

The massive rescue operation between 1981 and 1983 resulted in a further expansion of the state's role in the economy, a huge public spending, an accumulation of foreign debt and a reduction in foreign reserves. Given the massive rescue operation, the balance of payments problem was predictable. In fact, this had been a repeated pattern in the past: serious balance of payments crisis after massive government spending. This time, the Philippines was hit by its worst ever balance of payments crisis due to the structural weakness of the economy, the unprecedented level of spending through foreign debt and the prolonged delay of adjustment efforts.

[28] See, for example, Times Journal, 20 March 1983.

In early 1981, when the financial system was first hit by the Dewey Dee scandal, the economic policy-makers, including the governor of the Central Bank, did not realise how serious the consequences of the scandal would become. They were still confident about state activism in the economy and their ability to manage the economy. Soon after the Dewey Dee scandal, on 17 January 1981, Marcos announced that he would lift martial law. He stated that it was the most "propitious time" to lift martial law because the nation was at its strongest.[29] He stressed economic gains and the restoration of monetary and banking stability during the martial law period.[30] By 1983, Jaime C. Laya, the Central Bank governor claimed that the economic crisis was "A Crisis of Confidence".[31]

Despite some policy-makers' confidence and continuing support from international financial institutions, it became clear by the early 1980s that the government had failed to develop an efficient state apparatus to coordinate the government's economic projects. State control over economic activities had started to deteriorate in the late 1970s. Conflicts among policy elites over key economic policy were revealed in the late 1970s and deepened as the economic condition deteriorated in the early 1980s. Gerardo Sicat, the former Director General of NEDA and Monetary Board member until 1981, notes that the creation of the Ministry of the Human Settlement by the first Lady, Imelda Marcos, was a critical event in terms of the government's loss of control over the economy. "Eventually, the coordination of the economic programs of government became more difficult. Sometimes, the power centres gave conflicting commands " (Sicat,1985:59). Sicat admitted that, although the state's capacity to raise financial resources through taxes, savings and foreign loans improved, the state was not so successful in controlling public expenditure and private investment (see Sicat,1985:54-59).

[29] See, Bulletin Today, 20 January 1981, p.9.

[30] See, "An Encounter With Destiny", President Marcos' speech on 17 January 1981 proclaiming the termination of the state of martial law at the Heroes Hall, Malacañang Palace, reprinted in Times Journal, 18 and 19 January 1981.

[31] See Laya (1982). For critics against this view, IBON (1984).

Many observers have pointed to the problems of loose control over state-owned enterprises and their subsidiaries.[32] When Marcos first took office in 1966, there were only 37 state-owned enterprises. As the state's involvement in the economy expanded, the number of state-owned enterprises increased to reach 120 in 1975, having more than tripled in the first ten years. By 1984 the number had grown further to 303 (see Manasan,1995: Table 1). According to the Commission on Audit's report in 1984, fewer than two-thirds of all state-owned enterprises were audited by the Commission and several did not even file a financial statement.[33] The defects of the audit system were often revealed.[34] For example, the Ministry of Human Settlement, which had a total of seventy-three subsidiaries, was "notorious for its role as a dispenser of political patronage" (Haggard,1988:94).[35]

The first Lady, Imelda Marcos, who was Human Settlement Minister, Metro Manila governor and board chairman of the National Electrification Administration (NEA), was keen to provide "support" for the rural and urban poor.[36] For example, the Metro Manila Commission planned to spend P4 billion to improve basic services, including housing, water and power supply, from 1981 to 1985.[37] The Movement for Livelihood and Progress, or Kilusang Kabuhayan at Kaunlaran (KKK), was also launched by the Ministry of Human Settlement in September 1981 with high media interest.[38] The initial funds were P1 billion, but within a few months they had doubled. According to the advertisements, the programme was designed to help "the poorest of the poor," especially with interest-free "livelihood loans" of not more than P3,000 and to provide

[32] See, for example, Haggard (1988:94) and Manasan (1995:2-6).

[33] See Commission on Audit, 1984 Annual Financial Report. Volume II: Government-Owned or -Controlled Corporations (Manila: 1985) cited in Haggard (1988:94).

[34] See, for example, Business Day, 3 January 1985 and 4 January 1985.

[35] For a similar view, see Casper (1987:118). See, also IBON Facts and Figures, no.177 (December 31,1985).

[36] See, for example, Times Journal, 1, 2 and 3 January 1980.

[37] See Times Journal, 15 January 1981.

[38] KKK-related articles repeatedly appeared on the front page of daily newspapers such as Bulletin Today and Times Journal in September 1981.

credit for small-scale rural businesses.[39] However, it was reported that proper procedures for examining loan applications were often ignored and this programme was used to redistribute money to local government officials, barangay captains, mayors and governors (see Wurfel,1988:257). It was later revealed that Marcos bailiwick (Regions I and II) and Romualdez territory (Region VIII) acquired a total of P595.98 million or almost 40 per cent of the total P1,512.62 million KKK approved funding at the end of 1985.[40]

Over the issue of economic management and public spending, fierce conflicts between technocrats like Sicat and Virata, and Imelda Marcos and the other leaders of Marcos's ruling party were revealed. As the economy declined, economic management became a critical issue for the regime's survival. Technocrats could not avoid becoming involved in the ensuing political struggle. From 1978, Virata and other cabinet members had been appointed members of the new National Assembly by the President. The caucus meeting of the Marcos ruling party (KBL: Kilusang Bagong Lipunan) played a critical role in decision making. In the early 1980s, the political role of Marcos cronies was legitimised, as they were made members of the central committee of Marcos's ruling party (see Wurfel,1988:237). Eduardo Cojuangco, Roberto Benedicto and Antonio Floirendo became regional party chairmen.

In the early 1980s, under strict budget constraints, Virata and Sicat opposed lavish construction projects like the Heart Centre, the Lung Centre and the International Convention Centre, which were promoted by Imelda Marcos and her allies (see, De Dios,1988:106 and Sicat,1985:62). In the Committee, disagreements between Virata and Imelda Marcos were often uncovered over such issues. As a member of the Monetary Board, Virata was concerned about the huge non-performing assets of the PNB and the Benedicto-owned Republic Planters Bank, which mainly financed sugar planters. In 1982, the Monetary Board called for a stop to the rediscounting of funds through the Central Bank for the sugar industry, since they had reached their legal limit

[39] See, also, Jose Conrado Benitez (1983) "The Kilusan: Breakthrough for the Poor" in Fookien Times Philippine Yearbook, 1982-1983; Times Journal, 13 April 1983, cited in Wurfel (1988:257); and Times Journal, 5 April 1983.

[40] See Business Day, 12 June 1986, p.22.

(see De Dios, 1988:107), although the decision was reversed due to strong opposition from the sugar industry, which was heavily damaged by the sugar price slump. However, the Monetary Board's stance caused Benedicto to be hostile towards Virata. During a KBL meeting in April 1983, the leaders of KBL vehemently accused Virata of economic mismanagement.[41] They blamed government economic policies for being subservient to the IMF. Sicat, the Director General of NEDA who had once expected the martial law regime to bring economic discipline, left the government in 1981. In 1983, it is reported that Virata submitted his resignation but the resignation was not accepted.[42]

Within the military, another key state organisation which played a critical role under the martial law regime, internal conflict was also revealed in the early 1980s. There was a struggle between Ver, allied with Imelda Marcos, and Defence Minister Juan Ponce-Enrile, allied with Fidel Ramos.[43] Although Marcos asserted that he would continue in power, the succession problem occasionally surfaced in the early 1980s with rumours of his ill health. Enrile and Imelda Marcos were often seen as the two strongest contenders for succession.

Outside the state, various forms of anti-Marcos movements also became active during the economic recession. Two elections in three years (legislative elections in 1978 and local elections in 1980) had brought new political activity. The handful of leaders in the Liberal Party had not collaborated with Marcos (see Thompson,1995:102). Heavy spending for ailing companies owned by Marcos's cronies fuelled criticism against the government among business elites. For example, the Makati Business Club was established and became critical of government policy. Influential religious leaders were also critical of the President. The New People's Army, a communist-led militant group, strengthened their power in rural areas. The National Democratic Front (NDF) was formed on the initiative of communist leaders to unite their forces. In Mindanao, Muslim leaders also energised their opposition movements against the government. In

[41] See Business Day (Special Report), 27 February 1984, p.13.

[42] See De Dios (1988:108) and Asian Wall Street Journal, 27-28 May 1983.

[43] See, for instance, Thompson (1995:108) and Wurfel (1988:240).

Manila, urban violence erupted more frequently.[44] The "Light-a-Fire Movement" had started in mid-1979 and attacked symbolic places including the "floating Casino", a favourite project of Imelda Marcos.[45] Although the radical movement was smashed by the authority within a year, the population was surprised by the involvement of elite businessmen. The movement was headed by a Havard-trained businessman, Eduardo Olaguer, who was Vice-President of Business Day, part-time professor of the Asian Institute of Management, chief executive officer of a bus company and an active critic of the Marcos cronies. As security conditions deteriorated, the government lost public support, especially among business.

By late 1982, both the Prime Minister and Finance Minister Virata recognised the depth of the economic problems and thought that spending through foreign borrowing was unsustainable.[46] He often urged reform of the monetary system since the economy suffered severely from fluctuations in exchange and interest rates, due to monetary expansion fuelled by political activities.[47] However, it became much more difficult to control the economy due to a series of events in 1983 which were critical for the Philippine economy and politics. The economic and political crisis had deepened as the power of the authoritarian regime had eroded.

In August, Benigno Aquino, Jr., a leading Marcos opponent, was assassinated at the airport when he returned from the U.S. This brutal murder severely eroded the credibility of the Marcos Presidency. The assassination was a turning point for the anti-Marcos movements. Thompson (1995:115) notes that "antigovernment protests after Aquino's murder", in contrast to previous efforts by opposition politicians, "lasted for months, put Marcos on the defensive, and provided opposition politicians with a noncommunist following". The political instability had an adverse effect on the Philippine economy, since it made the maintenance of foreign credits harder and they were already starting to be withdrawn in late 1982 when the Mexican and Brazilian

[44] For radical movements during this period, see Thompson (1995:83-88), de Dios (1988:81-95) and Wurfel (1988:244).

[45] For the radical movement, see Business Day, 8 April 1986, p.24.

[46] Virata claimed that the main reason for the debt crisis in 1983 was that foreign credits were withdrawn in late 1982, triggered by the Mexican and Brazilian defaults. See, Virata (1984:274-275).

[47] See, for example, Times Journal, 17 April 1983.

defaults occurred (see Virata,1984:274-275). A large number of overseas commercial banks terminated their short-term lending to the Philippines in the last quarter of 1983. In addition, political unrest in the wake of the murder triggered an acceleration of capital flight (see Remolona and Lamberte,1986:113).[48] International reserves fell by over $1 billion between July and October 1983 (Mosley,1991:52). In October, a moratorium on debt repayments was declared by the Philippine government. Immediately after the debt moratorium, foreign exchange and import controls were imposed. In order to improve the government's fiscal and external balance, import tariffs were increased and export taxes were implemented.[49] The substantial depreciation of the peso from June 1983 was allowed to continue until June 1984. Furthermore, in October 1984, when all emergency exchange controls were lifted and the exchange rate was allowed to be determined by market forces, the peso depreciated sharply.

Even worse, in late 1983, "the most shocking economic scandal" was uncovered by an IMF team that inspected the Central Bank account (de Dios,1988:109). The inspection team reported that they had discovered an overstatement of the country's dollar reserves by $600 to $800 million, or 42 per cent to 58 per cent of the reserve. The international reserve had been overstated through manipulated transactions between the Central Bank, the PNB and its subsidiary, the National Investment Development Company (NIDC), and the Philippine National Oil Corporation.[50] The scandal seriously hurt the credibility of the government, which had already been eroded. Distrust was angrily voiced by the international financial community. Although governor Laya insisted that the incident was caused by statistical errors and some of them had been made before he became the governor, he resigned as governor of the Central Bank.[51] It must be noted that, although his explanation did not entirely persuade the international financial community, Marcos still retained Laya in his cabinet. He became the Minister of

[48] Boyce points out that this widely accepted version of the timing of capital flight has been disputed. Statistical evidence reviewed by his study suggests that capital flight in fact peaked in 1981 (Boyce,1993:258 and notes 26). For further analysis , see Boyce (1993:279-302).

[49] Lamberte, et al. (1985) reviews the government's response to the balance of payments crisis between 1983 and 1985.

[50] For the overstatement, see for example, Business Day, 13 March 1984, p.2 and 24 April 1984,p.2.

[51] See FEER, 5 January 1984:48-50; FEER, 29 March 1984:56-59; Times Journal,18 January 1984; and Javate-de Dios (1988:517-522).

Education, a key ministerial post.

Between 1981 and 1983, the government had conducted massive rescue operations to prevent further decline of the economy and to support the regime. The Central Bank and other state financial institutions were actively involved in the rescue operations. The Central Bank provided huge amounts of rescue funds, a measure which it had never previously taken. It became evident that to avoid further economic deterioration, curbs on public spending and changes in banking policy were necessary. Yet, threatened by a constellation of political institutions dependent on the resumption of elections and on the dictatorship losing legilimacy, the President was more concerned about generating broad support through public spending and protecting the business interests of his close cronies. The interests and capacities of the President in implementing necessary policy reform measures were undermined. In spite of the massive rescue operation, it proved impossible to restore the monetary and banking stability under the Presidential dictatorship in decline. The worst economic and banking crisis was yet to come.

Crisis and Reform of the Banking Sector between 1984 and 1986

Between 1984 and 1986, the banking sector faced its most serious turmoil. During the Philippines' worst ever economic recession, state banks, which formed the largest share of the entire banking sector, suffered huge losses. Since foreign credit was no longer easily available, the massive rescue operation for ailing banks was unsustainable. Election related spending reemerged as a serious threat to monetary stability. Both the IMF and the World Bank had maintained an exceptionally strict stance on lending conditionality in 1984 and 1985. Facing economic turmoil, scarce foreign credits and stronger pressures from the IMF and World Bank, the government finally implemented draconian stabilisation measures after the 1984 elections.

Faced with its worst ever economic and banking crisis, the Central Bank had altered previous policies to restructure the banking sector. The new governor, Jose B. Fernandez, Jr., took a tough stance on closing insolvent banks. The Central Bank also reformed monetary policy and foreign credit policy. Nevertheless, despite some regulatory reforms, the Marcos government did not improve the economy and banking

sector. After prolonged delay, the implementation of radical stabilisation measures led to a severe economic recession. The new Central Bank governor's initiative to rebuild the banking sector was not fully supported by the President. The government did not solve the most serious problem in the banking sector, which was that of huge non-performing assets in state banks. The government was not able to initiate the rehabilitation of the PNB and DBP, since these reforms potentially led to further job losses and closure of businesses which relied on state bank credits. Without financial support from foreign creditors, the government did not have incentives to implement banking reform. Negotiations with the IMF and the World Bank were halted, since the Philippine government consistently resisted reforming the monopoly of the sugar and coconut industries, which were dominated by Marcos's close cronies. As the Marcos authoritarianism declined, it became increasingly difficult to restore the stability of the banking sector.

In January 1984, when the economy was teetering on the brink of collapse, Jose Fernandez became the Central Bank governor. He had to face the worst balance of payments problem in the entire postwar era. Political uncertainty fuelled a sense of crisis among local business communities and foreign investors. Because of dishonest reporting about foreign reserves under the previous governor, Jaime Laya, the Central Bank had lost its credibility among the international financial community. Fernandez was chosen from among a very small number of candidates to meet the demands of the job. In 1989, Wilfrido C. Tecson, the President of the Bankers Association of the Philippines recalled: "When Jobo accepted the Central Bank governorship, no one in the banking community envied him. In fact, most of us really felt that he had for one brief moment lost his sanity".[52]

After completing his MBA degree at Harvard University, Fernandez started his banking career as assistant to the President of the Philippine Bank of Commerce (PBC) in 1949. The PBC occupied a prominent position in the banking community, as it was the

[52] See "Closing Remarks of the Bankers Association of the Philippines President" by Wilfrido C. Tecson at the joint luncheon of the BAP, Makati Business Club and Management Association of the Philippines in honour of Governor Jose B. Fernandez Jr. on January 12, 1989, reprinted in *The Central Banker* January-February 1989, p47.

first Filipino commercial bank. Miguel Cuaderno, who had been president of the bank since it was established in 1938, left the PBC to become the first governor of the Central Bank in 1949. The vice-president of the PBC, Alfonso Calalang, also joined the Central Bank as deputy governor. Later, he also became the governor of the Central Bank. Fernandez's boss, the new president of the PBC was Don Jose "Pepe" Cojuangco Sr., father of Corazon Aquino, who had been a congressman and close associate of President Quezon in the 1930s. In severe economic circumstances, President Marcos appointed Fernandez, who had had a tie with his opposition leader, Benigno Aquino, who was assassinated shortly before Fernandez's appointment. Don Jose "Pepe" Cojuangco Sr, Benigno Aquino's father-in-law, was a very influential person in Fernandez's career in the banking sector.

Fernandez left the PBC bank and established the Far East Bank and Trust Company in 1960,[53] which had steadily expanded its businesses during the 1960s and 70s. In 1983, the Far East Bank was the fifth largest private commercial bank in terms of assets in the Philippines. The Bank had the largest net income of private commercial banks in the same year.[54] Fernandez had experience as a representative of the banking community, when he was the President of the Bankers Association of the Philippines for three consecutive terms from 1971 to 1974, and a member of the Joint IMF-CBP Banking Survey Commission in the early 1970s. Fernandez also had close relationships with American and Japanese bankers, mainly through share-holding arrangements of the Far East Bank. In 1973 and 1974, the Far East Bank established relationships with Chemical Bank and Mitsui Bank respectively. Each bank bought 12.5 per cent of the share-holdings of the Far East Bank. Fernandez was the only Filipino banker at that time who sat on the international advisory board of Chemical Bank.

[53] For a brief history of the Far East Bank, see Far East Bank and Trust Company (1990) "A Vault of Memories: Far East Bank's Thirty-year Chronicle" (Manila); Espiritu, Octavio V. (1990:116) "Far East Bank: 30 years... into forever", in 1990 Fookien Times Philippines Year Book and Hutchcroft (1998:102-104). See also Business World, 27 February 1990, "Special Feature: CB; a changing of the guards".

[54] See Business Day, 1983 ed., "1000 Top Corporations in the Philippines".

Due to the legislative election in May, 1984 was a very difficult moment in which to control the money supply. As of the third week of April, the Central Bank's credits outstanding to the national government amounted to P18.23 billion.[55] The inflation rate in Metro Manila soared to 40% in February.[56] In spite of Fernandez's resistance,[57] it was reported that Marcos's party, the KBL, had access to limitless government funds for the election. P4.6 billion cash was printed during the campaign.[58]

Until the election was over, the Central Bank could not tighten monetary policy, in spite of consistent pressure from the IMF and the World Bank. After the election, the new Central Bank governor, Jose "Jobo" Fernandez took initiatives to reform monetary and banking policy. Facing the threat of uncontrollable inflation, further capital flight and peso depreciation, the Governor decided to adopt a radical measure to stabilise the economy. After failing to attract investors for a series of Central Bank bills (Central Bank Certificates of Indebtedness: CBCIs) in 1983, from September 1984 the Central Bank started to issue CBCIs ("Jobo" bills) which were sold at very high interest rates (40 per cent on 30-60 bills in September). As a result, domestic interest rates increased rapidly. The Manila Reference Rate jumped to 25.75 per cent and bank lending rates jumped to 30 per cent in September 1984 (Lamberte, et al., 1985:33). Due to this issue of Central Bank bills with high interest rates, formal commercial lending came to a virtual standstill. Between 1983 and 1985, total liquidity fell by almost one third in real terms (Lim,1996:65, Table 1a). This radical measure "very nearly killed the patient" (Mosley,1991:52). In the real economy, GDP fell sharply by over 10 per cent between 1983 and 1985, investment fell from 27 to 16 per cent of GDP and measured unemployment rose from 7.9 to 11.1 per cent (ibid.). Due to the serious delay in taking decisive action to stabilise the economy, the measures were much more painful than

[55] Business Day, 10 May 1984, p.3. See, also Business Day, 1 May 1984, p.2 and Business Day, 14 May 1984, p.6.

[56] Business Day, 3 May 1984, p.2

[57] Reports of the dispute between Fernandez and Marcos over the funds for projects connected with the election date back to the beginning of Fernandez's governorship. See, for example, FEER, 2 May 1984:13.

[58] This figure, P4.6 billion, is cited in FEER, August 30,1984:24, Wurfel (1988:287) and Thompson (1995:125). Lamberte (1989:51) also roughly estimated that the government pumped around P5 billion into the economy through election-related spending activities a few months before the National Assembly election of May 1984.

they should have been.[59] In its worst ever economic recession, the Central Bank faced the overwhelming task of rebuilding the banking sector.

Shortly before the implementation of the radical stabilisation measure, Fernandez declared a "crusade" in August 1984 to rebuild the banking system.[60] First of all, the Central Bank announced that it would stop rescuing all banks, including insolvent ones, to protect financial stability. He promised to take a strict stance in dealing with the problem of the weak banks, and prosecute those responsible for fraud, mismanagement, and DOSRI abuses. Second, the Central Bank sought to support the consolidation of the stronger and more conservatively managed banks by improving their public image. The Central Bank also hoped to bring funds back into the banking system by restoring public confidence and solving "image" problems in the banking system. Third, the Central Bank encouraged mergers and acquisitions among banks by suggesting and arranging options.

The Central Bank's decision to close insolvent banks was its most controversial decision, which had a significant impact on the banking sector. In addition to the limitation of government resources, the effectiveness of a policy which aimed essentially at rescuing "all" ailing banks, including insolvent ones, was seriously in doubt by 1983. Since massive rescue funds were allocated to insolvent companies owned by Marcos cronies, the Central Bank was severely criticised because of the further misuse of public funds. After all, the rescue operation did not improve the economy and the banking system.

After the declaration of the "crusade", the Central Bank closed the Royal Savings Bank (RSB), one of the leading thrift banks with 23 branches in Southern Tagalog. The Bank had already closed unofficially on 29 June 1984 after losing P100 million in deposits in less than one month and the Central Bank sought investors to rescue the bank.[61] As Lamberte (1989:27) observes, depositors took the closure of RSB as a signal that

[59] See Sicat (1985:26) and Business Day, 8 January 1985, p.9.

[60] See Business Day, 7 January 1985; FEER, 13 September 1984:56; FEER, 7 May 1987:81; and Hutchcroft (1998:174).

[61] One of potential investors was Metrobank but the negotiation was not successful. See Business Day, 16 April 1984,p.7.

showed the authority's decisiveness. In this climate of economic and political instability, many depositors started moving their funds into more liquid banks. Between 1984 and 1986, the Central Bank closed another three banks, including Banco Filipino Savings and Mortgage Bank (BF), Philippine Veterans Bank (PV) and Pacific Banking Corporation. All the banks closed had suffered huge losses due to mismanagement and DOSRI loans.

The evaluation of the assets and liabilities of banks inevitably left some ambiguity. However, it must be noted that the Central Bank's authority to handle the banking crisis was undermined by the direct intervention of President Marcos. During this period, the Monetary Authority's decisions were particularly arbitrary, due to this frequent intervention. All members of the Monetary Board, the decision-making body of the Central Bank, were appointed by the President and the majority of them were members of the Cabinet. Two of the three seats for private sector representatives were left vacant. Between 1984 and 1986 the Monetary Board consisted of Jose Fernandez (the Chair of the Board and the Central Bank governor), Cesar E. A. Virata (Minister of Finance), Roberto V. Ongpin (Chair, Board of Investments and Minister of Trade and Industry), Vicente B. Valdepeñas, Jr. (Director General of NEDA) and Cesar A. Buenaventura (private sector representative, President, Filipinas Shell Petroleum Corp).

After Roberto V. Ongpin, who had planned ambitious development projects, was once convinced by other Monetary Board members to suspend these projects due to the economic conditions, there was a broad consensus with regard to the importance of economic stabilisation measures and the redirection of banking policy to stop massive spending. However, the policy of the Central Bank was not fully supported by the President. Vicente B. Valdepeñas, Jr. (Director General of NEDA), who joined the Cabinet and the Monetary Board in July 1983, recalled that there were not many opportunities to meet the President and discuss economic policy during his tenure.[62] As the regime was losing support during the severe economic and banking crisis, President Marcos intervened directly in the Monetary Board's decision-making.[63] The

[62] Interview, Dr. Vicente Valdepeñas, Jr., 16 June 1998.

[63] Singson, senior deputy governor under Fernandez, notes that on at least two occasions he (Fernandez) dared to defy the President by refusing to accede to certain unreasonable requests (*Tinig Bangko Sentral*, July-Aug 1994:20).

KBL (Marcos ruling party) caucus became more important in terms of economic policy-making, while the Monetary Board of the Central bank was losing support from the President.[64]

The rescue of the Republic Planters Bank and the Banco Filipino were prominent examples. The Republic Planters Bank (RPB), which was controlled by Roberto Benedicto, a close presidential crony, had reserve deficiencies during the economic crisis. However, through a presidential letter of instruction, the Central Bank allowed penalties for RPB's reserve deficiencies to be accounted for as a central bank advance.[65]

The closure of Banco Filipino Savings and Mortgage Bank (BF) was the most controversial case. The Banco Filipino was founded by the Aguirre family in 1964. As a thrift bank, the bank was the second largest in terms of assets and had the largest branch network (more than 80 branches in Metro-Manila alone). A few days after the Central Bank closed RSB, Banco Filipino unilaterally declared a "bank holiday" when the Central Bank refused to grant it further assistance. According to the Central Bank, Central Bank examiners had discovered a misuse of P979 million of emergency aid which had been provided by the Central Bank from early June (FEER, 2 August 1984:78-79). They found that payments from the bank to depositors in the same period totalled only P670 million (ibid.). However, a little later President Marcos ordered the Central Bank to provide BF with a P3 billion emergency loan. Nonetheless, the bank failed to reverse its rapidly deteriorating financial situation. Finally, CB closed it on 25 January 1985. At the time of its closure, BF had more than two million deposit accounts amounting to P897 million. The exact reason why Marcos attempted to rescue the bank through direct intervention was not entirely clear. However, Marcos might have felt that it was necessary to scotch the rumours that the Aguirre family was being punished, since they were not on the Marcos side in the parliamentary elections.[66] The ugly rumours and the closure of the bank, whose depositors were low-income workers

[64] See, for example, Business Day, 3, 4 and 7 January 1985. The nomination of Jose Fernandez as the Central Bank governor was also the result of consultation with KBL leaders. See Business Day, 12 January 1984, p.3.

[65] See FEER, 26 July 1984:48; FEER, 13 September 1984:57 and Manapat (1991:125).

[66] See FEER, 30 August 1984:48-49 and 26 December 1991:68-69 and Hutchcroft (1998:178).

and small entrepreneurs, would fuel further social unrest and opposition movements during the economic crisis.

The Central Bank took a strict stance regarding the closure of Banco Filipino, in comparison with other banks which also suffered from mismanagement and DOSRI abuses. There was speculation that the personal conflicts between Fernandez and the Aguirre family might have been one of the reasons for the fierce disputes between the regulator and the regulated (see Hutchcroft,1998:178-179).[67] Nonetheless, there was also solid evidence that the bank had violated the law. 57.6 per cent of the total loan portfolio was extended to Aguirre-related companies as of 31 July 1984.[68] The Central Bank justified its strict stance vis-à-vis the Banco Filipino was by pointing to this clear violation of regulations. Taking decisive action against insolvent banks was a positive step forward in rebuilding a healthier banking sector, although this was not fully supported by the President. Rescuing all banks, including insolvent ones, without exception might have provided grounds for a "moral hazard" problem.

During the balance of payments crisis, there were also major changes in the Central Bank's selective credit policy. Rediscount windows, which had been a main instrument for selective credit, became far less important in financing the assets of the commercial banking sector.

By the mid-1980s a substantial amount of credit was provided by the Central Bank to commercial banks through the Central Bank's rediscount window. However, by 1985 the Central Bank had practically closed the subsidised rediscount windows. Instead of quoting fixed discount rates, it started to peg them on the 90 day Manila Reference Rate (MRR90). Since the MRR is based on actual transactions, credit allocation through rediscount windows can be seen as an instrument of short-run stabilisation rather than an instrument for development finance (Lamberte, et al.,1985:32). Tighter eligibility rules for rediscount windows were also imposed in March 1984.

[67] The legal battles between the Central Bank and the Aguirre family continued until the end of the 1990s.

[68] For details of the violations, see Business World, 20 - 24 May 1991.

In the early 1980s, the Central Bank encouraged private banks to acquire foreign credits through foreign swaps which generously transferred currency risks from the private banks to the Central Bank (Dohner and Intal, Jr.,1989:174). Between 1983 and 1984, total swaps increased both in absolute terms and as a proportion of total commercial bank assets. However, from 1985 the Central Bank stopped using foreign swaps. As revealed later, foreign swaps were an extremely risky strategy for the Central Bank, due to the potential for further devaluation.

These major changes in credit policy were significant in terms of favouritism in the banking sector, since rediscount windows and foreign currency allocation had been a key instrument of "preferential" credits.[69] In fact, in spite of the massive rescue operation, rapidly growing conglomerates, including financial institutions in the 1970s, which were owned by Presidential cronies and relied heavily on financial resources allocated by the state, had lost their businesses during the economic crisis. Notable examples were Herminio Disini's Herdis group of companies, Ricardo Silverio's group of automobile and financial companies and Rodolfo Cuenca's CDCP (the biggest construction company) and his other companies.[70]

It should be noted that not all the banks were distressed by the economic turmoil. In the banking sector, some banks managed to expand their businesses in the severe recession. Following Central Bank policy, leading private commercial banks consolidated their position through mergers. The Bank of the Philippine Islands (BPI) acquired Family Bank & Trust Co. (FBTC). Philippine Commercial and International Bank (PCIB) absorbed a successful bank, Insular Bank of Asia and America (IBAA). Far East Bank acquired the Pacific Bank which was closed in 1984. In 1984, while state-owned banks, namely the PNB and DBP, suffered huge losses, big private banks succeeded in making profits. In particular, leading private commercial banks, including the Bank of the Philippine Islands (BPI), Philippine Commercial & International Bank (PCIB), Metropolitan Bank and Far East Bank consolidated their positions in the

[69] See Patrick and Moreno (1985:347,351) and Hutchcroft (1993b:172).

[70] Silverio's businesses declined, in part, because he lost favour with the President. Doner (1991:182) notes that Silverio's car manufacturing business (Delta) was already in deep trouble regardless of its owner's financial problems.

banking sector (see, FEER, 25 April 1985:94). In 1984, Far East Bank had a net income (profits after tax) of P236 million, an increase of 50.2 per cent on the previous year, while the Bank of the Philippine Islands posted a net income of P217 million, up by 39.8 per cent. Metro Bank had a P150.4 million net income, an increase of 30 per cent. Philippine Commercial & International Bank (PCIB) also increased their profits, by 70 per cent, and had a P102 million net income. The rising profits of big commercial banks during the serious economic recession only revealed the distortions of the Philippine banking sector in the early 1980s.

In the 1970s, the rapid growth of some banks, including Allied Bank, United Coconut Planters Bank, Traders Royal Bank and Republic Planters Bank, which were controlled by close Marcos cronies, distinctively suggested influence of state activism and the advantages of Presidential favours. These banks also received massive rescue funds in the early 1980s. However, during the economic and banking crisis, the tight control of the President and his cronies on the economy and the banking sector were loosening. The relationship between Presidential favours and success in the banking business became ambiguous during this period. During the economic crisis, big private commercial banks were successful in making profits, while many bank owners and officers supported the opposition to Marcos.

The Bank of the Philippine Islands was headed by Enrique Zobel, who was the founding chairman of the Makati Business Club (MBC). This business organisation was formed in 1981 by business leaders who shared a sense of crisis regarding the control over the economy by the President's cronies, massive behest loans through state banks, media control, the rise of poverty and the increase in social unrest and radical left-wing opposition.[71] The MBC aimed to be a "forum for constructive ideas". In fact, they became a rallying point for members of the business community who wished to voice criticism against government policies and the Marcos regime. The MBC was "extremely active" in Makati demonstrations which called for Marcos's resignation after Benigno Aquino's assassination (see, FEER, 21 June 1984). Before the legislative elections of May 1984, the MBC clearly expressed their dissatisfaction with the

[71] See, Speech by Cesar Buenaventura, Vice Chairman, MBC, printed in *Inside MBC*, March 1997.

government.[72] They urged the adoption of an austerity programme and stressed the importance of political reform to rebuild the economy.[73] A number of MBC members were also supporters of NAMFREL (the National Citizen's Movement for Free Elections), which played a critical role as a monitor of polling during the 1984 and 1986 elections.

Another leading member of the Makati Business Club, Jaime Ongpin (brother of Roberto Ongpin), who was president of Benguet Corp. (a leading mining company), was an outspoken critic of government economic policies. While he was actively involved in activities against the Marcos government, he kept his position as director of Philippine Commercial & International Bank (PCIB),[74] whose large shares were supposed to be acquired by investors led by Benjamin "Kokoy" Romualdez (the brother of Imelda Marcos).[75] The President of the PCIB, Antonio Ozaeta, was also one of the core members of the MBC.

Another "winner" during the economic crisis, Metro Bank, was also known as a tightly managed bank with solid business bases in the local Chinese community. The Bank was founded in 1962 by George Ty with Placido Mapa, Sr. (former Minister of Agriculture), Don Pio Pedrosa (former Minister of Finance) and Emilio Abello (former Ambassador to the U.S.). Since then the Metro Bank had been steadily growing.[76] Although the Bank had close connections with key economic policy-makers, its success seemed to be secured by keeping a distance from Marcos cronyism during this

[72] See, "A Report on the Political Situation" a speech by Jaime Ongpin at the Makati Business Club on 29 February 1984, reprinted in Business Day, 1-2 March 1984, p.5. See, also Business Day, 5 March 1984, p.5.

[73] See Business Day, 26 April 1984, p.16 and Business Day, 27 April 1984, p.15.

[74] See, Philippine Commercial & International Bank, Annual Report 1983.

[75] See, Manila Times, 10 June 1986 and Hutchcroft (1998:137).

[76] For a brief corporate history of the bank, see George Ty, "Thirty Years of Metrobank", in Fookien Times Philippines Yearbook 1992; Sobrepeña (1998) and FEER, 9 November 1995:60-64.

period.[77] George Ty, one of the most successful businessmen in the Philippines, was careful enough to avoid political interference.[78]

The success of the Far East Bank often prompted speculation about favouritism on the part of the Central Bank governor, Jose Fernandez, who was the founder of the Far East Bank.[79] In particular, the acquisition of the Pacific Bank's assets by the Far East Bank was criticised in the banking community since the deal was favourable to the Far East Bank (See, FEER, 7 May 1987:82). However, the success of the Far East could hardly be explained by close connections with the Central Bank alone. Even before Fernandez became the Governor of the Central Bank, the Far East Bank had steadily expanded its business. Antonio Gatmaitan, former president of Commercial Bank of Manila, commented on the Pacific Bank deal by observing that "it was an obvious but very small" illustration of favouritism in the banking sector.[80]

The case of the Rizal Commercial Banking Corporation (RCBC) is worth noting. Thompson's study (1995:87) revealed that Alfonso Yuchengco, the Chairman of the Board of the RCBC, one of the largest commercial banks, backed the Light-a-Fire-Movement (LAFM), a radical urban terrorism movement. The wealthy businessman provided most of the funding for the LAFM. Although the RCBC did not expand its business successfully in comparison with other more successful big banks, the bank was able to maintain a healthy condition during the economic crisis. His involvement in the radical opposition movement did not seriously affect his banking business.

During the economic crisis, due to the failures of state banks and crony banks, leading private commercial banks consolidated their position regardless of their political ties.

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[77] After his Governorship of the Central Bank, Andres Castillo joined Metro Bank as President. Placido Mapa, Jr., who was former President of PCIB, Director General of NEDA and President of the PNB under the Marcos government, also joined the Metro Bank after he resigned from these government posts and became President in 1989. Edgardo Espiritu was the President of the Metro Bank before he was appointed President of the Philippine National Bank under the Aquino government.

[78] He has been seen as "the lone wolf of Philippine banking" (FEER, 9 November 1995:60).

[79] For detailed arguments, see Hutchcroft (1998:180-181).

[80] Interview, Antonio Gatmaitan, 3 June 1998.

After the Dewey Dee scandal, the big commercial banks immediately tightened their credit policy, while the state banks were actively involved in rescue operations. They provided funds strictly to viable customers only. In the uncertain climate in the banking sector, which was intensified by banking closures, depositors moved to the big banks, which seemed to be stable. Big commercial banks increased investments in national government securities with low risk.[81] Issuing the "Jobo" bills with high interest rates was certainly beneficial for the big commercial banks.

Although the big commercial banks had grown during the economic and banking crisis in the early 1980s, the state banks, namely the PNB and DBP, which had dominated the banking sector, could not avoid huge losses. In fact, both banks had become technically bankrupt by 1986. To support the state-led industrialisation strategy of the Marcos government, the two state-owned banks aggressively expanded their lending activities in the latter half of the 1970s, as state-allocated resources increased due to foreign borrowing. In the early 1980s, because of the financial instability created by the Dewey Dee scandal, the state-owned banks were actively involved in rescue operations on behalf of the government, unlike the other big private banks, which tightened up their lending activities during the recession. Between 1980 and 1984, the total assets of the state-owned banks more than doubled: the PNB's assets rose from 38,652 million pesos in 1980 to 87,196 million pesos in 1984 and the DBP's assets from 27,086 million pesos to 66,800 million pesos.

By 1985, the non-performing assets of the PNB and DBP had become a matter of serious concern for economic policy-makers. In 1984, the PNB, in its first loss since World War II, registered a P1,102 million loss. And the DBP also made a loss for the first time in its 38-year history. It's losses amounted to P6,641 million. Between 1983 and 1985, the total losses of the PNB and DBP amounted to nearly P30 billion. The Marcos government was forced to pump in P5.6 billion in 1984 just to keep the DBP functioning, despite restrictions which allowed the bank to lend only from previously established, fully funded credit lines (FEER, 3 October 1985:49). In 1984, the government cash flow to three public financial institutions including the PNB (P6.1

[81] The Commercial bank investments in securities rapidly increased during the economic recession, and had reached P22.3 billion by the end of 1984 (Business Day, 1 May 1984,p.2)

billion), the DBP (P5.8 billion) and the PGC, the Philippine Export and Foreign Loan Guarantee Corporation (P0.8 billion), amounted to P12.7 billion (2.4 per cent of GNP).[82]

In spite of the emergency in 1983, the Marcos government did not initiate reform of the state-owned banks. Facing a serious balance of payments problem, the government's expenditure was strictly monitored by the IMF after the declaration of a moratorium on principal debt repayments. To rehabilitate the PNB and DBP, the removal of non-performing assets from their books was essential, but the government could not form and implement a rehabilitation plan without considering the impact on negotiations with the IMF. During the severe balance of payments crisis of late 1983-1986, the IMF tightened conditionality, increased surveillance and demanded policy reform as a condition of further support. In order to improve the balance of payments problem, the government implemented macro-economic reforms including foreign exchange and import controls, tax reforms such as increase in import tariffs and export taxes, government expenditure cuts and rigid control of the money supply. In 1984, the Central Bank issued high-interest bills ("Jobo" bills) to dramatically tighten monetary policy after peso devaluation and the increase of spending for the legislative elections. Thanks to these reforms, by 1985 the balance of payments problem started to improve. Nevertheless, the IMF and other creditors maintained a tough stance in negotiations for further support.[83]

Negotiations with the IMF stalled, mainly due to the issues of government expenditure and the dismantling of monopolies in the sugar and coconut industries.[84] The coconut and sugar industries had become the targets of the first-ever joint reform effort of its kind by the IMF and the World Bank (FEER, 31 October 1985:103-110). Dismantling the monopolies in the Philippines' main agricultural sectors was seen as a significant

[82] These figures were in "the Philippines's letter of intent to the IMF" reprinted in Business Day, 2-4 January 1985.

[83] The strict stances of the IMF and other creditors were reported by FEER. See FEER, 9 May 1985:98-99; FEER, 30 May 1985:12; FEER, 6 June 1985:12; FEER, 1 August 1985:8; FEER, 29 August 1985:62-63; FEER, 10 October 1985:10; FEER, 24 October 1985:12; FEER, 31 October 1985:103-110; and FEER, 28 November 1985:8.

[84] See, for example, Business Day, 11 May 1984, p.2 and Business Day, 14 May 1984, p.6.

indication of the government's commitment to reform the economy, since they were controlled by close Marcos cronies: the coconut industry by Eduardo Cojuangco and the sugar industry by Roberto Benedicto. In addition to economic domination, both of them played critical roles in the ruling party, Kilusang Bagong Lipunan (KBL). Both of them became regional party chairmen when President Marcos created and gave prominence to the caucus of the ruling party. At that time, the determination of the IMF to reform the agricultural sector was unusual, since the IMF normally limited itself to short-term stabilisation targets such as control of the money supply, budget deficits, public sector outlays and exchange-rate policies.

Because of a lack of financial incentives from the IMF and World Bank and the political instability intensified by the assassination of former Senator Benigno Aquino, Jr. in August 1983, a major restructuring of the state-owned banks with large layoffs was avoided by the President. A rehabilitation plan involving the merger of the PNB and DBP was proposed by Prime Minister Virata, but it was suspended by the President.[85] Immediately before the Presidential election of February 1986, President Marcos announced that the PNB and the DBP would not be merged as long as he was President.[86] It was later disclosed by former Prime Minister Virata that the wife of former presidential advisor on legal affairs Manual M. Lazaro, who was an official of the DBP employers association, had successfully lobbied the President to block the PNB-DBP merger.[87]

The first quarter of 1986 was the most turbulent quarter ever experienced by the Philippine financial system. The presidential election and the EDSA revolution adversely affected the economy and the banking sector. Political events led to record highs in liquidity levels.[88] It is reported that during the two-month presidential election campaign, a desperate Marcos administration pumped nearly P10 billion in additional liquidity into the economy (FEER, 8 May 1986:85). In addition, another P2.8 billion was released in the two weeks that followed the election to counteract the effects of a

[85] See FEER, 8 May 1986:86. Also see, Business World, 22 July 1996 and FEER, 18 July 1985.

[86] See Business Day, 5 February 1986, p.2.

[87] See Business Day, 12 May 1986, p.2.

[88] It was predicted in the beginning of 1986. See, for example, Business Day, 8 January 1986, p.5 and 10 January 1986.

campaign for civil disobedience launched by opposition leader, Corazon Aquino, to protest against the widespread fraud during the elections (ibid.). Aquino urged depositors to pull their money out of banks which had close connections with the Marcos family and its cronies.[89] Massive withdrawals of deposits occurred in the six banks under government control and in some of the others controlled by Marcos's cronies including Security Bank, United Coconut Planters Bank, Republic Planters Bank, Traders Royal Bank, Union Bank, and Commercial Bank of Manila.[90] When the new government took over, cronies and political allies of former President Marcos withdrew their deposits from banks for fear of sequestration (Lamberte,1989:33).

Conclusion

The Philippine economy and the banking sector faced their worst decline ever in the early 1980s. Faced with the economic and banking crisis, the interests and capacities of the President to implement reform were severely undermined by the constellation of political institutions questioning the legitimacy of the dictatorship and demanding the resumption of electoral contests. While the dictatorship was in decline, the Marcos government failed to restore public confidence in the banking sector.

During this period, the political institutions centred on the dictatorship were changing. Marcos resumed elections in 1978 and officially lifted martial law in January 1981. The President continued to have a decisive influence on policy-making, due to his unlimited power to issue decrees. However, although they were unfair, the restoration of elections activated political opposition. As the regime's survival came increasingly to depend on the outcome of these political contests, election-related spending reemerged as a serious threat to monetary stability. The tight control of the President began to fade and the inability of the authoritarian regime to redirect the economy was revealed during the economic crisis. As the economic crisis deepened, fierce conflicts among policy elites over economic policy surfaced. The Marcos government had been losing the support of

[89] This controversy was reported by a business daily. See, for example, Business Day, 17 February 1986, p.16; 18 February 1986, p.2,p.5,p.18; and 20 February 1986, p.2,p.20.

[90] For the campaign for civil disobedience and its consequence on the banking sector, see Almendral (1987:209 and 734-737); Hutchcroft (1998:188); and FEER,10 July 1986:79 and 23 May1991:65.

the IMF and the World Bank due to its dishonest reporting of foreign reserves, uncontrollable government spending, Presidential cronyism and the lack of commitment to reform the economy. Political events such as the brutal murder of the opposition leader, Beniguno Aquino, triggered various opposition movements against the dictatorship and damaged business confidence in the country.

During the economic crisis, the disputes between KBL leaders and Monetary Board members, including Prime Minister Virata, who urged tightening of fiscal and monetary policy, became fiercer. After all, the President, who still wielded absolute power over policy-making, did not support the austerity measures promptly enough. The Central Bank was not able to tighten monetary policy nor to stop public spending until its foreign credits line was shut down.

During the 1984 elections, monetary stability further deteriorated. After repeated delay, the implementation of the radical stabilisation measures by the Central Bank caused severe economic recession. The new Central Bank governor, Jose Fernandez, took initiatives to rebuild the banking sector but his initiatives were not fully supported by the President. Despite some regulatory reform, the authoritarian government was not able to improve the economy and the banking sector. With the Presidential dictatorship in decline, the Central Bank's attempts to restructure the banking sector were often undermined by the direct intervention of the President, whose short-term goal was the survival of his regime. Critical reform, especially the rehabilitation of the state banks, was not implemented. In the banking sector uncertainty continued into the next administration. Ailing state banks, which had dominated the Philippine banking sector were symbolic of the state of banking at the end of the Marcos dictatorship. The stability of the banking sector was not restored under the Marcos dictatorship. The Marcos government left the banking sector in ruins.

Table 2-1. Reserve Money and Central Bank Assistance to Financial Institutions (in Billion Pesos)

Period Year (Quarter)	Reserve Money (1)	Assistance to Financial Institutions (2)	(2)/(1) in Per Cent
1983(4)	27.7	1.2	4.3
1984(1)	24.8	1.9	7.7
(2)	27.1	3.2	11.8
(3)	28.7	9.4	32.8
(4)	33.4	10.9	32.6
1985(1)	30.5	12.2	40.0
(2)	31.6	12.5	39.6
(3)	32.6	13.3	40.8
(4)	38.0	13.8	36.3
1986(1)	40.4	19.1	47.3
(2)	38.0	13.9	36.6
(3)	39.5	13.8	34.9
(4)	50.0	12.7	25.4
1987(1)	48.1	14.3	29.7
(2)	49.0	15.5	31.6
(3)	49.7	15.4	31.0
(4)	56.9	15.4	27.1
1988(4)	67.2	15.0	22.3
1989(4)	92.8	15.0	16.2
1990(4)	108.7	14.8	13.6
1991(4)	129.3	14.2	11.0
1992(4)	144.8	13.9	9.6
1993(4)	171.7	4.2	2.4
1994(4)	182.4	4.0	2.2
1995(4)	212.7	3.2	1.5

Note: Central Bank's assistance to financial institutions includes emergency loans and over drafts.

Sources: Central Bank, Quarterly Economic and Financial Report (various quarters), cited in Lamberte,1989, Table 14
BSP, Selected Philippine Economic Indicators, April 1996, Table 14

Chapter 3.

The Transition from Marcos to Aquino and Banking Sector Reform

Introduction

When Aquino came to power in 1986 after the twenty-year Marcos era, the Philippines was still in deep economic turmoil. The national economy had recorded negative growth for the previous two years. Unemployment and under-employment rapidly increased during the recession. The huge foreign debt and non-performing assets of the state-owned banks were symbolic of the failure of economic management under the Marcos government. Although some measures had been implemented to stabilise the economy under the Marcos government, the new government had to face the demanding task of rebuilding the economy and banking sector in a climate of political uncertainty.

In spite of some successful economic reform initiatives, including privatisation, trade liberalisation, export promotion, and rehabilitation of state-owned banks, many observers stressed the continuity of the Philippine political economy under the Marcos and Aquino governments.[1] Especially after the failure of progressive land redistribution through agrarian reform, a pessimistic view prevailed in terms of the ability of the Aquino government to sustain economic reform (see de Dios,1990:124).

In terms of redistribution of wealth and poverty alleviation, the achievements of the Aquino government were less than expected.[2] The domination of the economy by a small number of elites did not change significantly. The President tended to rely on family members and close allies of her late husband in terms of policy-making. They played an important role in the Legislature, although they did not support all the government's policies.[3] There was strong continuity with regard to the backgrounds of

[1] See, for example, Hutchcroft (1998), Jayasuriya (1995), Lindsey (1995) and Faustino (1992).

[2] For the achievements of the Aquino presidency, see the Presidential Management Staff (PMS) (1992a-j). For assessments of the Aquino government from various perspectives, see Abueva and Roman (eds.) (1993); Abueva and Roman (eds.) (1998a); and Abueva and Roman (eds.) (1998b).

[3] See Caoili (1993:24). For the presence of her family in the government, also see FEER, 26 March 1987: 70-73.

the members of the newly-restored Legislature.[4] Corruption and favouritism were not eradicated under the new democratic government. The regulatory power of the state apparatus could not be enhanced over such a short period.

However, it would be wrong to assume that there was no difference in terms of economic policy and policy-making between the Marcos and the Aquino governments. In terms of banking reform, the Aquino government had mixed results. It failed to take strong initiatives to reform the banking sector through the legislative process after the Legislature was restored. The failure to enact the new Central Bank Act, which was one of the urgent reforms required by the 1987 Constitution, was a prominent example. The establishment of a more independent Central Bank was broadly supported by business representatives, bankers and economists after the disastrous failure of banking and monetary management under the Marcos dictatorship. The World Bank was also keen to support the measure through conditionality lending. In spite of strong support, the government did not take all the action necessary to enact vital reform. Nevertheless, the transition from Marcos to Aquino was a critical trigger in reforming the banking sector.

In terms of the macro-economy, the Aquino government was able to steer the economy out of the severe economic turmoil of the mid-1980s, despite unfavourable circumstances, including political instability, particularly several coup attempts and natural disasters.[5] The GDP growth rate rose from 3.4 per cent in 1986 and was above 6 per cent in 1988 and 1989, although it slowed down to 3.0 per cent in 1990 (see Table 1-1.). Foreign debt stock also gradually decreased. In 1991, exports reached $8.8 billion, almost double the $4.8 billion level in 1986. The improvement of the macroeconomy was a precondition for the recovery of the banking sector which was severely damaged by economic and political turmoil in the last years of the Marcos dictatorship.

[4] See, for example, Gutierrez (1994) and Caoili (1993:14-16).

[5] For a similar view on the Aquino government, see, for example, Rigoberto Tiglao in FEER, 3 September 1992, reprinted in Abueva and Roman (eds.) (1993:63-64).

Although the political and economic uncertainty continued during the early period of the Aquino era, the banking sector started to recover from the banking crisis under the previous government. The commercial banks started to recover as soon as the economy grew after the new government took power. In 1988, all major performance indicators including resources, portfolio levels, deposit levels, liquidity, profitability and solvency rapidly improved.[6] The total assets of the commercial banking system expanded from the 1986 level of P 264 billion to over P 599 billion in 1991 (see Table 1-3.). Domestic credits grew from 136 billion pesos in 1986 to 331 billion pesos in 1991 (see Table 1-2.). Total deposits improved from P 144 billion at the end of 1986 to P 337 billion at the end of 1991 (see Table 1-2.). In terms of the commercial banks' business statements, a 2,607 million pesos total loss in 1986 had turned into a 15,706 million pesos profit by 1991 (see Table 1-5.). The Non-performing Loans Ratios (non-performing loans divided by total loans) significantly improved from 20.4 per cent in 1986 to 6.6 per cent in 1991 (see Table 1-6.).

It must be noted that the structure of the banking sector was largely altered by the restructuring of state banks. The highly-indebted state banks, namely the PNB and DBP, were rehabilitated, largely reducing their presence in the banking sector. This can be seen as a significant change in the Philippine banking sector, which had always been dominated by the state banks. The end of Marcos cronyism also contributed to the revitalisation of the economy and the banking sector. After Marcos and his cronies had left and active state interventionism had ended, the sources of favouritism in the banking sector were much reduced. In addition, the role of the Central Bank in finance was redirected, and the preferential credit allocation by the Central Bank was significantly narrowed. Foreign exchange policy was also liberalised in the early 1990s. After private businesses had more access to foreign exchange, the Central Bank no longer had a dominant influence on foreign exchange allocation. The reduction of direct credit allocation through the Central Bank provided the Bank with protection from political interference. Furthermore, the Central Bank initiated various liberalisation measures through regulatory reform in the early 1990s. On the Central Bank's initiative,

[6] For the initial recovery of the banking sector, see, for example, Manual L. Morales "The Role of Banks in the Recovery Effort", in Fookien Times Philippines Yearbook 1987-1988 and Marianne V. Go "Philippine Banking" in Fookien Times Philippines Yearbook 1989.

"consolidation and competition" in the banking sector was facilitated through various regulatory reforms including the encouragement of mergers and acquisitions, increases in capital requirements, deregulation of the numbers of branches and the entry of new domestic banks.

In this and the following chapters, the successes and failures of the Aquino reforms in the banking sector are examined by focussing on the decisions and interactions of policy elites in the context of changing political institutions. After President Aquino took power by extraordinary means, the "EDSA revolution", the political institutions were transformed by the end of the authoritarian government and the restoration of democracy under the new Constitution. During the first year, the President held absolute law-making power until the new Constitution was written and the new Legislature was opened as a result of the elections in May 1987. It should also be noted that the end of the dictatorship triggered restoration of the Central Bank control over monetary and banking policy. Unlike the former dictator, the new President did not intervene in Central Bank decisions on monetary and banking policy. With an absolute law-making power, the President implemented a key structural reform, namely the rehabilitation of state banks, which were left in ruin by the previous government. Supported by the President, the Central Bank took measures to strengthen the banking sector. In the early 1990s, the Central Bank further initiated reforms to liberalise the banking sector. Under the Aquino government the Central Bank was able to implement regulatory reform more effectively than under the late Marcos government due to an improvement in its relationship with the President.

However, structural reform was not smoothly implemented after the Legislature was restored under the new 1987 Constitution. The establishment of the new Constitution and the restoration of the Legislature radically altered the process of policy-making. The restoration of the executive-legislative relationship was a critical factor in deciding the fate of economic reform. The fierce conflicts over key economic policies and the lack of policy coordination between the Executive and Legislature, in particular the Senate, prevented the successful implementation of structural reform in the banking sector, including the Central Bank reform. Since there were no legislative elections

between 1987 and 1992 due to the transitional provisions of the 1987 Constitution, legislators did not need to ask for support from the President for immediate electoral purposes during the early years of the Aquino government.

In this chapter, banking reforms in the early period of the Aquino government are examined. A discussion of the changes in economic policy which mobilised support for the government from the IMF, the World Bank, the US government and other donor countries will be follow by an analysis of the rehabilitation of state banks. This chapter covers the last years of the Fernandez governorship. He retained his governorship of the Central Bank until the end of his tenure in January 1990. In the following chapter, regulatory reforms in the banking sector introduced by the new governor, Jose Cuisia, Jr., and the failure of the structural reforms under the newly restored constitutional democracy are analysed.

Redirecting Marcos's Policy

The day after Corazon C. Aquino took her oath, the new President formed the first Aquino Cabinet (from February to November 1986). It reflected the broad coalition of the anti-Marcos movement including politicians, civil activists, academics, businessmen and the military. Vice-President Salvador Laurel became Minister of Foreign Affairs. Juan Ponce Enrile stayed as Minister of Defence. Aquino's close allies and her husband's friends occupied important posts. Joker Arroyo, a corporate lawyer and strong critic of the Marcos dictatorship was appointed to the powerful position of Executive Secretary. Neptali A. Gonzales (Secretary of Justice), Ernesto Maceda (Secretary of Natural Resources), Ramon Mitra, Jr. (Secretary of Agriculture), and Aquilino Q. Pimentel, Jr. (Secretary of Local Government) were close associates of Benigno S. Aquino, Jr. They had been candidates in Benigno Aquino's LABAN party in the 1978 legislative elections in Manila (see Thompson,1995:220). They were seen as "traditional" machine politicians in the new government.

Jaime V. Ongpin (Secretary of Finance), Jose Concepcion, Jr. (Secretary of Trade and Industry), Solita C. Monsod (Director General of National Economic and Development

Authority) and Alberto G. Romulo (Secretary of Budget and Management) were appointed to key economic ministries. They were also members of the Monetary Board, the governing body of the Central Bank. Jose B. Fernandez, Jr. (Central Bank governor and the Chairman of the Monetary Board) stayed in his post. A representative from the private sector, Cesar Buenaventura (President of Pilipinas Shell) also retained his seat on the Monetary Board. He was suspected of being a beneficiary of Marcos government subsidies intended to stabilise oil prices (see Montojo,1998:54), but he was also a close ally of Jaime Ongpin and an active member of the Makati Business Club formed in 1981 by leading businessmen to discuss economic matters. Buenaventura became influential as a critic of the economic policy of the Marcos government.

Jaime Ongpin and Jose Concepcion were leading businessmen who were vocally opposed to the dictatorship of the Marcos government and the domination of the economy by Marcos' cronies. Jaime Ongpin, an MBA-holder from Harvard University, had been President of the Benguet Corporation, a leading mining company in the Philippines. Even before the assassination of Benigno Aquino, he openly criticised the government's economic policy. He was a leading opponent of the ambitious "Eleven Major Industrial Projects", which had been initiated by Roberto Ongpin, his own brother, who was Minister of Trade and Industry under the Marcos government. In the early 1980s, he strongly attacked the government when it used a massive amount of public money to bail out Marcos' cronies' companies such as the Construction Development Company of the Philippines (CDCP).[7] By late 1984, with Corazon Aquino and former Senator Lorenzo Tañada, he was one of the leading figures in the Convenor's Group, which was formed to unite opposition forces against the Marcos government. Ongpin was also an active member of the Makati Business Club.

It should be noted that Ongpin was thought to have influenced Aquino's decision to retain the Central Bank governor, Jose Fernandez. When Aquino came to power in 1986 after a series of extraordinary political events, the Philippine economy was still in a process of slow recovery from the economic turmoil that had occurred between 1983

[7] See Ongpin's paper "The Eleven MIP's" which was presented to the Financial Executive Institute of the Philippines (FINEX) on March 16,1983. For the CDCP controversy, see, also, Times Journal, 1 March 1983; 3 March 1983, p.8; and 4 March 1983, p.8.

and 1985. Due to draconian stabilisation measures, the government's external and fiscal deficits had started to improve, but the government, the Central Bank and the government's financial institutions were still heavily indebted after massive rescue operations to help insolvent companies. The Central Bank governor continued to face extremely demanding tasks after the transition from Marcos to Aquino. Jaime Ongpin, incoming Secretary of Finance, who had criticised the economic policy of the Marcos government and the Central Bank, strongly supported the retention of governor Fernandez. In an interview with leading national newspapers, Ongpin stressed the competence of Fernandez as Central Bank governor.[8]

Jose Concepcion, Jr. was President of Republic Flour Mills (RFM), one of the country's leading companies. RFM was established by Salvador Araneta, who was the father-in-law of Concepcion. Jose Concepcion, Jr. was an active member of the Bishops-Businessmen's Conference for Human Development (BBC), which was established in 1971. He had close contacts with Manila Archbishop Jaime Cardinal Sin who was an influential religious leader and had mobilised people against the Marcos dictatorship in 1986 (see Thompson,1995:126-127). After Aquino's assassination, Sin and many other bishops openly supported the opposition. In the anti-Marcos movement, the BBC played an important role as opinion leader. Bishops and businessmen including Ongpin and Concepcion set up the opposition-oriented Veritas magazine. Jose Concepcion, Jr. was at the core of the National Citizens Movement for Free Elections (NAMFREL). NAMFREL played a critical role as an electoral watchdog group in the 1984 legislative election and the 1986 presidential election. In the latter election, although COMELEC, the official government body for the election, declared a victory for Marcos, the NAMFREL vote-count, according to which Aquino had won, was broadly trusted.

Solita C. Monsod was an economist who had been educated in the Philippines (Bachelor in Economics from the University of the Philippines) and in the US (a Masters in Economics, from the University of Pennsylvania). As an economist, she criticised the economic policy of the Marcos government. She was an active participant

[8] Sunday Inquirer Magazine, July 6, 1986.

in workshops and seminars which discussed alternative economic policies.[9] She joined the government on leave from the University of the Philippines School of Economics where she was an Associate Professor. Her husband, Christian S. Monsod, who had a prominent career in business, was also a leading critic of the Marcos dictatorship. He had worked for Meralco Corporation before martial law and was a famous investment banker at Filcapital Development Corp. in the early 1980s. He was among the business leaders who were actively involved in the anti-Marcos movement. He became NAMFREL Metro Manila Coordinator in 1984 and then national Chairman in 1986.

Alberto G. Romulo, lawyer and accountant (CPA), was elected to the Batasang Pambansa (National Assembly) in the 1984 elections (representing Quezon City) and was a pillar of the opposition to the Marcos regime. Alberto G. Romulo was replaced by Guillermo N. Carague, his under-secretary, when Romulo ran for and won a Senate seat in May 1987. Carague, a lawyer and accountant, had a stable and progressive career at Sycip, Gorres, Velayo (SGV), a leading accounting and management consultancy firm before Romulo asked him to assist the government.

Predictably enough, given the transitional nature of the new government, there was no solid consensus on key economic policy issues among key economic ministers and Monetary Board members in the first Aquino Cabinet. There were fierce disputes over economic policies such as debt repayment, land redistribution and trade liberalisation.[10] In addition to political instability, deep differences among key economic ministers impeded the strong government initiatives to reform the economy in the early years of the Aquino government. However, there was broad agreement on economic development strategy which aimed essentially to redirect the active state interventionism of the late Marcos government. Aquino herself was fully committed to this economic development strategy, although she confessed that she did not have a clear idea of how to alleviate poverty.[11] For Aquino, to undo what Marcos had done was a critical policy

[9] For example, see De Dios (et al.) (1984).

[10] Deep differences among the Aquino Cabinet are often cited. See, for example, Putzel (1992, Chapter 6), the Presidential Management Staff (PMS)(1992b:27), Nemenzo (1988:222-223), and FEER, 28 August 1986:28-35.

[11] See Aquino's lecture in Abueva and Roman (eds.) (1993:8).

goal (see Nemenzo,1988:223). However, it should be noted that this did not necessarily mean that Aquino entirely lacked a vision of economic development. Filipino economists who criticised economic policy under the Marcos government and recommended various economic reforms to the new government in the "Yellow Book" noted that "the bulk of these reforms aim simply at undoing the biases and penalties carried over from the previous regime" (Alburo, et al.,1986:i).

The enthusiasm felt after the "EDSA revolution" prompted the formulation of a distinctive economic policy manifesto by Filipino economists at leading local academic and research institutions including the School of Economics (University of the Philippines), Ateneo de Manila University and the Philippine Institute for Development Studies. By early May, less than three months after the change of government, an agenda for reform entitled Economic Recovery and Long-run Growth (Alburo, et al., 1986) had been produced on the initiative of the New Planning Secretary (Director General of NEDA), Solita Monsod and other leading Filipino economists. The document, known as the "Yellow Book", urged institutional and policy reforms based on minimum government intervention, liberalisation, decentralisation and redistribution of the resulting growth. Although some key recommended reforms in the "Yellow Book" were not included in the Medium-Term Philippine Development Plan 1987-1992, which was published by the government in December 1986,[12] this development strategy based on liberal reform was influential in government economic policy-making during the early Aquino government.[13]

[12] A notable example was the limitation of debt service payments. Despite its emphasis, redistributive reform including land reform was also limited. In the "Yellow Book", the key recommended reforms included the following: "(1) an expansionary monetary policy and a limitation of debt service payments to what the Government could afford to pay; (2) greater independence of the Central Bank from political influences, a limitation of the involvement of the central bank in development finance and reform of government financial institutions; (3) tax reforms relying more on a direct and broader basis; (4) a more open trade regime, with an exchange rate determined by the free market; (5) elimination of government intervention in the labour market (including minimum wages); (6) and a substantial extension of land reform" (Alburo, et al.,1986:i).

[13] Rigoberto Tiglao observes that many recently announced government policies or major proposals for new policies appear to draw directly from the "Yellow Book" (see Business Day, 19 May 1986, p.2)

The Central Bank summarised the four principles of the New Economic Development Strategy as follows: (1) "the substantial reduction in the extent of government intervention in the economy; (2) the re-establishment of competitive markets; (3) renewed emphasis on rural development and on the equitable sharing of the fruits of sustained recovery; and (4) a more competitive and outward-looking economy through trade liberalisation and flexible exchange rate policies" (Central Bank, Annual Report 1986:3).

The core of the new development strategy showed a shift in emphasis away from the state-led and capital-intensive development strategy of the Marcos government. The Marcos government adopted some liberalisation and export promotion measures. Economic policy-makers like Finance Minister Cesar Virata recognised the importance of export promotion and foreign investment.[14] However, these measures were still limited.[15] Liberalisation measures often contradicted active state interventionism under the Marcos government. For example, on the one hand, in the banking sector, interest rate policy was progressively liberalised from the latter half of the 1970s.[16] On the other hand, the Central Bank provided massive credits with preferential interest rates through rediscount windows. As a result, the impact of interest rate liberalisation on resource mobilisation was not clear. Although some export promotion measures, such as the establishment of export processing zones, were implemented, foreign exchange policy did not promote exports. Trade liberalisation was initiated in the early 1980s but it was halted during the economic crisis. To reduce current account deficits and raise government revenue, an export levy was imposed and trade liberalisation measures were not implemented.

By contrast, under the Aquino government, the redirection of state interventionism, market-oriented policies, liberalisation and export promotion became the key elements of economic development strategy. Although each instance of various policy reform should be examined on its own merits, the new economic strategy can, in general, be

[14] Some authors stress the negative impact of the adoption of export oriented industrialisation on the economy in the mid-1980s. See, for example, Bello (1982) and Broad (1988).

[15] See Haggard (1990b;216) and Bello (2000:239-240).

[16] For the liberalisation of interest rate policy, see Lamberte (1988) and Laya (1982:99-116).

seen as an important guideline for reform.[17] In terms of banking reform, the rehabilitation of state banks, which involved a significant reduction in their size and the redirection of the direct involvement of the Central Bank in development finance were consistent with the economic strategy. Despite frequent reshuffles in the Aquino Cabinet, this new economic development strategy played an influential role and furnished a guideline, which importantly, was inherited more or less intact by the Ramos government.

The new development strategy, which stressed the reduction of the state's involvement in the economy, the establishment of competitive markets and more outward-looking economic policies, was consistent with the policies recommended by the IMF and the World Bank. Economic liberalisation was a broad international trend in the 1980s and 1990s. Nevertheless, as Haggard (1990b:247) points out, overemphasis on the influence of the World Bank or outside creditors on policy choices might miss the critical feature of the post-Marcos politics of economic reform. It must be noted that the experience of the Philippines played a critical role in altering its economic development strategy. This development strategy did not reflect "new" ideas among local economists.[18] Although the detailed policy measures and the success or failure of their implementation must be examined separately in each policy area, we can at least say that liberalisation as an economic development strategy emerging in the context of the failures of active state interventionism under the Marcos government was broadly supported by the Marcos opposition as an alternative policy agenda.

During the early years of the Aquino government, the core policy of liberalisation involved redirecting the active state interventionism which had existed under the Marcos government. Prominent critics of the economic policy of the late Marcos government included Filipino economists and business representatives who were proponents of the "new" development strategy under the Aquino government. They were influential

[17] Economic reform under the Aquino government is examined by various studies. For example, Montojo (1998, Chapter 4), Medalla (et al.) (1995), Montes (1992) and Alburo (1993) examine trade liberalisation. Montojo's study (1998) also includes the reform of the oil industry (Chapter 3). For the limitation of agrarian reform, see Putzel (1992). Magadia also examines agrarian (1999, Chapter 3) labour relations (Chapter 4) and urban housing (Chapter 5) reforms.

[18] See, for example, de Dios (et al.) (1984) and Sicat (1985).

supporters of the "EDSA revolution" and their leaders became key cabinet members under the Aquino government. All key economic ministerial posts were occupied by critics of the Marcos government and its economic policies. Due to the dramatic decline of the economy after active state interventionism, the redirection of previous policy was broadly supported. With the transition from Marcos to Aquino, active state interventionism as a key economic development strategy was terminated, although the critical role of the state in the economy remained unchanged. Under the Aquino government, the move towards liberalisation as part of the economic policy agenda was consolidated towards the end of her term. This policy shift generated broad support for the government from the IMF, the World Bank, the US and other donor countries, especially in the early years of the Aquino government.

Changing International Influences

The "peaceful" end of Marcos's 20 year rule brought hopes of a new era for the country. The "goodwill" of the international financial community should not be over-emphasised since the disbursement of new credits was less than expected and private creditors kept their strict lending stance towards the country. Yet, the transition from Marcos to Aquino was a critical trigger in altering the attitude of the international financial community.

After the dramatic "people's power revolution" in February 1986, the Aquino government restored amicable relations with the US government, the IMF, the World Bank and other donor countries. In addition to the adoption of a liberal economic development strategy during the first years of the Aquino government, various factors, including sympathy for the "people's power revolution", Aquino's debt policy, continuing political instability due to radical military factions and communist guerrillas, and the US base agreement, contributed to the consolidation of support for the government. Although the "EDSA revolution" adversely affected the economy in the short term, the re-establishment of favourable relations with external creditors was critical to improving the heavily-indebted economy. The IMF's tolerance for growth-oriented policy with larger budget deficits was in sharp contrast to its strict stance

towards the Marcos government. Expansionary fiscal and monetary policy contributed to efforts to revitalise an economy, which was in deep recession. The improvement of the macroeconomy was a vital precondition for the recovery of the banking sector.

Enthusiasm after the "people's power revolution" influenced the lending decisions of the international financial institutions. Immediately after the "EDSA revolution", the Asian Development Bank (ADB), whose headquarters were located in Manila, became the first financial institution to provide emergency loans to the new government. At the end of the Marcos era, there had been little agreement between the ADB and the Philippines on loans. One week after Aquino took power, the newly-appointed Secretary of Finance, Jaime Ongpin, met Masao Fujioka, the President of the ADB, and agreed on a US$100 million emergency loan to ease the serious unemployment problems in rural areas. According to Fujioka, they discussed the loan over lunch in a Japanese restaurant and it took just 45 minutes to reach a detailed agreement while Ongpin was eating *tempura teishoku* (set meal). Within 11 days, the members of the ADB Board agreed with the Governor's proposed emergency loan and it was authorised by a formal Board meeting on 7th April 1986 (See Fujioka,1994:179-183). Ongpin called the loan agreement "a new world speed record from inception to approval".[19] This might not be a exaggeration in comparison with the tireless efforts of his predecessor to negotiate a new foreign loan in the previous year. Fujioka explained that the quick decision was prompted by the excitement after the "people's power revolution", in which hundreds of thousands of people were mobilised against the Marcos dictatorship. The headquarters of the ADB are located very near the site of the "EDSA revolution". The members of the ADB Board appeared to be moved by the extraordinary events, as were other observers throughout the world. In these circumstances, it was very easy for the Board members to agree the emergency loan.[20]

More importantly, the establishment of the new democratic government influenced lending negotiations with the IMF. Immediately after the "EDSA revolution", the IMF initiated Article IV consultations with the new authorities, and a mission visited Manila during March 10-15, followed by others in April, June and July/August, 1986. The new

[19] Remarks at ADB Loan Signing April 1987.

[20] See Fujioka (1994:179-183) and Interview with Masao Fujioka, 9 July 1998.

government chose to cancel the ongoing standby arrangement in advance of the third programme review and to request a new 18-month standby arrangement for SDR 198 million. This was complemented by a SDR 224 million Compensatory Facility. Both were approved by the IMF in September 1986.

Although there were fierce conflicts on economic issues such as foreign debt repudiation and trade liberalisation among economic secretaries of the Aquino Cabinet, there was a consensus that an expansionary economic policy was necessary to reverse the two-year austerity programme.[21] By July 1986, negotiations between the government and the IMF were completed. Agreements were reached on most key components of an IMF aid programme including the increase of ceilings on the budget deficit, liquidity and inflation targets. Consistent with the growth-oriented strategy of the government, the Fund programme raised the medium-term GNP growth target from a strong negative rate in 1984 and 1985 to 1.5 per cent in 1986, and to 6-7 per cent for 1987. The external current account balance was also raised, from equilibrium in 1985 and 3 per cent of GNP surplus in 1986 to deficits of 1.6 and 2 per cent of GNP in 1987 and 1988 respectively. The consolidated public sector deficit was allowed to rise from 6.1 per cent of GNP in 1985 to 7.5 per cent of GNP in 1986 and to remain at levels higher than 5 per cent of GNP in the following two years.[22] The adoption of a growth-oriented policy, which allowed large budget deficits, contributed a great deal to the improvement of the economy in the initial years of the Aquino government. Government expenditure, including that on rural-based projects under the Community Employment and Development Programme (CEDP) and on salary hikes for government workers, contributed not only to the generation of jobs and incomes in rural areas, but also to the mobilisation of support for the new government.

The Philippine negotiators felt that the IMF team was very receptive to the main policy thrust of the Aquino government.[23] This was in sharp contrast to the IMF's negative

[21] See, for example, Business Day, 7 April 1986, p.3.

[22] This data on monetary targets is adopted from "Program Performance Audit Report, Economic Recovery Program and Economic Recovery Technical Assistance Project" in World Bank (1992:4).

[23] A Philippine monetary official commented that "there has been a complete switch in attitude (see Business Day, 24 July 1986, p.3). Also, see FEER, 14 August 1986:104-105.

attitude and aggressive posture in talks with the government of former President Marcos in 1985. The IMF mission reviewed the status of structural reforms in the three areas of their concern: the sugar and coconut sectors, the import liberalisation programme and the restructuring of government financial institutions. Central Bank governor Fernandez said that "the discussions would be less weighted on macro figures for this year and the next and more on the accomplishment of structural reforms which, with or without the Fund, we will have to do anyway".[24]

It is reported that the IMF mission was satisfied with the decisive position of the government regarding the dismantling of the monopolies in the sugar and coconut industries, which had previously been the major stumbling block to successful negotiations. After Marcos left, it was very easy to satisfy the IMF by dismantling the monopolies, although the improvement in the production of sugar and coconut was a totally different matter. Ongpin noted that "abolishing the monopolies was basically a stroke of the pen. It didn't really require any involved implementation".[25]

The establishment of the new government and its new economic policy was also warmly welcomed by the World Bank. Some of these economic reforms, such as tax reform, trade liberalisation, the public expenditure programme and rehabilitation of the state banks, were supported by the Economic Recovery Loan of the World Bank with the Japanese government as co-financer. These issues had been matters of concern between the Philippine government and the World Bank since the World Bank started policy-based lending in the early 1980s.

The World Bank mission visited Manila in April 1986 and its economic report provided the foundation for the Economic Recovery Loan.[26] Along with the Philippine government and the IMF, the World Bank's report recommended the adoption of growth-oriented policies, to be financed through a much-intensified effort on public resource mobilisation (the report having pointed out that the country's tax effort was

[24] Business Day, 18 July 1986, p.2.

[25] Euromoney, interview with Jaime Ongpin, July 1987:122.

[26] See World Bank (1986) "The Philippines, A Framework for Economic Recovery", Report No. 6350-PH November 5, 1986.

exceptionally low), and by expanded external financing through concessionary loans and debt relief. In addition to the US$300 million of the ERL, the Philippine government received large co-financing loans from Japan. The Export-Import Bank of Japan contributed Yen 50 billion (equivalent to US$300 million at that time) and the OECF contributed Yen 30 billion (equivalent to US$180 million at that time).

Support from the US government facilitated debt negotiations with the IMF and World Bank, which were favourable to the Aquino government. The US's support for the government was closely connected with Aquino's debt policy, continuing political instability and the US military base issue. When Aquino became President, the huge foreign debt which the former dictator had left was the most contentious economic policy issue. In the early days of Aquino's government, this was also the main area of concern for the US government. Finance Secretary Ongpin and Central Bank Governor Fernandez, who were in charge of the debt negotiation, were committed to full repayment of foreign debts and negotiated with creditors for various debt reduction schemes and new concessional loans. President Aquino fully backed Ongpin's and Fernandez's position. In June 1986, when US Secretary of State George Shultz visited Aquino, he received reassurances with regard to the government's policy on this issue. The US support for Aquino's debt policy was supposed to be influential in smoothing negotiations with the IMF and the World Bank. The Japanese government, the biggest donor country to the Philippines during the Aquino era, also repeatedly expressed its opposition to the selective repudiation policy during debt negotiations. In fact, in terms of foreign debt policy, there was no realistic alternative option for the Philippine government since all creditors, including the US government, strongly opposed the selective repudiation of foreign debt.

However, Finance Secretary Ongpin and Central Bank Governor Fernandez were severely criticised for their foreign debt policy. There was a fierce dispute among Cabinet members over this issue. Some key economic policy-makers, namely Solita Monsod, Director General of the NEDA, strongly advocated the selective repudiation of foreign debts. Alberto Romulo was another influential Cabinet member, later Senator, who supported the selective repudiation policy. This position was broadly supported by

economists, civic activists and politicians who played a leading role in the "EDSA revolution".[27] The organisation Freedom from Debt Coalition (FDC) was formed to unite critical voices against the government's debt policy. This fierce dispute later became one of the reasons for Secretary Ongpin's resignation.

In its first years, the Aquino government faced continuing political instability.[28] The Communist Party of the Philippines (CPP) and New People's Army (NPA) continued to challenge the new government. The secessionist movement in Mindanao led by the Moro National Liberation Front (MNLF) and insurgency in the Cordilleras were still active. More importantly, radical military factions led by Marcos loyalists and some members of the Reform Armed Forces Movement (RAM) continued to threaten the new government. By the end of 1989, there had been seven coup attempts, two of which were serious and led to many casualties. In spite of some scepticism about Aquino's ability to restore political stability, the US government continued to support the government. Further political instability in the Philippines impeded smooth negotiation of the lease agreements on the US bases, which were due to expire in 1991.

US President Ronald Reagan accelerated the process of appropriations for additional US financial aid to the unstable newly-democratised country. An additional $200 million of financial assistance repeatedly stalled in the American Senate. It was only finally passed after the importance of the aid was recognised by Senators to generate support for the position of the US government in the Philippines over the US bases issue.[29]

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[27] For powerful arguments by proponents of the selective repudiation policy, see de Dios and Rocamora (eds.) (1992).

[28] The fragility of the Aquino government is documented by Reid and Guerrero (1995). For the official investigation into coup attempts, see Hilario Davide, *et al.* (1990) "The Final Report of the Fact-Finding Commission". Also, see, PMS(1992d) "The Aquino Management of the Presidency: In the Face of Crisis".

[29] See, Montojo (1998:86). For the close links between US aid and the military bases issue under the Aquino government, also see Pregg (1991).

It should also be noted that support from the US government, the IMF and the World Bank was helpful in facilitating foreign debt negotiation with private foreign banks.[30] For example, it is reported that senior US officials, including US Treasury Secretary James A Baker III and Federal Reserve Board chairman Paul Volcker, had been exerting "moral suasion" on Citibank to ease up its strict stance on debt negotiation with the Philippine government in February 1987.

After the new government restored amicable relations with the US government, the IMF and the World Bank, their lending conditionality was not strictly enforced. The IMF's and the World Bank's stance on conditionality was very strict in the Philippines in 1984 and 1985. However, except for this period, the conditionality of the IMF and the World Bank cannot be seen as strong "leverage". In particular, during the initial years of the Aquino government, the IMF's decisions on lending negotiations were supposed to be influenced by US pressure to speed up negotiations or to loosen the terms of lending conditions (see Montojo,1998:254). Under the new government, the World Bank also "took a golden opportunity" to implement lessons learnt from its experience of the previous ten years (see Mosley,1991:55), the key lesson being the vital importance of the government's commitment to policy reform. The World Bank "handed over to the Philippine Government the policy initiative in determining the next steps to be taken within the reform programme" (ibid.).

As the World Bank admitted, its critical role was "intellectual leadership" rather than the enforcement of recommended policies. In its overall evaluation to the Economic Recovery Programme (ERL), the Bank notes that "the Bank's intellectual leadership provided an important influence during the transition period. Had this been the only accomplishment of the ERL, it would have been sufficient to consider the operation a success".[31] Initially, the release of the third tranche of the Economic Recovery Programme was delayed because some conditions were only partially fulfilled, namely those regarding public expenditure, trade liberalisation and the privatisation of six

[30] See Business Day, 19 February 1987, p.13. For the debt talks, also see Business Day, 4 February 1987, p.2 and 24 February 1987, p.2.

[31] "Program Performance Audit Report, Economic Recovery Program and Economic Recovery Technical Assistance Project" in World Bank (1992:22).

banks. Later, however, the Philippine government managed to get these conditions waived. It should be noted that massive co-finance with the Japanese government might be seen as another factor which made the enforcement of conditionality difficult for the World Bank. Due to differences in the timing of disbursements, the Philippine government received large funds from the co-financer on some occasions before the World Bank had assessed conditionality requirements and formally decided on proceeding with the disbursement.[32]

Rebuilding the Banking Sector: Rehabilitation of the State Banks

After the transition, financial instability continued. The extent of the CB's assistance to financial institutions reached a peak during the first quarter of 1986. The Presidential election in February 1986 shook the financial system due to the expansion of election-related spending and the massive withdrawal of deposits from the banking system. As part of the anti-Marcos campaign, Aquino attacked Presidential cronyism in the banking sector. She urged the withdrawal of deposits from Marcos's crony banks. After the elections many businessmen, including cronies under the Marcos government, pulled their money out of the banks because of fear of sequestration.

In 1987, two further banks, PISO Development Bank and Manila Bank were closed. PISO Development Bank was the largest private development bank in the country and one of the conduits of foreign currency loans from the World Bank and Asian Development Bank (ADB). The bank suffered huge losses from foreign currency loans totalling P560 million due to the sharp peso depreciation during the economic crisis.[33] Three months after the closure of PISO Bank, Manila Bank, a universal bank, collapsed. When the bank ceased operating, Manila Bank had 633,614 deposit accounts valued at P 1.9 billion (see Lamberte,1989:28-30). Manila Bank actually experienced a bank run in 1984. This rapidly depleted its deposits, which stood at P 4.1

[32] The Bank notes that the "Bank accepted the different disbursement arrangements in a spirit of pragmatism." See, for this coordination problem, "Program Performance Audit Report, Economic Recovery Program and Economic Recovery Technical Assistance Project" in World Bank (1992:21).

[33] For the PISO bank's closure, see, for example, Business Day, 5 February 1987, p.13.; Business Day, 6 February 1987, p.8; and Business Day, 12 February 1987, p.13

billion at the end of 1983 (ibid.). In 1985 a son-in-law of Marcos, Gregorio Araneta III, was elected Chairman of the Board of Manila Bank and this was said to be helpful in preventing the bank's closure under the Marcos government (see FEER, 11 June 1987). Although the Central Bank continued to prop up the Manila Bank until the latter's overdrafts with the CB swelled to P 6.1 billion, it closed the Manila Bank after the May legislative elections in 1987.[34]

To rebuild the banking sector, the first task was the rehabilitation of the state-owned banks, most notably the Philippine National Bank (PNB) and Development Bank of the Philippines (DBP). During the first year of the Aquino government, while the President held dominant legislative power, the rehabilitation of the state banks was chosen as the only major banking reform. With regard to the importance and urgency of this reform, there was a loose consensus among the fragmented economic policy elites in the first Aquino Cabinet. The reform was also strongly supported by the IMF and the World Bank. There was little opposition among policy elites to reducing the direct involvement of the state in the banking sector through the rehabilitation of the state banks, although the transfer of the liabilities of the state banks to the national government was controversial. The Central Bank governor, Fernandez, the former President of the BAP, was a persistent opponent of excessive involvement of state banks in the banking sector. Owners and managers of the big private commercial banks welcomed the reform. They were in position to gain from the reduced presence of the state banks. For the officials of the state banks, Aquino's decision to rehabilitate the PNB and the DBP was clearly more acceptable than the abolition or merger of the state banks.

The new economic development strategy enabled the Aquino government to significantly reduce the direct involvement of the state in the banking sector through the rehabilitation of state banks. By the end of 1985, the two major state-owned banks held nearly half of the total assets of the banking system (see Table 3-1). In 1985, the PNB was the largest of all the banks in the Philippines in terms of assets, i.e. 76 billion pesos (see Table 3-1). The DBP's assets amounted to 72 billion pesos, the second largest. However, about 70 per cent of the combined loan portfolio of PNB and DBP consisted

[34] For the Manila Bank's closure, see Business Day, 27 May 1987, p.14; Business Day, 28 May 1987, p.13; and Business Day, 29 May 1987, p.9.

of non-performing loans.[35] Both banks suffered huge losses equivalent to almost three per cent of GNP and became technically bankrupt.

Their lending activities were closely connected with government economic policies. As state-owned banks, they aggressively involved themselves in lending activities to support the state-led development strategy of the Marcos government and engaged in massive rescue operations during the economic downturn after 1979, especially between 1981 and 1983. Both banks were established to promote the allocation of subsidised credits to "priority" sectors. Their reliance on deposits from national government and semi-government agencies had been fairly high, although both banks, especially the PNB, also mobilised deposits from the private sector. There were strong links between foreign debt accumulation, an increase in central bank credit and the expansion of state-owned banks in the late 1970s and early 1980s.

To support state-led industrialisation, the strategy of the Marcos government, the two state-owned banks aggressively expanded their lending activities in the latter half of the 1970s as state-allocated resources increased due to foreign borrowing. In the early 1980s, unlike the other big private banks, which reduced their lending activities during the recession and the financial instability created by the Dewey Dee scandal, the state-owned banks, as the government's main instrument, were actively involved in rescue operations. Between 1980 and 1984, the total assets of the state-owned banks more than doubled: the PNB's assets rose from 38,652 million pesos in 1980 to 87,196 million pesos in 1984 and the DBP's assets from 27,086 million pesos to 66,800 million pesos (see Table 3-1.).

By 1985, the non-performing assets of the PNB and DBP had become a matter of serious concern for economic policy-makers. In 1984, the PNB registered a P1,102 million loss, its first since World War II. The DBP was even worse with losses amounting to P6,641 million, the first losses it had suffered in its 38-year history. The government of President Marcos was forced to pump in P5.6 billion in 1984 just to keep the DBP functioning, despite restrictions which allowed the bank to lend only

[35] This figure is from "Project Completion Report, Part II: Project Review from the Borrower's Perspective", in World Bank(1992:76).

from previously-established, fully-funded credit lines (FEER, 3 October 1985:49). Between 1983 and 1985, the total losses of the PNB and DBP amounted to nearly P30 billion.

In spite of the emergency prevailing in 1983, the Marcos government did not initiate reform of the state-owned banks in serious trouble. During the period of political instability intensified by the assassination of former Senator Benigno Aquino, Jr. in August 1983, a major restructuring of the state-owned banks with large layoffs and significant reduction of loans to his close cronies was avoided by the President. Under the Marcos government, a rehabilitation plan involving the merger of the PNB, the DBP and other banks was proposed by the Monetary Board, but it was suspended by the President, as examined in the previous chapter.

The transition from Marcos to Aquino was a critical trigger for the initiation of reform of the state-owned banks. In one PNB publication, the "EDSA revolution" was referred to as "a miracle" which saved the country from massive economic ruin (PNB,1996:74). After Marcos left, the Aquino government was able to initiate reforms of the state-owned banks thanks to the IMF's favourable view of expansionary government budgets. The restructuring of the state banks was one of the key structural reforms recommended by the IMF in the first lending negotiation with the new government. The World Bank also encouraged this reform with its Economic Recovery Loan (ERL). Reforms were focussed on three main areas: changes in the guiding principles of Government Financial Institutions, the transfer of non-performing assets to the national government and organisational reform.

As early as 1985, the problems of the state-owned banks had been identified and discussed by the World Bank and the economic policy-makers of the Philippine government (mostly within the Central Bank and the Ministry of Finance), resulting in a projected financial sector loan which ended up being absorbed into the ERL package. Even at this stage, it was not difficult for economic policy-makers and World Bank officials to reach agreement on the principal guidelines for the reforms, namely that "they should be allowed to operate on strictly commercial lines rather than as

instruments of political patronage," although there were some differences of opinion on issues such as private equity and capital/asset ratios for the DBP.[36] After the regime change from Marcos to Aquino, this principal guideline was maintained. By early 1986 an amicable agreement between both parties had been negotiated on all but minor details. Although this reform was one imposed as a condition of the Economic Recovery Loan, it had already been implemented before the loan was formally approved by the Board of the World Bank.

Through Resolution No. 1077, dated 28 November 1986, the Monetary Board of the Central Bank issued revised policies with respect to the role of the financial system in general, and government financial institutions in particular, in fostering sustainable economic growth. The guiding principles included: (1) limitation of GFIs' market share relative to the entire banking system; (2) GFIs' financial viability and independence from government assistance; (3) equal treatment with private banks in terms of regulatory requirements; (4) borrowing without national government guarantee except as may be required by official foreign sources in connection with debt restructuring; (5) limited access to public sector deposits and a required liquidity balance against these deposits; and (6) a ban on subsidised government credit programmes from GFIs' resources.[37]

Following these guidelines, the Revised Charter of the PNB was embodied in E.O. No. 80, dated 3 December 1986. It was intended to serve as "the basis for the operations of a reorganised and rehabilitated, smaller but stronger and more operationally viable bank". In the Revised Charter the primary objective of the PNB was defined as that of providing "banking services for the development of agriculture and small and medium scale enterprises, particularly in the countryside" but "within the context of financially viable and stable banking institutions". The new policy statement was approved by the

[36] Mosley (1991:57). For issues that were an initial source of disagreement, see Mosley (1991:58),Table 12-7.

[37] See "Project Completion Report, Part II: Project Review from the Borrower's Perspective", in World Bank (1992:76).

PNB Board and Monetary Board on December 23, 1986.[38]

The new Charter of the DBP, which was revised through E.O. No. 81, dated December 3, 1986, laid the groundwork for the rehabilitation programme. According to this new charter, the DBP was to evolve primarily into a wholesale bank, channelling funds to other financial institutions for lending to private business enterprises in order to pursue its primary objective of providing medium- and long-term financing to the private sector. A new policy statement was approved by the DBP Board and Monetary Board on December 23, 1986.[39]

The essential part of the reform was the removal of huge non-performing assets from the books of the PNB and the DBP. P47 billion of non-performing assets (NPAs), P55 billion of liabilities, including government deposits and foreign borrowings, and P16.7 billion of contingent liabilities were transferred to the national government from the PNB.[40] The transfers reduced the PNB's total assets from P76.1 billion in 1985 to P26.9 billion in 1986 and its capital accounts to P2.5 billion. As with the PNB, non-performing assets amounting to P61.4 B and liabilities amounting to P62.2 billion were transferred from the DBP to the national government in 1986. The total assets of the

[38] The policy statement includes the following: (1) interest rate policies shall ensure positive spreads and consistency with interest rates prevailing in the market; (2) loans are to be made on the basis of viability assessment; (3) uncovered foreign exchange risks are to be avoided and a favourable foreign exchange position maintained; (4) lending in support of government programmes for social purposes is to be undertaken only if funds are specifically provided by the government and treated off books; (5) private deposits are to be actively sought to reduce dependence on government deposits; and (6) public offering of shares is to be initiated by early 1989.

[39] The new policy statement includes the following: (1) DBP shall submit to the test of financial viability to ensure a sound capital structure, generation of sufficient earnings to cover costs and earn a profit margin, build-up of appropriate reserves, and protection of its equity base; (2) DBP shall compete in the market and operate on an equal footing with its private sector counterparts; (3) public sector lending shall be avoided; (4) interest rates shall be guided by full recovery of all costs and consistency with those prevailing in the market; (5) exposure to a single client shall be limited to 15 per cent of DBP's unimpaired capital and surplus, and total equity investment in any single company shall be limited to 15 per cent of DBP's own total equity; and (6) DBP shall conduct lending activities in support of government programmes only if funds are specifically provided, DBP is appropriately compensated and such lending is treated off books.

[40] Data on the PNB and DBP are taken from "Project Completion Report, Part II: Project Review from the Borrower's Perspective", in World Bank (1992:69-82).

DBP were thus reduced from P72 billion in 1985 to P9.5 billion in 1986.

The transfer of non-performing assets was approved by President Aquino in 1986 while the legislature was closed and a new Constitution was being written. After the government's representatives (Ongpin, Secretary of Finance and Fernandez, the governor of the Central Bank) had already agreed with the World Bank on the basic principles of the Economic Recovery Loan, Aquino authorised the recommendation of the transfer by Ongpin and Fernandez in a Cabinet Meeting without serious discussion. Later, Solita Monsod (the former Director General of NEDA) recalled the decision-making in the Cabinet meeting with dissatisfaction. According to Monsod, Ongpin and Fernandez insisted that the transfer of non-performing assets was the only realistic option to rehabilitate the state-owned banks, referring to a very long list of diversified borrowers and adding that they (Ongpin and Fernandez) had already reached an agreement with the World Bank.[41]

The disposal of the non-performing assets transferred from the PNB and DBP to the national government was made part of the government's privatisation programme. Proclamation No.50, dated December 8, 1986, established a Committee on Privatisation (COP) to control the programme. The COP was composed of the Secretary of Finance (Chairman), the Secretary of Budget and Management, the Secretary of Justice, the Secretary of Trade and Industry and the Director General of the National Economic and Development Authority. While the COP formulated policy guidelines and approved sales, the Asset Privatisation Trust (APT) was responsible for actual marketing and disposal of the assets. The APT was also established under Proclamation No. 50 to dispose of the non-performing assets transferred from the PNB and DBP as well as certain government corporations earmarked for privatisation. The privatisation progressed gradually.[42] Of the 399 non-performing accounts lodged with the APT for disposal, 230 had been fully or partially sold within four years (until end-December 1990) (World Bank,1992:80). The APT's biggest account, Nonoc Mining & Industrial Corp. (formerly Marinduque Mining & Industrial Corp., which

[41] Interview with Solita Monsod, 4 June 1998.

[42] For issues relating to privatisation and the APT under the Aquino government, see, for example, Patalinghug (1996), Manasan (1995) and Business World, 6 January 1992.

had collapsed in 1984 owing to weak copper and nickel prices on the market), was sold for US $325 million on October 12, 1990. The DBP had an exposure of P12.7 billion in the company, or 16% of the total of the bank's non-performing accounts (FEER, 4 June 1987:75).

Organisational and institutional reforms of the state banks included two key components: first, cost reduction through leaner staffing and streamlining of branch networks and second, managerial strengthening through organisational change, improvements to the credit review process, strengthening of the management of risk assets and staff training.

These text-book style institutional reforms had been formulated and implemented by strong initiatives from top management. After the short tenure of Vicente R. Jayme, Edgardo B. Espiritu (the former President of Metrobank) was appointed as President of the PNB with a brief to rehabilitate the Bank. Joker Arroyo (the Executive Secretary) became the new Chairman of the PNB. Jesus Estanislao and Roberto Anonas were appointed as the Chairman and Chief Executive Officer, and Vice-Chairman and Chief Operating Officer respectively to rebuild the DBP. Jesus Estanislao was the former President of Associated Bank and a consultant to the Philippine Commercial Bank. He was also a Director of the Centre for Research and Communication, a leading research institution which had affiliations with a conservative catholic force, namely Opus Dei. Roberto Anonas was also an experienced banker.

By 1988, at the end of the rehabilitation programme supported by the ERL, initial measures for cost reduction were implemented.[43] 2,002 PNB personnel had been made redundant. As a result, the PNB's personnel complement compared favourably to those in the private sector in relation to total assets, loans and deposits. Rationalisation of the bank's domestic and overseas branch networks also led to the abolition of ten regional offices and nine overseas offices and divestment of lending functions from 25 branch offices. To ensure the PNB's overall operational efficiency, every aspect of management such as credit control, financial management and operational management was reviewed

[43] The following data on cost reduction measures was taken from "Project Completion Report, Part II: Project Review from the Borrower's Perspective", in World Bank (1992:77).

and reorganised.

The DBP revitalised its branch banking network through the streamlining of the organisational structure of the branches and the intensification of deposit generation activities. To correct the previous unbalanced lending policy, which had concentrated on narrowly-selected sectors and regions, the bank also adopted the Proactive Balanced Development Program (PBD), which focussed on three main sectors including Urban Development, Regional Development and Sectoral Development.[44] Within two years, the DBP had reduced staffing levels from 3,350 to less than 2,000 (FEER, 4 June 1987:76). The DBP offered attractive incentives to those who volunteered for retirement. According to its original plans, that level should have been achieved by 1988 but the DBP opted to do it quickly to remove the air of uncertainty created by a phased reduction. Also, the number of departments was trimmed to 11 major groupings from an unwieldy 38. The bank's experience with "behest" loans contributed to the new credit philosophy of the DBP. The key principle was to "maintain a prudent and diversified loan portfolio" (ibid.). Total exposure, including loans, guarantees and equity investments in any single project, was now limited to P50 million and could not exceed 60% of the total project cost.

After the initial rehabilitation programme, there were still many questions left in terms of the viability of the PNB and DBP and the corruption of the state banks. Although they stressed their independence from the government, they still enjoyed the privilege of having considerable access to government deposits. After the partial privatisation of the PNB through the public offering of its shares, the issue of government deposits was still a controversial matter. Despite the conditionality of the World Bank's Economic Recovery Loan, the audits of the state-owned banks were conducted by a government body (the Commission of Audit) rather than an independent body. The PNB's inefficiency and its loose review process were often pointed out.[45] In fact, after the currency crisis of 1997, the seriousness of the PNB's non-performing loans was revealed.

[44] Estanislao, in Fookien Times Philippines Yearbook 1987-1988, p.108.

[45] See, for example, Delhaise (1996:166-167).

Under the Aquino government, there was ample cause for speculation about various forms of favouritism, fraud and corruption with regard to the operations of the state banks. For example, some asset sales which were transferred from the PNB and DBP were often criticised due to their unfairness.[46] In May 1990 Senator Enrile filed Res. No. 834, which urged an investigation of suspected PNB behest loans to the Petrochemical project proposed by the Taiwanese-owned USI Far East Corporation through the Luzon Petrochemical Corporation.[47] Concern was first voiced by Joker P. Arroyo, former Executive Secretary and Chairman of the Board of Philippine National Bank. Although an investigation by the Senate Blue Ribbon Committee with fifteen public hearings did not find any of the principal features of a behest loan in the case, the Monetary Board of the Central Bank was accused of giving the Luzon Petrochemical Corporation special treatment in terms of the Debt/Equity conversion.

Controversy regarding suspected election-related finance still continued under the Aquino government. In May 1992 Edgardo Espiritu, the President of PNB and a supporter of LDP presidential candidate Ramon Mitra, criticised President Aquino for selectively releasing funds to local government units to buy political support for her chosen candidate, Fidel Ramos of the Lakas Edsa-NUCD.[48] The Aquino government denied this accusation but the resignation of Espiritu was accepted with amicable statements from the President.

Speculation regarding share-dealing by the PNB continued under the Ramos government, provoked by a successful businessman, Lucio Tan, who had once been accused of using his close connections with President Marcos to the benefit of his companies. Favouritism in the allocation of state credits could not be eradicated. As a "public" lending agency, state banks could not avoid extra risks in its lending activities. The role of the state-owned banks remains a controversial issue. Towards the end of the 1990s, state banks, particularly the DBP and the LBP, grew rapidly.

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[46] See, for example, PDI, 2 November 1992, "Behest loans to behest sale".

[47] For a summary of this case, see Salonga (1995:173-175).

[48] See, Manila Chronicle, 8 May 1992 and 16 May 1992; and Manila Bulletin, 14 May 1992.

Nevertheless, the rehabilitation of the state banks was a significant reform measure in the economy and banking sector. After the initial rehabilitation of the PNB and DBP, their presence was much less dominant in absolute terms, although they steadily expanded their businesses later. This was a critical event since the banking sector had always been dominated by state banks in the Philippines. With the rehabilitation of these banks, the most urgent objective of the initial reform had been achieved. The PNB and DBP were no longer the cause of government budget deficits under the Aquino government. It could not be assumed that without proper regulation, private banks would be better managed than public banks. Nonetheless, in the Philippine context of the mid-to-late 1980s, the new restrictions on the state-owned banks' activities constituted a positive step towards building a solid banking system. The amount of credit which was allocated by the state-owned banks was a critical matter in determining the extent of favouritism, as the dramatic decline during the economic crisis of the Marcos cronies, including Herminio Disini, Rodolfo Cuenca and Ricardo Silverio, suggested. The huge expansion of the state-owned banks fostered unprecedented presidential cronyism and added to the fragility of the entire banking system under the Marcos government.

In addition to the rehabilitation of the state banks, the end of Marcos cronyism in the banking sector can be seen as an important event in revitalising the banking sector. After President Aquino took power, she established the Presidential Commission on Good Government (PCGG) by means of her first executive order, which had three main objectives: (1) to recover the ill-gotten wealth accumulated by the Marcos/Romualdez families and their associates; (2) to investigate the cases of graft and corruption in government by order of the President; and (3) to adopt safeguards to ensure that the practices of the Marcoses should not be repeated. The PCGG was given full authority to sequester and freeze ill-gotten wealth. In the banking sector, the PCGG sequestered a controlling share of United Coconut Planters Bank and Traders Royal Bank; and a part of the shares of Allied Bank, Philippine Commercial International Bank and Republic Planters Bank. The PCGG seized documents from the Security Bank.

The fates of banks owned by Marcos' cronies were determined by various factors including their owners' and managements' determination, tactics, financial resources, political influence and luck. UCPB, which was led by Aquino's first cousin and a close Marcos crony, Danding Cojuangco (who fled the country with Marcos), was sequestered and brought under a new management team, in spite of the fact that the chair of the bank, Ponce Enrile, retained his post in the new government (see FEER, 10 July 1989:78). Benedicto made a compromise settlement with the PCGG early on, gaining civil and criminal immunity from prosecution in exchange for information and part of his assets, including frozen funds at Traders Royal Bank. Roland Gapud of Security Bank was also one of sixteen former cronies who made a compromise settlement with the PCGG. Lucio Tan's Allied Bank evaded PCGG's grasp due to, at least in part, his bank's contribution to the generation of foreign currency during the crisis and its continuing constant access to foreign currency.[49]

As many argued, the PCGG's performance was not entirely satisfactory.[50] However, the end of Marcos cronyism in the banking sector contributed to its revitalisation. As a means of dealing with the sequestered banks, the process was not entirely unfair. The non-crony elites gained from the lost wealth of Marcos's cronies but the way in which they obtained a share in the sequestered banks was very different from the practices of the powerful Marcos cronies. The PCIBank's case was an important example. The prominent family bank owner, the Lopez family, which was forced out by Marcos, regained part ownership of the bank under the Aquino government. In November 1987, fifty-two per cent of the shares of PCIBank, owned by the Development Bank of the Philippines, were sold by bidding and were bought by a group led by the industrialists Eugenio Lopez, a former owner of the bank, and John Gokongwei. The share deal involved P 1.345 billion, one of the largest single share transactions in local business history at that time.[51] The selling price per share was P66.10 compared with a book value of close to P30 per share, or a premium of 120%. It was not easy to judge

[49] For the survival of the Allied Bank, see FEER, 15 December 1988:112-116 and Hutchcroft (1998:188).

[50] For an assessment of the PCGG from various points of view, see Abueva and Roman (1998b:133-155). See, also, Nozawa (1991).

[51] See Manual L. Morales "The Role of Banks in the Recovery Effort", in Fookien Times Philippines Yearbook 1987-1988.

whether the bidding was entirely fair but it was clearly different from the way in which the Marcos cronies, namely "Danding" Cojuangco and Benedicto, had acquired their banks under the Marcos dictatorship. After the Marcos era, there were no banks like the Marcos crony banks, including United Coconut Planters Bank, Traders Royal Bank, Republic Planters Bank and Allied Bank, which had grown rapidly in a very short time in the 1970s, delivering benefits as a result of the government's policies and Presidential favour.

Conclusion

The transition from Marcos to Aquino caused a change in policy elites, in the interactions among them and in economic policy, although the new government had mixed results in terms of banking reform. It also triggered a recovery in the economy, although corruption and favouritism were not eradicated as expected. In spite of the instability of the banking sector in the early years and continuing political uncertainty, the banking sector was restored to stability under the Aquino government.

After the failure of active state interventionism under the long-term authoritarian government, the new government, which took power as a coalition to end the authoritarian regime, was committed to redirecting previously-adopted economic policy. During this period, the government took initiatives to redirect active state interventionism, to dismantle the state monopoly, to rehabilitate the state banks and to end Marcos cronyism. In particular, the rehabilitation of the state banks which was implemented by the President before the restoration of the Legislature was seen as a significant reform in the banking sector. These were policy areas which a loose consensus among the policy elites in the fragmented Aquino government regarded as urgent.

Redirecting Marcos's policy generated support from the US government, the IMF, the World Bank and other donor countries. The US government strongly opposed the selective repudiation of foreign debt. However, once the Philippine government adopted a foreign debt policy which was in favour of the US government, they were

supportive of the new democratic government, which had been facing serious security and economic problems. In the early Aquino years, US security concerns also facilitated US economic assistance. Their support contributed to the recovery in the economy and the banking sector.

It must also be noted that the transition improved the relationships between the Central Bank and the President. Unlike her predecessor, President Aquino did not intervene in the Central Bank's policy decisions. The Central Bank, backed by the President, started to improve the stability of the banking sector through regulatory reforms. However, the government initiatives to reform the economy were undermined by the fragility of the transitional government. There were fierce conflicts among policy elites in the Aquino Cabinet. They did not agree on the key policy issues, including foreign debt, trade liberalisation, land reform and the US bases policy. In addition, the government, which had to put a high priority on restoring political order, was not very effective in reforming the economy through the legislative process. Under the newly-restored democratic system, structural reform through the legislative process was not smooth. An ineffectual executive-legislative relationship was once again an obstacle to reforming the economy. The next chapter examines further some of the successes of liberalisation by regulatory reform towards the end of the Aquino government and the failure of structural reform through the legislative process.

Table 3-1. Total Assets: Banking System, PNB and DBP (in Million Pesos)

Year	Banking System	PNB	PNB/ Banking System	DBP	DBP/ Banking System	PNB+DBP/ Banking System
1980	188,824	38,652	20.5%	27,086	14.3%	34.8%
1981	226,057	44,866	19.8%	34,707	15.4%	35.2%
1982	226,057	58,710	26.0%	43,988	19.5%	45.4%
1983	265,016	70,502	26.6%	54,934	20.7%	47.3%
1984	388,901	87,196	22.4%	66,800	17.2%	39.6%
1985	331,757	76,157	23.0%	72,043	21.7%	44.7%
1986	304,085	26,913	8.9%	9,504	3.1%	12.0%
1987	330,304	31,268	9.5%	10,532	3.2%	12.7%
1988	392,054	38,758	9.9%	11,432	2.9%	12.8%
1989	479,010	56,302	11.8%	11,322	2.4%	14.1%
1990	609,695	73,463	12.0%	17,151	2.8%	14.9%
1991	691,098	93,799	13.6%	27,011	3.9%	17.5%
1992	811,959	107,809	13.3%	41,015	5.1%	18.3%
1993	1,019,065	131,755	12.9%	56,733	5.6%	18.5%
1994	1,253,911	148,208	11.8%	60,614	4.8%	16.7%
1995	1,595,482	167,199	10.5%	67,531	4.2%	14.7%
1996	2,109,636	196,921	9.3%	75,726	3.6%	12.9%
1997	2,776,563	248,612	9.0%	101,205	3.6%	12.6%

Sources: PNB Annual Reports (various years),
DBP Annual Reports (various years),
Philippine Banking Almanac (various issues),
Philippine Statistical Year Book 1999, Table 16.9

Chapter 4.

Aquino Reforms in the early 1990s: Initiating Liberalisation through Regulatory Reform and the Failure of Structural Reform in the Banking Sector

Introduction

Under the Aquino government, the Central Bank implemented various regulatory reforms within the existing legal framework. After the initial economic recovery, the Central Bank undertook various liberalisation measures in the early 1990s. Liberalisation, which was initiated by the Aquino government to redirect active state interventionism, was further promoted in the early 1990s. In the banking sector the Central Bank implemented important reforms such as deregulation of the establishment of new banks and new branches and on foreign exchange control. The banking business experienced rapid changes through regulatory reform.

A confluence of factors facilitated these liberalisation measures, but support from the President and the emergence of a consensus among the Monetary Board members (a majority from the Cabinet) was a critical precondition enabling the Central Bank to initiate liberalisation in the banking sector in the early 1990s. In the beginning of the 1990s signs of economic deceleration appeared. Security was a matter of serious continuing concern for domestic and foreign businesses. In particular, the coup attempt in December 1989, which damaged the centre of the financial district in the country, raised serious doubts about the business climate among foreign investors. In the early 1990s, the Gulf War and natural disasters adversely affected the economy further. The government had to show its strong commitment to reforming the economy to attract foreign investment and loans. The IMF and the World Bank consistently encouraged the liberalisation of the economy and the banking sector. After the end of the "Cold War" and the controversial Senate decision to terminate the lease agreements on the US bases, "special" US support was no longer expected.

After taking office, President Aquino continued to support the Central Bank's initiatives to reform the banking sector. After fierce conflict over the main economic issues and

repeated reshuffles of the Cabinet, the key Economic Secretaries became more cooperative with each other, consensus on liberalisation reform being consolidated as a key economic strategy to attract foreign investment and loans and to promote exports in the early 1990s. Banking reform was broadly supported by the business sector, which expected an improvement in services and a lowering of interest rates as a result of various liberalisation measures. While the entry of new domestic banks provided some big businesses with a good opportunity to enter the profitable banking sector, the big commercial banks, which were the most powerful in the banking sector, were potential losers since the entry of powerful new entrants was a threat to their business. However, once the consensus among policy elites in the Cabinet and the Central Bank emerged, opposition from the banking sector was not strong enough to defeat the liberal reform. It is also worth noting that the big commercial banks were beneficiaries of other liberalisation measures during this period. The significant reduction of the state banks' presence provided the big domestic banks with opportunities to expand their businesses. Another liberal reform measure, namely deregulation of the opening of new branches, was supported by the big commercial banks, which were keen to expand their own businesses. Foreign currency liberalisation also created new business opportunities for them, such as dealing with remittances from overseas Filipino workers.

By contrast, structural reform through the legislative process came to a standstill, although the vital necessity of banking sector reform was recognised. Although the Central Bank advocated several amendments to existing laws to strengthen monetary authority, the President refrained from intervening and left the reforms to the Legislature. In the newly-restored constitutional democracy, the process of structural reform was constrained by the inefficiency of the Bicameral system of the Legislature and by conflicts between the Legislature, particularly the Senate and the President. Under the Aquino government, although the Central Bank implemented various regulatory reforms within the existing legal framework, further structural reforms through the legislative process were not implemented. The capacity of the Central Bank to implement regulatory reforms in the banking sector was enhanced by support from the President and the emerging consensus among the Cabinet. However, the capacity of the Aquino government to promote structural reform through the legislative process

was constrained by the restoration of the Legislature. In this chapter, the key events in the banking sector of the early 1990s, namely liberalisation through regulatory reform and the failure of structural reform under the Aquino government, are explored by focussing on the decisions of the policy elites and the interactions among them in the context of changing political institutions after the restoration of democracy.

Initiating Liberalisation through Regulatory Reform

The transition from the Marcos government to the Aquino government led to changes in the relationship between the President and the Central Bank. In terms of presidential interference in monetary and fiscal issues, there was a sharp contrast between the Marcos presidency, especially in the first half of the 1980s, and that of Aquino. Apart from "behest" loans and the rapid growth of crony banks, President Marcos often intervened in the Central Bank's decisions under the martial law regime in the early 1980s. During the economic and banking crisis, the reform initiatives of the Central Bank were not fully supported by the President. President Marcos reversed the Central Bank decisions to deal with ailing banks, most notably in the cases of the Banco Filipino and the Republic Planters Bank. Massive spending for the elections in 1984 and 1986 seriously damaged monetary stability.

In order to strengthen coordination between monetary and fiscal policy, Aquino added another Cabinet member (Budget Secretary) to the members of the Monetary Board, the decision-making body of the Central Bank. However, unlike Marcos, the new President did not intervene in the Central Bank's decisions. Under the Aquino government, the Central Bank governor and the Secretary of Finance maintained a grip on monetary and fiscal policy. Although there was fierce controversy on fiscal and monetary issues, especially on debt repayments, in her Cabinet and with the Legislature, President Aquino supported the position of the Central Bank governor and the Secretary of Finance, who were in charge of these issues. On the debt repayments issue, the Central Bank governor and the Secretary of Finance were strongly opposed to restrictions on debt repayments through a selective repudiation of Marcos crony-related debts, or the imposition of ceilings on annual debt repayments (debt cap) that were endorsed by the Legislature. Although the Finance Secretary was replaced twice

(Jaime V. Ongpin, Vicente R. Jayme and Jesus P. Estanislao) and Jose L. Cuisia, Jr. replaced Jose B. Fernandez, Jr. as Central Bank governor under the Aquino government, basic stance on this issue and the support the President gave the Central Bank remained unchanged. Under the Aquino government, the Central Bank regained relative autonomy vis-à-vis the Presidency in spite of continuing political uncertainty. This was a critical precondition for the implementation of various regulatory reforms and liberalisation measures in the early 1990s.

After the initial recovery of the banking sector from the ruin of the mid-1980s, the Central Bank took the initiative and began to liberalise the banking system. A Central Bank official notes that "The thrust for the nineties is liberalisation" (Suleik,1992b:14). Senior deputy governor, Gabriel Singson, at that time explained that "a thrust of the policy initiatives" under the Aquino government is "that of removing economic control."[1] In the early 1990s, the most important reform initiatives were the liberalisation of rules and regulations on the establishment of new banks and new branches and on foreign exchange control. In particular, the liberalisation of foreign exchange control, which ended over four decades of pervasive exchange control, was a vital reform due to its long-term impact on the economy.

In February 1990, the Central Bank governor was replaced by Jose L. Cuisia, Jr., who first joined a state financial institution under the Aquino government as administrator of the Social Security System (SSS).[2] Cuisia was chosen by the President as the successor of governor Jose Fernandez, who was appointed by President Marcos. There was no clear explanation for the President's choice but Fernandez's recommendation was seen as an influential factor in her decision.[3] Cuisia was an MBA-holder from the University of Pennsylvania's Wharton School and had extensive experience in the financial sector. He worked for the Ayala Investment & Development Corporation as senior Vice-President for Corporate Finance and later moved to Filinvest Credit Corporation as its Executive Vice-President and Chief Operating Officer. Before

[1] See Business World, 6 January 1992, "Measures encouraging liberalisation were laid last year".

[2] For Cuisia's background, see, for example, Business World, 27 February 1990, "Special Feature: CB; a changing of the guards".

[3] Interview, Paderanga, Jr., 10 June 1997.

President Corazon C. Aquino invited him to join the SSS, he had been President and Chief Executive Officer of the Insular Bank of Asia and America (IBAA) and Director of the Philippine National Bank. Cuisia, who had had a long career in the private sector, essentially shared policy preferences with his predecessor. The new governor was fully committed to reducing state intervention in the banking business and to keeping a "conservative" approach to debt policy. Under Cuisia's governorship, the Central Bank continued to implement banking reforms initiated by governor Fernandez to develop a stable banking sector.

In order to facilitate financial stability and effective resource allocation, the Central Bank took conventional policy measures such increasing the minimum paid in capital, reforms of reserve requirements and rediscounting policy reforms. The minimum paid-in capital, which was increased in 1989, was raised again from September 1990 as follows: (1) for expanded commercial banks from P1.0 to P1.5 billion; (2) for commercial banks, from P500 million to P750 million; (3) for thrift banks (Head Offices - National Capital Region) from P10 to P20 million; (4) thrift banks (Cebu and Davao) from P5 to P10 million and (5) for investment houses from P20 to P50 million for old and P100 million for new businesses.

To improve resource allocation by reducing intermediation costs, a gradual unification of reserve requirements across banks and deposit types was implemented in 1989 and 1990. A series of adjustments to the reserve requirement ratios for demand deposits, short-term deposits and deposit substitutes over this period of time was undertaken to equalise and rationalise the imposition of the reserve ratio across banks and non-banks (Suleik,1992b:16).

The Central Bank also reformed rediscounting policy, rationalising its rediscounting window to enhance its role as a mechanism for liquidity control, rather than for credit allocation. The CB moved away from its early role as the "bank of first resort" (Suleik,1992b:16). The Central Bank gradually reduced its role in the credit allocation programme by transferring the administration of ALF, IGLF and APEX funds to the Land Bank of the Philippines and the Development Bank of the Philippines in 1990.

In May 1989, the moratorium on the establishment of new banks was lifted through the issuance of CB Circular 1200.[4] This was followed in April 1991 by the easing of regulation regarding the establishment of new branches under Circular 1281. An auction system was introduced for the awarding of franchises to eligible commercial and thrift banks wishing to open more branches in Metro Manila, in the big cities of Cebu and Davao and in the first-class cities and municipalities. In addition, banks were provided with incentives to open more branches in other areas, particularly those which continued to be "under-banked" in relation to economic activity and population. To open branches in these areas did not require minimum bids. Rural banks were also given the privilege of nationwide branching under Circular 1280 of April 1991, to improve credit delivery in the countryside. The regulations pertaining to ATMs were also eased, the operation of ATMs in off-site or off-premises areas being allowed in May 1991 to facilitate the delivery of banking services to a broader of clientele.

Foreign exchange liberalisation can be seen as a critical reform to support the key development strategy under the Aquino government, which stressed export promotion and foreign investment as an engine for economic growth.[5] Cuisia stated that "the deregulation of foreign exchange transactions is aimed at substantially enhancing the country's export trade as well as its ability to attract foreign investments".[6] After the initial economic recovery, including increases in exports, improvements in the foreign reserve position and the reduction in foreign debt, the government took initiatives to liberalise the economy. Along with the trade liberalisation efforts and the Foreign Investment Act of 1991, foreign exchange liberalisation was seen as the key measure to promote exports and to attract foreign investment. It must be noted that foreign exchange liberalisation led to a significant reduction of the Central Bank's direct role in controlling and allocating foreign exchange.

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[4] For the liberalisation of regulation relating to new banks and new branches, see Martinez (1993) and Suleik (1992b:15).

[5] For an overview of the foreign exchange liberalisation, see Zialcita (1994).

[6] Jose L. Cuisia, Speech delivered before the meeting of the Wharton Club of the Philippines on 29 July 1992, reprinted in *Philippine Banking Almanac, 1993 Edition*, pp.53-56.

In 1991, liberalisation of the rules governing foreign exchange was announced and gradually implemented. The full implementation was scheduled to begin the following year. The key measures included the following: (1) the allowable retention of export receipts by exporters was raised to 40 per cent from the previous ceiling of only 2 per cent; (2) the access of exporters to foreign exchange resources from the foreign currency deposit units (FCDU's) was increased; (3) full and immediate repatriation privileges for all types of foreign investment - whether direct equity or in listed shares / securities was allowed; and (4) non-trade foreign exchange regulations were liberalised (Suleik,1992b:16).[7]

In the early 1990s, liberalisation reform was accelerated by various factors. By the end of the 1980s, the high economic growth period brought about by expanding government expenditure was ending. GNP slowed down to 0.5 per cent in 1991. The Gulf War led to higher oil prices and to a reduction in remittances from Filipino overseas workers in the Middle East. Natural disasters adversely affected the economy further. The political instability was the most serious threat to attracting foreign investment. In particular, the coup attempt in December 1989, which damaged the country's financial centre, raised serious doubts among foreign investors about the business climate of the country. The IMF and the World Bank continued to encourage liberalisation efforts. Special support from the US government was not expected after the controversial decision by the Senate in 1991 to terminate the lease agreements on the US bases and the end of Cold War.

Faced with a declining economy, a loss of "special" support from the US government and continuing political instability, the Aquino government decided to promote liberalisation reform, to attract further foreign investment and loans which were seen as essential for economic growth. The Aquino government recognised that improving the economy was crucial to the survival of the government. After the coup attempt in December 1989, the Aquino Cabinet members held a meeting in early 1990 where they acknowledged their failure to improve economic conditions, particularly with regard to rural and urban poverty.[8] The Cabinet members reconfirmed the critical importance of

[7] For detailed lists of the liberalisation measures, see Zialcita (1994: Table 12.1.).

[8] See, Manila Chronicle, 19 May 1990, p.14, cited in Montojo (1998:219).

the liberalisation reforms which aimed to expand the economy through market-mechanisms.[9] A solid consensus among Cabinet members was crucial to the promotion of liberalisation. In terms of the working relationships among the Aquino Cabinet members, there was a sharp contrast between the early years of the Aquino government and the latter years of the early 1990s. The former Director General of NEDA, Paderanga, pointed out that the working relationship between Cuisia, Estanislao and himself was totally different from that between Fernandez, Ongpin and Monsod in the first Cabinet of the Aquino government.[10] According to him, this strong consensus on economic policy was the critical driving force behind liberal reforms. Estanislao also stressed the importance of the decisive leadership of President Aquino and of cooperative initiatives taken by Aquino Cabinet members to liberalise the economy in the early 1990s.[11] The appointment of a new Central Bank governor helped to foster a co-operative relationship among the Cabinet members. In discussions of fiscal and monetary policy, it was not very easy for governor Fernandez, who was appointed by President Marcos, to build good working relationships with some of the Cabinet members and legislative leaders. Fernandez was often severely criticised, due to the Central Bank's role in the accumulation of the former dictator's personal wealth.

By the 1990s, liberalisation measures were broadly supported by key policy-makers and domestic businesses. The "competitor's" policy was studied and referred to as the model of liberalisation. The other ASEAN Four countries, including Indonesia, Malaysia and Thailand, were seen as competitors which were more successful in promoting exports and attracting foreign investment to expand their economies through liberal reforms. For example, the Central Bank deputy governor at that time, Singson, explained that the loosening of foreign exchange regulation was in keeping with the "more liberal exchange regulatory environment of competitor countries in the ASEAN region such as Indonesia, Malaysia and Thailand".[12] Until the foreign currency crisis of

[9] For the economic reform package (or "new economic order") and solid consensus, see, for example, Business World, 15 June 1990, p1; 18 June 1990, p1; 20 June 1990, p1; 21 June 1990, p1; 25 June 1990, p1; 27 June 1990, p1

[10] Interview, Dr. Cayetano Paderanga, Jr., 10 June 1997.

[11] Interview, Dr. Jesus Estanislao, 3 July 1998.

[12] Business World, 6 January 1992, "Measures encouraging liberalisation were laid last year". See, also Suleik (1992a:37).

1997, the "competitor's policy" had been an influential model of economic policy. A Central Bank official pointed out that a study of the other ASEAN Four countries' policy was the first thing needed to form a draft of regulatory reform.[13]

There were many beneficiaries of these liberalisation measures among domestic businesses which expected improved services and lower interest rates. There were also strong proponents for the entry of the new domestic banks. This liberalisation measure created an opportunity for some big businesses to enter the profitable banking sector. Asian Bank became the first commercial bank authorised to upgrade from a thrift bank in more than a decade. The bank was backed by the Andres Soriano Corporation, the holding company of one of the country's largest industrial conglomerates. Strong new entrants were a potential threat to the existing big commercial banks, which constituted the most powerful segment of the banking sector. However, the consensus which emerged on the reform measure among the Monetary Board members included the Cabinet members; opposition from the existing big banks was not strong enough to resist the reform measure.

The deregulation of the opening of new bank branches was welcomed by the commercial banks, which were keen to expand their businesses, although the Central Bank denied that the deregulation was the result of strong pressure from the commercial banks. Central Bank officials stressed that the deregulation had been carefully planned by the Central Bank after many years' study and discussion about the number of bank branches needed to improve financial stability and services.[14] The total number of the expanded Commercial Banks' branches increased from 1273 in 1990 to 1618 in 1992.

[13] A Monetary Board member commented that he was sometimes irritated by the attitude of Central Bank officials to policy reform. They were not keen to do something that other countries had not yet done. The member insisted to them that they should have done what they thought was best for the Philippine economy. It did not matter what other countries were doing. Interview, Mr. Guillermo Carague, 25 November 1997.

[14] Interview, Mr. Fernando Silvoza and Ms. Editha Alido, 25 November 1997.

The impact of deregulation on foreign exchange was a further reason why the banking sector supported the liberalisation measures. Foreign exchange liberalisation provided new business opportunities, especially for the expanded commercial banks which enjoyed certain advantages in foreign currency dealing. For example, Rafael B. Buenaventura, the President of PCIBank at that time, welcomed the reform to liberalise foreign exchange control, since it created a business opportunity with regard to foreign workers' remittances,[15] which was estimated to have risen from US$ 4 billion to US$ 7 billion a year at that time. This was attractive in a country whose annual export of goods totalled only US$ 8.8 billion in 1991.

These liberalisation measures, with the regulatory reforms initiated by the Aquino government in the early 1990s, played a critical role in improving the financial system (see Gochoco-Bautista and Reside, Jr., 2000:86-87) although liberalisation did not always facilitate the development of a stable banking sector and economy. In the short run, they stimulated the banking sector without destabilising the financial system. The new banks tried hard to attract deposits with favourable saving rates and various campaigns and these moves also stimulated the businesses of the existing banks. In the more competitive business environment, management and the owners of banks were forced to be more concerned about solvent lending activities and effective management, at least in the short run.

The Central Bank was able to initiate liberalising regulatory reform in the early 1990s. With support from the President and a consensus among the Cabinet and Monetary Board members, it was not very difficult for the Central Bank to promote liberalisation in the banking sector through regulatory reform. By contrast, structural reform through the legislative process under the Aquino government was not smooth, as will be seen in the following section.

[15] See Rafael B. Buenaventura, Speech delivered at the Centre for Research and Communication (CRC) on 27 August 1992, reprinted in *Philippine Banking Almanac, 1993 Edition*, pp.17-20.

The Restoration of the Legislature and Banking Sector Reform

The restoration of the Philippine Congress on 27th July 1987 marked the return of the country to parliamentary politics. The outcome of structural reform through the legislative process was constrained by institutional and organisational factors related to the newly restored Legislature. The executive-legislative relationship reemerged as a critical factor influencing the success or failure of economic reform.

The Aquino government had failed to enforce structural reforms in the banking sector, although it had implemented some important economic reforms through the legislative process such as the Foreign Investment Act. After the disastrous failure of the banking sector under the Marcos government, the importance of Central Bank reform was broadly recognised. The establishment of an independent monetary authority was one of eighty-one specific reforms identified in the 1987 Constitution.[16] The Central Bank advocated reform and the World Bank and the IMF strongly supported it. In addition, big commercial banks were in favour of Central Bank reform. The Bankers Association of the Philippines (BAP) also endorsed the reform. They largely shared the idea that, under the authoritarian government of the Marcos era, the economy and the banking sector had been adversely affected by the lack of an independent Central Bank. Since there was no strong opposition in the business sector, the establishment of an independent Central Bank was seen as a relatively easy structural reform.

Commentators often point to "weak" Presidential leadership on economic reforms under the Aquino administration.[17] However, in terms of fiscal and monetary policy, this was not entirely accurate since the President did not compromise her position with the Legislature on key fiscal and monetary policy. President Aquino had been determined to pursue her administration's policies with respect to the country's external debt and

[16] For a review of the performance of Congress with respect to the specific agenda, see Institute for Strategic and Development Studies (1998) "Evaluation of the Performance of the 8th Philippine Congress in Relation to the Legislative Agenda in the 1987 Constitution" in Abueva and Roman (1998a:116-125).

[17] See, for example, Daily Globe, 30 June 1992, "Departure, Not Continuity, from Aquino's Leadership", by Noel C. Cabrera and Manila Standard, 30 June 1992, "A Failed President", by Nestor Mata, cited in Abueve and Roman (eds.) (1993).

the management of the budget deficit. This was a serious source of conflict between the Executive and legislators. Both the House and the Senate made strong efforts to alter the government's policy. Restrictions on foreign debt repayments were popularly supported by the general public. In addition, the policy led to an increase in government budgets, which were influenced by legislators. The failure of the structural reforms highlights the difficulty of reform under a constitutional democracy which faced economic turmoil and political instability. The legislative process was particularly slow under the newly-restored bicameral legislature. There were no effective formal or informal procedures or rules to facilitate reaching a consensus on the priority of bills in the national interest. Under the constitutional democracy, the conflicts between the Executive and the Legislature became a serious obstacle to forming and implementing vital economic reforms.

Before the restoration of the Legislature, the Central Bank proposed amendments to banking laws to the President. The main objectives of the amendments to the Central Banking Act included: (1) to enhance the supervisory power of the Central Bank to prevent and penalise irregularities and fraud by banks; (2) to clarify the roles of the receiver and liquidator and their powers and privileges; (3) to impose stiffer penalties for submitting false statements and violation of laws and regulations; and (4) to prohibit banks with outstanding Central Bank emergency advances from expanding the total volume of its loans or investments, or granting new loans or renewals of existing loans (see Lamberte,1989:65). The Central Bank also submitted proposals for amendments to the General Banking Act, most of which focused on curbing insider abuses including DOSRI loans (ibid.).

However, the President was not keen to amend these laws by Presidential decree. President Aquino acted on only two of the recommendations; one was the clarification of the role and powers of the receiver and liquidator and the other related to inter-bank settlements. Mario B. Lamberte, the Deputy Director of the PIDS and a leading expert on the financial issues facing the country, explained that the President simply chose the two least controversial issues.[18] Therefore, the fate of structural reform rested with the Legislature.

[18] Interview, Dr. Mario Lamberte, 23 June 1998.

After the Central Bank failed to persuade the President to amend the banking laws by presidential decree, the World Bank mission was invited in 1988 to evaluate the financial system of the Philippines. The mission endorsed the overall direction of the Central Bank's initiatives for structural reforms (see World Bank,1988). They agreed with most of the CB-initiated proposed amendments to the Central Bank Act and General Banking Act. The World Bank incorporated them into the set of conditions attached to the Financial Sector Adjustment Loan.

The recommendation by the World Bank mission covered a broad range of issues including (a) banking operations and financial conditions; (b) supervision and regulation of commercial banks; (c) supervision and regulation of securities market institutions; (d) legal issues affecting the Central Bank; (e) an enlarged role for the Philippine Deposit Insurance Corporation; (f) legal issues involved in debt recovery and insolvencies; (g) a proposal to set up special courts for banking and insolvency cases; (h) a government / Central Bank-directed credit programme; and (i) gaps in financing selected real sectors (export finance, provision of long term credits and foreign exchange resources).[19] With respect to the enhancement of the regulatory power of the Central Bank, the key recommendations included the following issues: rules on emergency advances to banks; criteria for bank insolvency; regulatory instruments, detecting and countering insider abuses; and protection of Central Bank officials from law suits.

However, the World Bank's support for structural reform in the banking sector was not sufficient to push structural reforms through the legislative process. Under the Aquino administration, the fate of structural reform was left largely in the hands of the Legislature, since President Aquino was not keen to implement structural reform by Presidential decree before the Legislature was restored in 1987. The legislative process required to pass laws is "usually a long and tedious process, made more so, by the present bicameral structure" of Legislature (de Leon, in Velasco,1989:96). Particularly under the Aquino government, the legislative process was constrained by the institutional inefficiency of the Legislature, newly-restored after more than fifteen year's

[19] For details, see World Bank (document) (1988:155-164).

closure, and the fierce conflicts between the Executive and the Legislature, particularly the Senate, over key legislation including foreign debt issues, land reforms, annual budgets and the U.S. bases issue.

These fierce conflicts can be understood in the context of the unique features of the Aquino government during the transitional period: the suspension of legislative elections between 1987 and 1992, and the continuing tradition of Philippine parliamentary politics, namely the lack of a strong political party which shared the legislative agenda and disciplined the voting decision of member legislators. The 1987 elections demonstrated the popularity of President Aquino, who deposed Marcos. The elections resulted in a landslide victory for Lakas ng Bayan (LABAN), the pro-Aquino coalition party, which captured 150 of the 200 contested seats in the House and 22 of the 24 seats in the Senate. Aquino's popularity and widespread anti-Marcos sentiment were the main factors contributing to this landslide victory (see Velasco,1989:68). However, this victory in itself did not secure the successful promotion of the Executive's legislative agenda. LABAN itself was a broad coalition party with no common legislative agenda. Once elected, legislators did not need to cooperate with the President in order to ask for her support for immediate electoral purposes since there was no legislative election between 1987 and 1992. In addition, although the LABAN party's candidates were endorsed by the President in the elections, President Aquino did not belong to the party. President Aquino did not lead any political party which she could use to bridge the gap between the executive and legislative branches for her legislative agenda.

To understand the difficulty of implementing structural reform under the newly-restored democracy, it is worth briefly examining the legislative process involved in policy-making. Under the 1987 Constitution (Section 1, Article VI), the Congress is composed of two houses: the Senate and the House of Representatives. The Senate is a nationally-elected body with 24 seats. The House of Representatives is composed of not more than 250 members, to be apportioned on the basis of area and population. In

the 1987 elections, 200 legislators were elected.[20]

Members of the Senate and the House can file bills for legislation on almost any subject. The Senate is generally expected to concentrate on legislation which is of national concern; the House of Representatives, in addition to national concern, tends to spend more time on bills of limited concern. These expectations reflect the responsibilities of each House, as stated in the Constitution. Under the 1987 Constitution, all treaties or international agreements are ratified by the Senate (Section 3, Article XVIII) while all appropriation, revenue or tariff bills, bills authorising an increase in public debt, bills of local application and private bills are initiated by the House of Representatives (Section 24, Article VI). In the bicameral structure of the Congress, a bill has to be discussed and passed in both the House and Senate. Thus, two bills on the same issue, a House bill and a Senate Bill, are filed and discussed in each committee and on the floor of the House and the Senate.

Apart from making laws, the Legislature expresses its concern and declares its intention to act upon important issues facing the country by passing resolutions. A resolution is filed and is discussed in the Legislature, but a resolution, except for joint resolutions, does not constitute legislation and need not be presented to the President for approval. The 1987 Constitution also confers on the Senate and the House or any of their committees the power "to conduct inquiries in aid of legislations in accordance with its duly published rules of procedure" (Section 21 of Article VI). The so-called Blue Ribbon Committee of the Senate, otherwise known as the Committee on Accountability of Public Officers and Investigations, is responsible for the investigations into the conduct of public officers.[21]

A large amount of legislative work normally rests with the Committees. Every bill filed by a member of either the Senate or the House is referred to one or more committees. A Committee is seen as a sub-division of Congress which prepares a piece of legislation

[20] In addition to 200 seats, from the 1998 election, 50 representatives were elected through the party list system, which essentially aimed to choose representatives from minority political organisations. Large parties were excluded from the party list system.

[21] For an overview of the investigative function of the Senate and the Committee's activities during the first Congress after the restoration, see Salonga (1995:163-184).

for enactment. Through study, discussion and public hearings in a Committee, a bill is finalised. The chair, who is appointed by the Speaker of the House, or the President of the Senate, who is elected by the members, is expected to play a vital role. At the eighth Congress, the first Congress after the restoration in 1987, the Senate had 35 permanent or standing Committees and the House had 43 committees. Since there were 24 senators, each senator was heavily burdened with committee work. For the First Regular Session of the newly-restored Senate, each senator was a member of an average of 21 standing Committees. Fourteen of them were also Chairs of at least two committees. For the consideration of important issues, there tends to be less reliance on committee discussion in the Senate and more on deliberation from the floor, since there is little opportunity to discuss matters among Senators in a Committee. Senators are often occupied by their work for committees which they carry the responsibility of chairing. As substitutes for the Senators, their staff often attend other committees of which the Senators are members.

The final form of a bill is shaped by the Conference Committee, which is composed of selected members of both the Senate and House. In the Conference Committee, the points of difference between the House and Senate bills are discussed. It is expected that the House and Senate will reach agreement about the final form of a bill, although there is no stated rule as to how such a compromise should be reached. Neither the House nor Senate rules are clear on the extent to which the Conference Committee can settle differences. Legislative leaders, including Committee Chairs of the Senate and House, the Senate President and the Speaker of the House, play a crucial role in forming a final bill by settling the differences between the two bills, in particular in controversial cases.

The Failure of Central Bank Reform through the Legislative Process

The importance of structural reform in the banking sector had been broadly recognised after the economic crisis. In particular, the establishment of an independent monetary authority was seen as a critical and urgent task, due to fiscal and monetary mismanagement under the Marcos dictatorship. The 1987 Constitution states that:

> "The Congress shall establish an independent central monetary authority, the members of whose governing board must be natural-born Filipino citizens, of known probity, integrity and patriotism, the majority of whom shall come from the private sector. They shall also be subject to such other qualifications and disabilities as may be prescribed by law. The authority shall provide policy direction in the areas of money, banking and credit. It shall have supervision over the operations of banks and exercise such regulatory powers as may be provided by law over the operations of finance companies and other institutions performing similar functions" (Section 20, Article XII).

A bill relating to independent monetary authority was filed in the House on 9th May 1988 by Exequiel B. Javier (Antique) who was chair of the Sub-Committee on the Banks, Currencies and Miscellaneous Matters.[22] Javier was a former corporate lawyer who had experience in banking and financial businesses. He was one of the founders of the BONIFACIO human rights lawyers group. The filed bill was referred to the Committee on Government Reorganisation chaired by Bienvenido O. Marquez, Jr. (3rd District, Quezon), who was also a former corporate lawyer with a knowledge of banking. The reason why the bill was initially referred to the Committee on Government Reorganisation rather than to the Committee on Banks and Currencies was not clear. But a secretary of the Committee on Banks and Currencies points to the lack of coordination and inefficiency as a "bureaucratic" problem related to filing and allocating bills in the House.[23] The filed bills are allocated to a Committee by the administration of the House, without consulting the author or committee. The author of the bill, Exequiel B. Javier, was often invited to the Committee on Government Reorganisation as a guest.

[22] House Bill No. 9126, an Act amending Republic Act No. 265, was amended to establish the central monetary authority, defining its role, responsibilities, objectives and powers in the administration of the monetary, credit and banking system and for other purposes. Co-authors are Ramon S. Bagatsing, Jr. and Renato P. Dragon.

[23] Interview, Atty. Ramon Federizon, 15 May 1997.

The main points addressed by the amendments included:[24] (1) the composition of the Monetary Board; (2) legal protection of Central Bank officials from legal action; (3) the enhancement of the Central Bank's powers to supervise banks including the power of investigation; (4) the imposition of stricter sanctions to prevent violation of banking laws; (5) the clarification of the PDIC's role as a receiver of closed banks; (6) the redefinition of the processes and criteria involved in bank closures; and (7) the provision of clearer rules for emergency loans. These were not dissimilar to the main points addressed by the previous recommendations of the Central Bank, although the Central Bank's recommendations did not include the issue of the composition of the membership of the Monetary Board.

In May 1988, the Committee started to discuss the bill intended to establish the Central Monetary Authority. However, its slow process could be seen as a typical example of the common perception of the legislative process. Although there were useful public hearings on key issues and position papers were submitted by various organisations and experts, the process of law-making was repeatedly delayed, particularly in the first two years. The Central Bank officials were regular participants in a resource capacity at the committee meetings. Governor Fernandez and deputy governors were often invited to the committee meetings.[25] However, the Central Bank Bill was not given high priority among the other bills on which the Committee worked. The Committee dealt with a variety of bills and resolutions: for example, HB 24664 "The National Stud Farm"; HR 924 "the Decentralisation Bill"; HB 5644 "An Act Creating the Department of Ethnic Affairs"; HB 28649 "The Creation of the Department of Energy"; and HB 532 "Philippine Statistical System". In August 1989, three Subcommittees were created by the Committee, which still had a very large jurisdiction. For example, Subcommittee A, chaired by Enrico G. Dayanghirag, covered 24 institutions which were responsible for key development issues including education, agriculture, land reform, trade and industry

[24] House Bill No. 9126 and Salient Features of H.B. No. 9126 prepared by Committee on Government Reorganisation.

[25] Other key resource persons were officials from the Department of Finance and representatives of the Bankers Association of the Philippines. See Committee Records and Minutes of the Regular Meeting of Committee on Government Reorganisation on 2 June 1988;13 September 1988; 29 November 1988; 9 May 1989; 18 May 1989; 25 May 1989; 6 June 1989; 8 August 1989; 18 September 1989; and 29 March 1990.

and finance.[26]

The Executive had deliberately kept a distance from legislation concerned with the Central Monetary Authority. Although the Committee requested the Executive to submit a position paper or comments on the bill, Executive Secretary Catalino Macaraig, Jr. politely declined the request. Macaraig explained that, since the 1987 Constitution (Article XII, Section 20) urged the establishment of an independent central monetary authority, providing comments on the bill "could be construed as being in violation of the independent central monetary authority".[27]

The slow process by which legislation moved through the House was a matter of serious concern for the Central Bank, Department of Finance and the Bankers Association of the Philippines. They asked the Committee to act on HB9126 at the earliest possible opportunity.[28] The author of the bill, Rep. Javier, also shared this concern and expressed the opinion that the Committee on Banks and Currencies would be in a better position to deliberate on the bill.[29] With the co-operation of the Committee on Banks and Currencies, a bill (HB30508) which substituted HB 9126 with minor changes was filed and the Committee Report on the bill was submitted in September

[26] For the membership list and jurisdiction of these three subcommittees, see Committee Records and Minutes of the Regular Meeting of the Committee on Government Reorganisation on 8 August 1989. The jurisdiction of Subcommittee A included: Department of Agriculture; Department of Agrarian Reform; Department of Environment and Natural Resources; Department of Education, Culture and Sports; Department of Trade and Industry; National Economic and Development Authority; Department of Finance; Department of Budget and Management; Energy Regulatory Board; Games and Amusements Board; National Computer Centre; National Statistical Coordination Board; National Stud Farm; Office of Energy Affairs; Securities and Exchange Commission; Presidential Commission on Culture and Arts; Presidential Commission on Good Government; Presidential Committee on the Philippine Nuclear Power Plant; Presidential Management Staff; Sacobia Development Authority; President's Centre for Social Studies; Philippine Deposit Insurance Corporation; Philippine High School for the Arts and Southern Philippine Development Authority.

[27] See Letter from Catalino Macaraig, Jr. (Executive Secretary) to Bienvenido O. Marquez (Chairman, Committee on Government Reorganisation, House of Representatives) on 21 October 1988.

[28] See Committee Records and Minutes of the Regular Meeting of the Committee on Government Reorganisation on 18 September 1989.

[29] Internal Memo (Code:GIC011), Committee on Government Reorganisation of 21 March 1990: "Minutes of the Meeting with the CB Governor Cuisia".

1990 for a second reading.[30] After a prolonged delay, the House Bill was finally approved by the House on 24 October 1991 and transmitted to the Senate for debate in the Conference Committee. However, it should be noted that the bill concentrated on the question of the Monetary Board and the enhancement of the Central Bank's regulatory powers. Some critical provisions, such as the transfer of the Central Bank's losses, which had become a highly controversial issue from late 1990, were not discussed by the House.

The legislative process in the Senate was even slower than that in the House and the Senate did not respond promptly to the passage of the bill in the House. Since the Senate bill was not finalised, the Conference Committee was not held for discussion of the bill. The fate of the bill and of the proposal to establish an independent Central Monetary Authority was left in the hand of the next Congress and Executive. The Senate's inaction was a result largely of its limited legislative capacity and, more importantly, the fierce conflicts between the Senate vis-à-vis the President and the Central Bank. After the restoration of the Congress, the Senate Committee on Banks, Financial Institutions and Currencies chaired by Alberto G. Romulo, had started to prepare the bill to establish an Independent Central Monetary Authority. However, the process of the legislation in the Senate was even slower than it had been in the House. By September 1989, the bill had not yet been filed, although the Committee had started to call for position papers from various organisations and experts on the unnumbered bill.[31]

The first public hearing of the Senate Bill to amend the Central Bank Act, with experts including the Central Bank governor, was held in October 1990 after the Committee Reports of the House on this issue had been submitted and the Second Reading had scheduled. According to Sen. Romulo, the Central Bank was partly responsible for the delay, since the Committee did not receive a response from the Central Bank for a long

[30] House Bill No. 30508, an Act amending Republic Act No. 265, as amended to establish a Central Monetary Authority which shall be known as the Central Bank, defining its role, responsibilities, objectives and powers in the administration of the monetary, credit and banking system and for other purposes. Twelve other members of the House are co-authors.

[31] For example, the BAP submitted its position papers and comments on both the House Bill (H.B.9126) and the unnumbered Senate Bill in September 1989.

time after the Committee had asked the Central Bank for comments on their bill in February or March 1990.[32] The Senate Committee filed two bills, S.B.1514 and S.B. 1515, to amend the Central Bank Act (R.A. 265). S.B. 1514 focused on provisions regarding the Monetary Board and addressed the issue of the independence of the Central Bank. S.B. 1515 included provisions to amend the whole of the existing law.

Although the House Bill seemed to be the outcome of close cooperation between the House Committee and the Central Bank, the Senate Bill included some provisions which were very different from the Central Bank's position.[33] For instance, the bill stated that the minutes of the Monetary Board meetings should be released within five days without any restrictions. Although the Central Bank agreed with the principle of transparency, the disclosure of information without any limitations was unacceptable for a monetary authority which dealt with sensitive monetary issues. Also, in the Senate bill, the Central Bank governor who chaired the Monetary Board was different from the head of the Central Bank who was called a Chief Executive Officer.

The structural problems of the bicameral Congress were among the main factors behind the slow functioning of the Senate Committee. Since there were only twenty-four senators, many of them chair two committees. Alberto Romulo chaired both the Committee on Banks, Financial Institutions and Currency and the Committee on Social Justice, Welfare and Development. He was also vice-chairman of three Committees (on Finance; Labour, Employment and Human Resources; and Local Government) and a member of twenty-four other committees. The Senate floor tends to be the place for lively discussion among senators, since they do not have many opportunities to argue in Committee meetings. Senators are also active in considering various issues of national concern, apart from law-making. Romulo's Committee was very active in investigating the financial issues of the day, for example, the transfer of the CB's debts to the national

[32] See Senate Committee Records: Committee on Banks, Financial Institutions and Currencies on 25 October 1990.

[33] See Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 25 October 1990.

government,[34] foreign currency loans to the oil companies,[35] and high interest rates.[36]

In addition to these problems, it must be stressed that fierce conflicts concerning financial issues between the Executive and the Senate can be seen as a critical factor with regard to the slowness of the Committee and the distance between the Committee and the Central Bank.

The Committee chairman, Alberto Romulo, was a lawyer and CPA-holder. He was elected to the Batasang Pambansa in the 1984 elections and was a pillar of the opposition to the Marcos regime. Romulo was also a former member of the Monetary Board as the Secretary of Budget and Management under the first Aquino Cabinet until he resigned from the post to run for a Senator's position in the May 1987 elections. He recognised the importance of an independent monetary authority. He stressed the vital importance of the Central Monetary Authority in a Committee Meeting.[37] Nonetheless, the Chairman did not place the issue of an independent monetary authority high up the list of the Committee's priorities. For the chairman, it was clear that the foreign debt issue was the most important of the various issues related to financial institutions and monetary policies.

The foreign debt had been the most controversial financial issue under the Aquino administration and a source of fierce conflict between the Senate and the Executive from the early period of the restoration of the Legislature. The Senate firmly opposed Aquino's policy on the foreign debt issue, but the Aquino administration did not alter its

[34] For a summary of the problem, see *The Manila Chronicle*, 23 May 1990, "Policy Lessons from CB's losses" by Benjamin E. Diokno (Undersecretary, Department of Budget and Management and Professor, School of Economics, the University of the Philippines). See, also Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 16 May 1990, 21 May 1990 and 23 May 1990.

[35] See Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 27 September 1990.

[36] See Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 17 January 1991.

[37] He mentioned that "it becomes more obvious now that a Central Monetary Authority really must be passed". See Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 23 May 1990.

policy, which had been adopted on the recommendation of the Central Bank and the Department of Finance. The Senate filed resolutions to express its opposition to the Executive on this issue from 1987 to 1991, until the end of the eighth Congress (the first Congress after the restoration). For example, the Senate filed S.R. 44 in 1988 to express its disagreement with foreign debt policy.[38] S.R. 148 was also filed in late 1990 to investigate the country's foreign loan portfolio and determine which loans were fraudulently obtained or guaranteed.[39] The fierce conflict over the issue of debt repayment reached its height when the Congress enacted the 1992 General Appropriations Act, which included a provision for the suspension of payment on a loan contracted for the Bataan Nuclear Power Plant. The President vetoed certain items in the 1992 General Appropriations Act. The Congress tried to override the presidential veto, although the attempt failed.

Sen. Alberto Romulo and his Committee took strong initiatives to investigate the problem of fraudulent loans under the Marcos government. Sen. Romulo was a leading advocate for partial debt repayment, which put him in opposition to government and Central Bank policy. There was fierce disagreement between Sen. Romulo and governor Fernandez on this issue. In addition, in the early 1990s, the Senate's ability to enact the bill was severely undermined by the US bases issue, which resulted in the most controversial decision taken by the Senate during the Aquino Presidency and dominated its discussions between February and September 1991 (see Salonga,1995, Chapter 9).

The necessity of Central Bank reform seemed not to be very controversial, since it was broadly supported after the failure of the Central Bank to regulate the banking sector under the Marcos government, particularly in the first half of the 1980s. The 1987 Constitution clearly stated that an independent monetary authority should be established by the Congress. The IMF and the World Bank were supportive of the

[38] The S.R. 44: "Resolution to Express the Sense of the Senate to Suspend, Avoid, and Disengage from Any Further Payments on the Balance of the Debt Incurred in Connection with the Philippine Nuclear Power Plant, Pending the Formulation of a National Consensus on Our Foreign Debt Problem, and to Seek the Final Condonation of, or Definitive Relief from, the Said Balance."

[39] For the discussion of this resolution, see Senate Committee Records: the Committee on Banks, Financial Institutions and Currencies on 28 November 1990.

reform. In particular, the World Bank encouraged reform through the Financial Sector Adjustment Loan and the Central Bank was keen to advocate reform to enhance its regulatory powers. The BAP, which represented the banking sector (big commercial banks in particular), was also in favour of reform.

Nevertheless, structural reform was not implemented. After a long tradition of executive dominance in policy-making under the Marcos authoritarian regime, Aquino was very selective in her use of Presidential power to implement structural reform while she held absolute law-making power. The President was not keen to enforce her will on the legislative process in a decisive way. Once they were elected, legislators did not need to be cooperative with the President's legislative agenda in order to ask her to support them in immediate elections, since there no legislative elections were held until 1992. In addition, the President did not head any political party which could act as a bridge between the Executive and Legislative branches as she sought to push through her legislative agenda. Although the Executive attempted to improve coordination with the Legislature to prioritise bills,[40] it had only limited success. The House approved a bill (HB 8697) to establish a joint Executive-Legislative Development Council (ELDC), which aimed to provide greater coordination in government, in terms of economic and political reform planning and implementation. However, the President did not endorse the establishment of the ELDC. The President tended to emphasise the importance of the separation of the Executive and Legislative branches of the democratic government. Under the newly-restored constitutional democratic system, without a strong Presidential initiative, the government, which lacked the formal and informal procedures and rules needed to prioritise economic reforms and suffered from the lack of coordination between the Executive and the Legislature, was not able to implement the vital reform.

Conclusion

The Aquino government had a mixed record in terms of banking sector reform. Although the key structural reforms, including amendments to the Central Bank Act and General Banking Act, were not implemented by the government, the banking sector

[40] For example, the President established the Legislative Liaison System, see PMS (1992b:18-22).

experienced radical changes during this period. Soon after Aquino came to power, the insolvent state banks, which were left in ruin by the former dictator, were rehabilitated and their presence was significantly reduced. After an initial recovery of the economy, the Central Bank facilitated the liberalisation of the banking sector through various regulatory reforms. The banking sector was revitalised by the economic recovery, the elimination of Marcos's crony banks, a reduction in the state bank's presence, the entry of new commercial banks and the establishment of new branches and new banking businesses such as those dealing with remittances from Filipino workers in foreign countries.

As "restorationists" claim, there was strong continuity in Philippine society, politics and the economy in the transition from Marcos to Aquino. The transition did not affect "the social structure" in terms of the concentration of wealth. In spite of the regime change, the family backgrounds of the political elites were largely unchanged. President Aquino tended to rely on familial ties to consolidate support in the Legislature for the government, although they were not always supportive. She had relatives in both the Senate (a brother-in-law) and the House (a brother, an uncle, a cousin and sister-in-law). Her husband's close friends and relatives also occupied important posts in the government. In addition, businesses which opposed the domination of Marcos's cronies and supported the "EDSA revolution" had a decisive advantage, benefitting from policy reforms such as the redirection of active state interventionism, privatisation and liberalisation, although Aquino's "cronyism" was very different from that of Marcos in terms of its plurality, accountability and volume.

Nevertheless, the transition triggered a critical change in economic policy and policy-making. The Aquino government first took strong initiatives to alter the economic policy adopted by the Marcos government. Under the new economic development strategy, the government reduced state involvement in major export commodities and financial markets. In addition to popular support for the Aquino government, which terminated the long term dictatorship by extraordinary means, this redirection of economic policy generated broad support from the US government, the IMF, the World Bank and other donor countries. With regard to foreign debt policy, the US government used its strong influence to assume full responsibility for all foreign debts

left by the previous government. However, once the Philippine government adopted the US (and other creditors) recommended foreign debt policy, the US, the IMF, the World Bank and other donor countries were supportive of the economic policy of the Aquino government. The continuing US security concern also helps to explain this support. Due to this broad support, the government was able to adopt an expansionary monetary and fiscal policy to stimulate the economy, which had been in severe recession during the previous two years. Economic recovery was a vital precondition to rebuilding the banking sector.

Importantly, the transition triggered a change in the relationships between the President and the Central Bank. Unlike her predecessor, President Aquino did not intervene directly in Central Bank decisions on banking policy and also supported the Central Bank in its foreign debt policy. After fierce conflict over the key economic issues and frequent reshuffles of her Cabinet, a consensus on liberalisation measures as the key strategy to attract foreign investment and to promote exports emerged in the early 1990s. Faced with a declining economy and continuing political instability, and losing the "special" support of the US government, the government decided to facilitate liberalisation reform to improve the economy in the early 1990s. After the consensus among Monetary Board and Cabinet members had emerged, it was not very difficult for the Central Bank to initiate regulatory reforms, including various deregulation and liberalisation measures to activate the banking sector.

However, the Aquino government was not capable of implementing structural reform in the banking sector through the legislative process, after the Legislature was restored. The legislative process was constrained by the lack of effective procedures and rules necessary to facilitate prompt legislative action. Since there were no legislative elections between 1987 and 1992, legislators did not need to be cooperative with the President in order to secure her support for immediate electoral purposes in the early years. Structural reform was further discouraged by the fierce conflict between the Executive and the Legislature. The Central Bank reform was left to the next administration as an important phase in the task of developing the economy and the banking sector.

Chapter 5.
Banking Sector Reform under the Ramos Government (Part I): The Establishment of the New Central Bank (Bangko Sentral ng Pilipinas)

Introduction

Under the Ramos government, the Philippine economy made an impressive recovery. The banking sector expanded as the economy grew. After the currency crisis of 1997, although the economy faced a downturn, the government was able to manage the macro economic shocks relatively well. After the currency crisis, the banking sector showed relative stability, although the vulnerability of one state bank, namely the PNB, was revealed. The various efforts to reform the economy helped to moderate the economic shocks. The economic strategy based on liberalisation and the enhancement of the regulatory power necessary to expand exports and attract foreign investments had been initiated by the Aquino government. Under the Ramos government, liberalisation was consolidated with broad support as a major policy thrust. The establishment of a more independent Central Bank enhanced the regulatory power of the monetary authority and led to relative monetary stability. The Ramos government became the first administration to implement key structural reforms in the banking sector through the legislative process. The establishment of the New Central Bank, the Bangko Sentral ng Pilipinas, and the entry of new foreign banks had been critical reforms for the development of the banking sector since the Central Bank was established in 1949. They were landmark laws which reflected the successful promotion of the key principles of banking reform since 1986: the liberalisation of the banking sector and the enhancement of the Central Bank's regulatory power.

This chapter and the following chapter examine the key structural reforms, the establishment of the New Central Bank and the entry of new foreign banks respectively, and seek to address a key question: how was the Ramos government able to implement these critical reforms which contributed to the improvement of the economy and the banking sector?

The Central Bank has long been a key regulatory authority of the Philippine economy. The Central Bank has drafted monetary policy, influenced the foreign exchange rate, regulated the banking sector and protected financial stability. The Central Bank has been playing a critical role in the control of the growth of the economy for many decades. The state has not behaved entirely as a unitary actor in the economy. Yet, the case of the Central Bank remains relevant to the study of the development of the state apparatus as a regulatory authority.

The establishment of the new Central Bank was seen as "the most fundamental structural reform" in the financial system (Singson,1994:2). The Central Bank was financially restructured and improved its capability to manage the macro economy. The New Central Bank was established as a more independent body to pursue the primary objective of price stability. The Central Bank also enhanced its regulatory power as a monetary authority over other banks.

International factors including support (or pressures) from the US government, the IMF, the World Bank and other donor countries were influential in promoting (or impeding) economic reforms. Economic reform should thus be examined in the context of changing international factors. In particular, the Ramos era was a period of critical changes in the international arena. With the end of Cold War, US security interests in developing countries changed.[1] In the Philippine context, the US military bases, which had been the foundation for the special relationship between the Philippines and the US, no longer existed.[2] The Philippine government lost the generous support it had received from the US government as a consequence of the special relationship. The event became a catalyst, moving the economy in a new direction and facilitating further the process of liberal reform which had been initiated under the Aquino government. The Ramos government, which faced the loss of "special" support from the US government, promoted liberalisation and Central Bank reform to attract foreign investment and loans.

[1] Needless to say, US security interests have changed significantly since the events of September 11.

[2] For the argument which stresses this dimension as a cause of the Ramos reform, see, for example, Hutchcroft (1998:244-245).

Yet these changes in the international environment should not be seen as the sole factor underlying the push towards structural reforms in the economy and banking sector. The Ramos government was committed to the reforms for reasons relating to its own political and economic agenda, which was formulated in the political and economic conditions of the Philippines. As noted in the previous chapter, the importance of Central Bank reform had been recognised since the mid-1980s, after the role of the Central Bank, in maintaining monetary stability and in regulating banks, was severely undermined under the Marcos government. However, despite strong support from the IMF, the World Bank and local businesses including banks, the Aquino government failed to implement this critical reform mainly due to the deadlock between the Executive and the Legislature, in particular the Senate.

In the following section, the problems of the Central Bank and the proposals leading to the Central Bank reform are first examined. Then, the legislative process involved in the establishment of the New Central Bank is analysed. In the final section, various factors centring on changing political institutions and the interactions among policy elites are examined to explain the successful implementation of the Central Bank reform. In brief, the successful central bank reform under the Ramos government was contingent on a new constellation of political institutions emerging as a consequence of the establishment of the 1987 Constitution. This new constellation strengthened the interests and capacities of the President, the centre of the government, and weakened the potential for resistance among legislators.

The Establishment of the New Central Bank

The establishment of the New Central Bank (or Central Monetary Authority: CMA) was one of most important reforms in the Philippine banking sector. This was the first key structural reform of the regulatory authority which included amendments to the law under constitutional democracy in the Philippines since the Central Bank Act was passed in 1948. This reform had two key objectives: the establishment of an independent monetary authority and the financial restructuring of the Central Bank.

The definition and measurement of Central Bank independence is still a contentious issue.[3] The Central Bank cannot be entirely independent from the government and there are close links between fiscal and monetary policy. However, the independence of the Central Bank can be a useful concept in examining the development of the regulatory authority. Central Bank independence can be defined in a variety ways, depending on the type of central bank operation (see Maxfield,1997:6). They can be divided into two main categories: the extent of independence from government and independence from regulated banks. The former directly affects the central bank's ability to control the money supply. The latter influences the effective regulation and supervision of the financial sector. It must be noted that, in Philippine banking history, the Central Bank's independence from the government has had a significant impact on the independence from regulated banks, particularly until the mid-1980s, since the state banks have had a large presence in the banking sector. In addition, the owners and management of private commercial banks often try to use close connections with the government, the President in particular, to obtain personal favours.

The independence of the Central Bank cannot be secured by legislation alone. As seen in the previous chapters, the transition from Marcos to Aquino helped to secure the Central Bank's independence, since the new President, unlike President Marcos, did not intervene directly in the Central Bank's decisions. The reduction in direct credit allocation through the Central Bank also helped to protect the Central Bank from political interference. Yet, the legislation provides the basic rules needed to define the Central Bank's regulatory powers and the relationship between the Central Bank and the government. In the Philippines, the legislation that created the new Central Bank was a critical step forward in the enhancement of the regulatory power of the Central Bank and its independence vis-à-vis the government and regulated banks.

In the Philippines, the importance of an independent monetary authority had been recognised after the drastic failures of fiscal and monetary policy under the late Marcos administration. Faced with economic crisis, the Central Bank was not able to maintain

[3] For this controversy, see Maxfield (1997); Fry, Goodhart and Almedia (1996); and Cukierman (1992).

monetary and banking stability. The monetary and fiscal expansion fuelled high inflation. The implementation of economic stabilisation measures were repeatedly postponed by the President's intervention, due to the legislative elections in 1984. The Central Bank had essentially served the President's interests under the dictatorship. As a result of this experience, the 1987 Constitution clearly stated that the "Congress shall establish an independent monetary authority" (Section 20, Article XII). Since the Fernandez era (1984-1990) recommendations had been made urging the Central Bank to strengthen its regulatory power through the establishment of an independent monetary authority. Key reform measures included: (1) Monetary Board reforms (more representatives from the private sector on the Monetary Board); (2) enhancement of supervision of banks; (3) improvements in the regulation of emergency loans, receiverships and liquidations; (4) legal protection for Central Bank officials; (5) higher penalties against illegalities; (6) prevention of irresponsible DOSRI loans; and (7) prohibition against development financing.

With respect to the independence of the Central Bank, the termination of development finance and Monetary Board reform were important measures. The Central Bank cannot be entirely independent from the government. However, the termination of the development finance helped the Bank to maintain a distance from political affairs. Under the new legislation, the Central Bank's function as the government's fiscal agency was more strictly limited than before. The majority representation of non-Cabinet members on a full-time basis also had advantages. The changes of Cabinet members, which were often caused by various political conflicts, would not affect the membership of the Monetary Board. Thus the Monetary Board could maintain a greater distance from political conflicts. Due to their full-time membership, the Monetary Board members could play a more important role in conducting and supervising the Central Bank's operations.

In the previous Congress, a bill to create an independent monetary authority was discussed both in the House and the Senate. The House succeeded in drafting a final bill for the Bicameral Conference Committee. However, the Committee did not meet since the Senate would not finalise their bill by the end of the Eighth Congress. The

IMF and the World Bank consistently supported the Central Bank's position through their lending activities. The establishment of the independent monetary authority was one of the conditions for the second tranche of the World Bank's Financial Sector Adjustment Loan, which was agreed in May 1989. Since the Aquino government failed to establish independent monetary authority, the release of the second tranche was repeatedly postponed.

The problem of the losses of the Central Bank was also an old problem and the World Bank's report of 1986 expressed concern over this problem.[4] The problem had been a matter of concern between the Central Bank and the World Bank and the IMF during the Aquino era. They discussed a plan to transfer part of the losses to the national government and the Senate Committee had a public hearing on this matter in May 1990.[5] However, the Central Bank underestimated the potential risks of the problem. According to governor Cuisia, they started to discuss this matter seriously among Monetary Board members from August 1991 and it was only in 1992 that the Central Bank submitted its proposal to the Monetary Board.[6]

As seen in the previous chapter, under the Aquino government the Central Bank formulated monetary policy and regulated the banking sector more autonomously since, unlike the Marcos government, the Aquino government did not directly intervene in Central Bank operations. The Aquino government fully supported the Central Bank's position on the foreign debt repayment issue, which had been highly controversial. However, structural reforms were not implemented under the Aquino government in spite of the Central Bank's advocacy and the support of the IMF and the World Bank. The lack of strong initiatives from the President, the fierce conflict between the President and the legislative leaders and the inefficiency of the newly restored Legislature caused a significant delay to the reform.

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[4] See The Manila Chronicle, 15 September 1986, "CB deficits mount due to 'Jobo' bills".

[5] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 16th May 1990.

[6] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, pp.46-47.

After Ramos took power, the new government swiftly moved to implement this critical reform. The Ramos government took the bold initiative of reforming the banking sector and tried hard to cooperate with the legislature to enact key legislation. The Central Bank was also very keen to advocate reform, as the problem of the Central Bank's accumulating losses grew worse. Facing economic downturn and high inflation rates, the Central Bank emphasised the importance of the establishment of an independent monetary authority as a first priority after the foreign debt problems became a less serious matter for the economy. The Central Bank formulated its own draft bill to establish the New Central Bank and presented the bill to the President and to the Legislature, both the Senate and the House of Representatives. The Central Bank's proposal was backed by the government and was influential in the drafting of bills in the House and the Senate. In order to gain a better understanding of this extraordinary event, the "bankruptcy" of the Central Bank and its restructuring, the causes of the huge losses and the proposal to restructure the Central Bank are analysed in the following section.

The Central Bank Proposal

Due to a series of discussions in the previous Congress and a statement in the 1987 Constitution, there had been a broad consensus on the importance of the creation of an independent monetary authority. However, the financial restructuring of the Central Bank was a very controversial issue, due to the potential losses of public funds. The Central Bank claimed that its losses stemmed largely from economic policy during the economic crisis between 1983 and 1985 under the Marcos government. The main causes of the losses were: (1) the foreign exchange loss caused by the devaluation of the peso; (2) the costs incurred by rescue operations to banks and financial institutions; (3) the various forms of subsidies to the National Government; and (4) interest

payments for high-yielding Central Bank Bills.[7]

The Congressional Planning and Budget Office, which is the research body of the House, investigated the causes of the Central Bank losses.[8] The most detailed CPBO report on the Central Bank losses divided the losses into four categories: losses on forward exchange cover (P51.6 billion); servicing CB foreign liabilities (P77 billion); concessional loans to exporters and other priority sectors and losses on monetary operations including Central Bank bills (P101 billion) and opportunity losses such as "losses" due to CB's holding low yielding National Government Securities (P105 billion).[9]

The Central Bank's ability to control the money supply and to curb inflation began to be impaired in the 1970s as the country's current account tilted towards a deficit. At the end of the 1970s, the current account deficit was accumulating as the country's import expenses exceeded foreign currency gained from exports, grants and other sources. As the imbalance worsened, the Central Bank had to face the problem of an increase in the prices of essential goods and a decrease in the Bank's foreign exchange reserves. In addition, at that time, the economy faced oil price hikes and a decrease in the price of export commodities. To address these problems, the Central Bank undertook forward cover and swap arrangements. In effect, the Central Bank took risks of foreign exchange loss through these operations.

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[7] For the Central Bank's explanation, see The Central Bank, Script For A Computer Presentation on Video Tape (Audio Video): "Toward An Independent Central Monetary Authority" presented at Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992 and House Joint Committee of Committee on Banks and Financial Intermediaries and Committee on Economic Affairs, 23 November 1992, hereafter referred to as the Central Bank, Video Script; House Committee on Economic Affairs, "Understanding and Addressing the Huge CB Deficit" prepared for a joint committee: Committee on Banks and Financial Institutions and Committee on Economic Affairs; and Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992.

[8] See Congressional Planning and Budget Office (CPBO), "Central Bank Losses and the Proposed Central Monetary Authority", submitted to the House Committee on Banks and Financial Intermediaries, on 11 March 1993.

[9] See Table 5-1 "CB Loss / Special Accounts".

Through forward cover operations the Central Bank enabled the prices of oil, grains and other essential commodities to remain stable by providing fixed rate foreign exchange to importers of these products.[10] In effect, the Central Bank subsidised the prices of these goods by assuming the foreign exchange risk. According to the Central Bank, losses on forward exchange cover amounted to P51.6 billion including cover for local oil companies (P 41.9 billion), cover for the National Food Authority (P 7.6 billion) and cover for the National Steel Corp. (P 2.1 billion).[11] Swap contracts were basically a measure to shore up the Central Bank's dollar reserves. On the swap contracts, received foreign exchange from banks was replaced by pesos at the prevailing exchange rate.[12] At an agreed future date, the Central Bank was supposed to give back the foreign exchange to banks at a predetermined rate. In this operation, the Central Bank blocked the peso deposits to keep inflation manageable by limiting the supply of pesos in circulation. The Central Bank paid interest on the blocked pesos while they were not delivering.[13]

In 1983, the importance of forward cover and swap arrangements intensified under the foreign debt crisis. After the assassination of Benigno Aquino, Jr., political instability fuelled capital flight and further slimmed the country's foreign credit line. The peso was devalued a second time in that year. In October, the government declared a moratorium on the payment of principal on foreign commercial bank debts. Because of the lack of dollars, public and private sector debtors could not pay their foreign obligations as they matured. Under the foreign debt crisis, these debtors were allowed to deposit pesos equivalent to their amortisation of reschedulable loans at prevailing exchange rates in the Central Bank.[14] In effect, the Bank assumed the payment of interest and the foreign exchange risk on the portion of liabilities covered by the peso deposits. In this operation, the Central Bank also blocked the peso deposits to keep inflation manageable by limiting the supply of pesos in circulation. Because of this peso blocking, the

[10] See the Central Bank, Video Script, p.2.

[11] See Table 5-1 "CB Loss / Special Accounts".

[12] See the Central Bank, Video Script, p.2.

[13] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.34.

[14] See the Central Bank, Video Script, p.2.

Central Bank lost opportunities to gain interest income. Losses on these foreign loans due to the peso devaluation amounted to P77 billion.

Second, the massive rescue operations to financial institutions during the economic crisis also caused huge losses.[15] The Central Bank provided massive funds to distressed financial institutions in various ways to restore public confidence in the financial system under the Marcos government. The Central Bank noted that most of the funds advanced to those banks remain outstanding to this day, although the CB did not specify the amounts of rescue funds and recipient banks.

Third, the losses of the Central Bank were aggravated by the Marcos government's heavy reliance on the monetary authority for budgetary support. The Central Bank granted loans at preferential rates: (1) to finance massive public sector spending in the 1970s; (2) to prop up agriculture and exports; and (3) to help rehabilitate distressed industries and government corporations.[16] As a result, the Central Bank had to carry various low-yielding government securities in its portfolio. For example, the Central Bank purchased 2 and 4 per cent bonds for public works (PW & ED bonds) while the CB bill's interest was between 20 - 40 per cent during the crisis years, 1983 to 1985.[17] In addition, the Central Bank claimed that many hidden subsidies had been provided to the national government. For instance, the Central Bank provided the national government with P6 billion as interest-free subscription loans. This loan was a payment of the quota for membership of the IMF which had recently increased.[18]

Fourth, these quasi-fiscal lending operations and emergency rescue operations led to monetary expansion which forced the Central Bank to "mop up" at great cost. The "Jobo Bill", which was issued in 1984, yielded more than 40 per cent interest to curb

[15] See the Central Bank, Video Script, p.3.

[16] See the Central Bank, Video Script, p.3.

[17] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.16.

[18] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.45.

the extremely high inflation.[19] These high-yielding debt instruments necessitated large interest payments which in turn led to renewed monetary expansion. Thus, "the Central Bank finds itself in a vicious cycle where it continuously incurs costs to mop up the liquidity created by interest expenses that go with mopping up operations".[20]

The losses which were caused by emergency loans, concessional loans and other monetary operations amounted to P101 billion.[21] In addition, according to the Central Bank, other "losses" due to the CB holding low-yielding National Government Securities came to P105 billion.

These Central Bank losses were recorded in three special accounts as "assets" on its balance sheet. The three special accounts included the Monetary Adjustment Account (MAA), the Exchange Stabilisation Adjustment Account (ESAA), and the Revaluation of International Reserve Accounts (RIR).[22] Extraordinary expenses placed in the MAA, ESAA and RIR rose from P11.8 billion at the end of 1982 to P302.5 billion by the end of 1991 (MAA: P48.5 billion, ESAA:P87.8 billion and RIR: P166.3 billion). Since the early 1980s, the Central Bank had continued to amortise the MAA and ESAA accounts.[23] From 1982 to 1991, this amortisation had reached a total of P38.2 billion. As the Bank's net profits improved, amortisation increased significantly. In the three years proceeding the inauguration of Ramos as President, the total amortisation reached P23.5 billion: P2.7 billion in 1989, P10.2 billion in 1990 and P10.6 billion in 1991. The sharp increase in the amortisation was largely caused by a debt buyback package, with foreign creditors help, to reduce its interest payments in 1990 and 1991. The remaining foreign obligations were to be converted into longer-term bonds with relatively low interest rates.[24]

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[19] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.15.

[20] See the Central Bank, Video Script, p.4.

[21] See Table 5-1 "CB Loss / Special Accounts".

[22] For the functions and accumulations of these three accounts, see Appendix 5-1 at the end of this chapter.

[23] See the Central Bank, Video Script, p.7.

[24] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.88.

Apart from the debt buyback package, the Central Bank claimed that it had been taking various measures to minimise potential losses including: the transformation of the major credit programmes to government financial institutions; improvements in policy to support weak banks; the abolition of forward cover contracts for oil and other imports; and administrative cost reductions including organisational reforms.[25]

The Central Bank argued that although these efforts were helpful, they were not enough to lower its extraordinary expenses to a level where it could conduct its monetary management functions normally.[26] Since further debt reduction through negotiations with foreign creditors could not be expected, further accumulation of losses led to higher inflation.[27] Thus, legislative action to eliminate the deficits was urgent.

The Central Bank stressed the following merits of the creation of the New Central Bank. First of all, a financial restructuring would improve the macroeconomic condition through lower reserve requirements, lower intermediation costs and a reduction in interest rates.[28] The Central Bank's extraordinary expenses would continue to exert tremendous expansionary pressure on the money supply, which would have to be mopped up through an increase in reserve requirements and open market operations. Reducing this expansionary pressure would lead to lower reserve requirements and lower intermediation costs, which in future would help to reduce interest rates and inflation. These improvements in macroeconomic conditions would encourage more investment and thereby create jobs for more Filipinos.

Second, the creation of an independent monetary authority was essential to prevent the recurrence of the financial disasters of previous decades. Since the New Central Bank could concentrate on monetary functions due to the termination of quasi-fiscal

[25] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, pp.21-24.

[26] See The Central Bank, Video Script, p.8.

[27] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.56.

[28] See House Committee on Economic Affairs, "Understanding and Addressing the Huge CB Deficit".

functions, it would become more transparent.[29] The New Central Bank would have to bear the cost only of its monetary management. The establishment of an independent monetary authority would also enhance the regulatory power of the existing Central Bank and improve various regulations to develop a stable financial sector.

Third, the creation of an independent monetary authority and financial restructuring would improve the fiscal operations of the national government. Due to the end of quasi-fiscal operations, the national government would no longer have to complicate its operations by supporting the open market operations of the Central Bank. In the early 1990s, treasury bills were issued by the government as a part of open market operations and money was deposited in a Central Bank account. The national government deposits with the Central Bank amounted to P56 billion out of the outstanding P177.8 billion T-Bills in January 1991.[30] By reducing interest rates through financial restructuring, the national government could reduce interest payments on its domestic debt.

Fourth, the Central Bank insisted that the restructuring of the Central Bank's financial position did not necessarily require an immediate cash outflow from the National Government, although the proposed New Central Bank bill sought to provide the independent monetary authority with paid-in capital of P10 billion. In the initial proposal of the Central Bank, the subscription of interest-bearing securities for the Central Bank was suggested as one way of injecting fresh capital.[31] Even without a fresh capital injection, the New Central Bank could keep the initial P10 billion net worth by transferring P10 billion more assets than liabilities from the existing Central Bank.[32]

Fifth, the Central Bank stressed the vital importance of the New Central Bank bill, arguing that, if the bill were not passed, the Philippines would lose an opportunity to receive $450 million of concessional loans in the second tranche of the Financial Sector

[29] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.48.

[30] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 17 January 1991, p.66.

[31] See The Central Bank, Video Script, p.8.

[32] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.58.

Adjustment Loans from the World Bank. In fact, the condition for the second tranche was the establishment of an independent monetary authority. The government could have received the second tranche without the financial restructuring of the Central Bank. The Central Bank was desperate to establish an independent monetary authority to secure the World Bank loan, but the Central Bank governor, Jose Cuisia, Jr. also mentioned a $1.4 billion loan from the IMF over five years, which would be secured if the government could restructure the financial losses of the Central Bank.[33]

The Central Bank's explanation for the causes of the losses inevitably left some unanswered questions. The Central Bank could not clearly explain the exact amount of losses and beneficiaries from each operation, such as losses from foreign exchange operations, emergency loans, concessional loans and the high costs of CB bills. The total losses in the three special accounts were only approximately identical to the gross losses caused by the above cited operations, although governor Cuisia claimed that there were no behest loans among the P308 billion losses.[34] He categorically denied the existence of the suspected behest loans in expenses of the foreign liabilities which recorded in the Exchange Stabilisation Adjustment Account (P87.8 billion). Cuisia explained that the Central Bank had absorbed the foreign liabilities of private borrowers during the debt crisis. They were not behest loans, because these private borrowers paid on the basis of contracts. The private borrowers delivered the pesos to the Central Bank and received foreign exchange promissory notes, since the Central Bank could not provide dollars. In terms of foreign liabilities, the Central Bank submitted to the data on private sector foreign loans assumed by the Central Bank.[35] However, the governor did not explain clearly which losses were caused by emergency loans and which by concessional loans under the Marcos government. In fact, Cuisia himself later admitted that there was a lack of transparency with regard to the emergency loans under the Marcos government, particularly in the case of the P3 billion advanced to the Banco

[33] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.45.

[34] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.28.

[35] See Letter from Jose L. Cuisia, Jr. (Governor of the Central Bank) to Jose Carlos V. Lacson (Congressman and Chairman, House Committee on Banks and Financial Institutions), 14 October 1992.

Filipino.[36]

Although the ambiguity surrounding the Central Bank losses stemmed, at least in part, from a technical difficulty of account management, this ambiguity was severely criticised by the opposition as an example of the secrecy of the Central Bank and the defects of monetary and regulatory policy. In fact, the Central Bank underestimated the negative impact of the losses on monetary stability. In addition, the suspected pressures from international financial institutions in support of the reforms were criticised by the opposition.

However, through numerous hearings and meetings, the Central Bank was largely successful in convincing the Executive and the legislative leaders of the merits of their claims on this issue. The huge losses of the Central Bank were caused principally by foreign currency losses, emergency rescue operations and the high costs of open market operations. There was no alternative policy to curb inflation and to prevent further deterioration of the national economy during the first half of the 1980s. They aimed to stabilise macroeconomic conditions. Thus, the entire economy and the Filipino people as a whole were beneficiaries. The National Government, it was argued, should pay these costs, at least in part, because some of the losses were caused by quasi-fiscal operations including subsidies paid to stabilise key import prices. To prevent the recurrence of the losses which caused monetary instability, it was urgently necessary to establish an independent monetary authority and to undertake a financial restructuring of the Central Bank. Financial restructuring was essential to curb inflation and interest rates, which would benefit the national economy. The restoration of monetary stability would attract more foreign investment. Furthermore, the financial restructuring could be achieved at low cost, since the completion of these reforms would help to secure concessional loans from the IMF and the World Bank.

[36] See PDI, 21 October 1998, "Cuisia hits BSP grant of emergency loans".

Drafting House Bill No. 7037

The House was responsive to the drafting of the bill to establish the New Central Bank, since the bill had already been approved on its third reading in the previous Congress under the Aquino government. The first draft of House Bill No. 296, "An Act Amending R.A. 256 to Establish a Central Monetary Authority", was identical to the previous bill. The bill included the key provisions to establish an independent monetary authority and was fully supported by the Central Bank, although the bill did not contain provisions to deal with the Central Bank's losses.[37]

This time the bill was supported by, and discussed in, the Joint Committee of the Committee on Banks and Financial Institutions, chaired by Jose Carlos V. Lacson (Lakas-NUCD, Third District, Negros Occidental) and the Committee on Economic Affairs, chaired by Felicito C. Payumo (LP, First District, Bataan). There were some strong supporters of this bill among the members of minority parties. Margarito Teves (LDP, Third District, Negros Oriental) was one of the main authors, although many LDP members were opposed to this bill. Exequiel B. Javier (Lakas-NUCD, Lone District, Antique) also became a sponsor. He was a former chairman of the Committee on Banks and Financial Institutions and a main author of the previous bill, which aimed to establish an independent monetary authority under the previous Congress. Under the Ninth Congress he was chairman of the powerful Ways and Means Committee.

The first joint committee meeting was held on 8th October 1992. The bill had been discussed extensively in late 1992 and early 1993. With regard to the provisions to establish an independent monetary authority, it was not so difficult to reach a consensus among committee members. However, the issue of the financial restructuring of the Central Bank was controversial, although Ramos's coalition constituted a majority. Some congressmen and congresswomen were particularly sceptical about the Central Bank's proposal to transfer the losses to the national government. Among them Joker P. Arroyo (Independent, Lone District, Makati), the former Executive Secretary and the

[37] Letter from Jose L. Cuisia, Jr. (Governor of the Central Bank) to Jose Carlos V. Lacson (Congressman and Chairman, House Committee on Banks and Financial Institutions) on 6th October 1992.

Chairman of the Philippine National Bank under the first Aquino Cabinet, was very hostile to the Central Bank. In the first joint meeting, Arroyo strongly criticised Edgardo Zialcita, Deputy Governor of the Central Bank due to the lack of clarity in his explanation of the amount of the losses.[38]

In addition, the suspected intervention from the IMF and the World Bank on economic policy was criticised by members of the opposition. Some members of the Committee, including Bonifacio H. Gillego, a leader of the "progressive bloc", (Lakas-NUCD, Second District, Sorsogon) and Salvador H. Escudero III (NPC, First District, Sorsogon) were suspicious with regard to the close connections between the Central Bank and the international financial institutions, including the ADB, IMF and World Bank. They requested that the Central Bank submit a list of CB officials who had worked previously (or after their retirement from the Central Bank) for these institutions.[39] Faced with the complicated issues of financial restructuring, the Committee chairs were sceptical about finalising the bill in a short time. The chairs suggested to the Central Bank governor Cuisia that there might not be enough time to draft and pass a final bill to restructure the Central Bank's losses.[40]

Through intensive work, the bill was passed quickly in spite of initial fears of delays in the legislative process. Central Bank officials were frequently invited to join in discussions. There were many public hearings with leading economists from the country's leading research institutes, including the Asian Institute of Management (AIM), Centre for Research and Communication (CRC), the Philippine Institute for Development Studies (PIDS), and the School of Economics, University of the

[38] See Committee Records: A Joint Committee; Committee on Banks and Financial Institutions and Committee on Economic Affairs, 8 October 1992, pp.70-71.

[39] See Committee Records and Minutes: the Joint Meeting of Committee on Banks and Financial Intermediaries and the Committee on Economic Affairs, 23 November 1992.

[40] See Committee Records, Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.82.

Philippines.[41] The Bankers Association of the Philippines (BAP) also submitted a position paper as a contribution to the discussion.[42]

Legislative leaders including House Speaker, Jose de Venecia, Jr. (Lakas-NUCD, Fourth District, Pangasinan) and House Majority Leader, Ronaldo B. Zamora (Lakas-NUCD, Lone District, San Juan/Mandaluyong) were keen to enact the bill. To facilitate the passage of the bill, the Speaker, Jose de Venecia, formed a Task Force composed of the sponsors, authors, Majority leaders, and members from the Minority. The Congressional Planning and Budget Office (CPBO), the research body of the House of Representative, and the staff of a number of Committees played important roles by providing technical support. This was in sharp contrast to the very slow legislative process under the previous Congress. After the intensive work by the committees and the task force, the Committee Report (Report No. 00068) was submitted for a Second Reading on 3 February 1993.

During the floor discussion, questions from the opposition caused some delay. According to Congressional rules, all members of the House are entitled to ask an unlimited number of questions about a bill in floor discussion. There were some resilient opponents, including Rep. Joker Arroyo. Rep. Arroyo was opposed to the final bill and expressed his hostility against the Central Bank in a speech explaining his vote. "The Central Bank is the most dishonest and irresponsible government entity we ever had. It has contributed immensely to the country's financial ruin. How else could Mr. Marcos and his cronies have hoarded their dollars abroad without the Central Bank's

[41] Major contributors included as follows: Prof. Victor S. Limlingan "The Central Monetary Authority: A Clear Mandate, Not a Clean Slate" (Testimony before the House Committee on Banks and Currencies on the Proposed Central Monetary Authority) 7th December 1992; Dr. Mario B. Lamberte, Vice-President, Philippine Institute for Development Studies, "Comments on House Bill No. 296: An Act Amending RA No.265"; Dr. Maria Socorro Gochoco-Bautista, Associate Professor, School of Economics, University of the Philippines "Comments on House Bill No. 296 An Act Amending R.A. No. 265 to Establish A Central Monetary Authority"; and Dr. Benjamin E. Diokno, Professor, School of Economics, University of the Philippines, "Comments on CMA Bill and Restructuring of the CB losses".

[42] See Bankers Association of the Philippines, "Position Paper of the Bankers Association of the Philippines on the House Bill Entitled An Act Amending RA 256, As Amended to Establish a Central Monetary Authority".

assistance over the years?"[43] Despite some opposition, support for the bill was consolidated. The pro-Ramos coalition, led by Lakas-NUCD, controlled a majority in the House. Since there was no strong opposition outside the House, the members of the majority had no strong reasons to oppose the bill. The Bankers Association of the Philippines expressed their support for the enhancement of the regulatory power of the Central Bank and the restructuring the Central Bank's losses, since these reforms would improve macro-economic conditions and lead to lower reserve requirements, which would be favourable for the banking sector. Philippine industry was also sympathetic, since the reform was expected to lower interest rates, which would be beneficial for industry. The House approved a third reading of the bill with 149 votes in favour, 15 votes against and 1 abstention on 31 May 1993.[44]

Drafting Senate Bill No. 1235

The legislative process in the Senate was slower than in the House. When the Committee on Banks, Financial Institutions and Currencies, chaired by newly-elected Senator Raul Roco, was held in late 1992, four bills were proposed to establish an independent central monetary authority (CMA).[45] In fact, when the Central Bank governor was first invited to explain the Central Bank's proposal for the Committee Meeting on 3 December 1992, governor Cuisia suggested the possibility of separating the matter of the financial restructuring from the establishment of an independent monetary authority, since the former seemed to be more difficult for the House and the Senate to agree on. The Central Bank was desperate to obtain the second tranche of the Financial Sector Adjustment Loan (the World Bank's $450 million concessional loan) which the country would receive if Congress passed the bill to establish an independent monetary authority.[46] The financial restructuring of the Central Bank did not include the conditionality for the second tranche.

[43] Record of House of Representatives, 31 May 1993, p.16.

[44] See Record of House of Representative, 31 May 1993, p.21.

[45] The four bills were : (1) S.B. No. 844 authored by Sen. N. Gonzales; (2) S.B. No.23 authored by Sen. A. Romulo, the former chairman of the Committee for the last Congress; (3) S.B. No. 945 authored by Sen. T. Guingona; (4) S.B. No. 867 authored by Sen. J. Osmeña.

[46] Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 3 December 1992, p.94.

Between December 1992 and February 1993, the intensive work done by the Senate Committee to formulate the bill was remarkable. According to Senator Roco, there were numerous meetings and most of them were informal. By the end of February, the Senate Bill, which aimed to establish an independent monetary authority and to restructure the losses of the Central Bank, was largely consolidated except with regard to the management of the losses after clearance of the balance sheet of the Central Bank. Dr. Benjamin E. Diokno commented on the Senate Bill as of February 1993 that "I find the consolidated bill prepared by the Senate Committee on Banks, Financial Institutions and Currencies a remarkable improvement over the various related bills that I have seen before", although he recognised some problems, he added "I believe it comes close to what is an ideal CMA bill".[47]

After massive work by the Committee, the bill was scrutinised by senators during the second reading. The bill was extensively discussed between 19 May and 7 June 1993. Leading critics of the bill included Sen. Arturo M. Tolentino, Sen. Ernesto M. Maceda and Sen. Wigberto E. Tañada. The main reason for their opposition was similar to that underlying the opposition to the bill in the House, i.e. the urgent enactment was forced on Congress by international financial institutions; the causes of the losses, the beneficiaries, and the identities of those responsible for the actions of the Central Bank were not properly explained; and the provisions to prevent recurrence were not persuasive.

Sen. Maceda, a vocal critic of the Ramos government, argued that "this bill is another in a long series of Executive Department actions and/or recommendations that is, in effect, an acceptance of the interference of a foreign body into our internal affairs. And so, the $US 450 million has been dangled to us since last December yet, or what I call '450 pieces of silver' which we seem to need out of a state of mere panic. Thus, we have been

[47] See Benjamin E. Diokno, Professor of Economics, School of Economics, University of the Philippines, "Comments on the Bill Creating the Central Monetary Authority (Senate Version -- as of 23 February 1993)".

rushed into approving this measure."[48]

Sen. Tañada articulated the problem of the lack of clarity in the Central Bank's explanations of issues relating to the financial restructuring. Before he would agree to vote for the creation of a new Central Bank, he demanded the resolution of the following issues: (1) "How did the Central Bank incur losses and liabilities amounting to P307.5 billion as of November 1992? How did these losses and liabilities increase by P 9.1 billion as of December 1992?" (2) "What steps should be undertaken to prevent the continuous increase in Central Bank losses and liabilities?" (3) "What specific provisions should be provided in the Charter of the New Central Bank to minimise possible losses and liabilities it may suffer, considering past experiences and projected future considerations?" (4) "Who shall absorb the CB losses and liabilities, and how shall they be paid?" and (5) "How shall the liabilities equivalent to the 'ampaw' assets represented by the three accounts now be paid and who should pay for them?"[49]

During the second reading, Tolentino consistently opposed the provision for the transfer of the Central Bank's assets and liabilities. He proposed that the bill should be geared to establishing an independent monetary authority and the provision relating to the financial restructuring of the Central Bank should be deleted. After Tolentino's amendment was rejected by Committee chairman Roco, he demanded a vote on his proposed amendment. As a result, the vote was lost but another six senators agreed with Tolentino.[50] In spite of this resilient opposition, particularly to financial restructuring, the pro-Ramos allies consolidated support for the bill. The President certified the necessity of the immediate enactment of the bill on 2 June. Due to this certification, immediately after the vote for the second reading on 5 June, the bill was approved for a third reading on 7 June 1993.

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[48] See the Senate Records: Bill on Second Reading, "S. No 1235 -- The New Central Bank Act", 7 June 1993.

[49] See the Senate Records: Bill on Second Reading, "S. No 1235 -- The New Central Bank Act", 7 June 1993.

[50] See the Senate Records: Bill on Second Reading, "S. No 1235 -- The New Central Bank Act", 5 June 1993.

The Bicameral Conference Committee

After both the House bill and the Senate bill were consolidated, there were important tasks still left for the Bicameral Conference Committee.[51] There were 16 provisions in the House bill which differed from those in the Senate Bill.[52] However, after many formal and informal meetings and various public hearings with same experts including the Central Bank officials, there emerged a basic consensus among legislative leaders in the House and Senate. As House Chair of the panel, Rep. Ronaldo Zamora claimed that House members and Senate members worked together like a working group, rather than a negotiation panel, to form a unified bill.

Within three days, after further intensive discussion and hard work, the final bill was passed by the Committee. Overall, a reasonable compromise was achieved. With respect to the establishment of an independent monetary authority, the House version of the provision on the members of the Monetary Board was adopted. On the other hand the Committee adopted the the Senate version of the provision relating to the restructuring of the losses of the Central Bank. Although both bills shared a basic framework for the financial restructuring of the Central Bank, the House version, similar to the Central Bank proposal, recommended the issuance of 25-year bonds by the National Government. The Senate insisted that a special Committee should be formed to examine the financial restructuring further. This committee would determine what assets and liabilities should be transferred to the BSP. Then, the Monetary Board would recommend that Congress waive the Central Bank's liabilities and losses.

Although the final bill differed from the Central Bank's proposal, the bill largely fulfilled the Central Bank's recommendations. Finally, the independent monetary authority which the Central Bank had advocated since the beginning of the Aquino

[51] Conferees on the Part of the Senate: Raul S. Roco, Blas F. Opel, Teofisto T. Guingona, Jr., Wigberto E. Tañada (dissent), Arturo M. Tolentino, Herherson T. Alvarez, Jose D. Lina, Jr. and Agapito A. Aquino. Conferees on the Part of the House of Representatives: Ronaldo B. Zamora, Jose Carlos V. Lacson, Felicito C. Payumo, Exequiel B. Javier, Rolando R. Andaya, Feliciano R. Belmonte, Salvador H. Escudero III, Ricardo C. Silverio, Jaime C. Lopez, Antonio M. Diaz, Edcel C. Lagman (dissent), Margarito B. Teves and Joker P. Arroyo (dissent).

[52] See Table 5-2 "Differences Between House Bill No. 7037 and Senate Bill No.1235".

government was established. The New Central Bank Act included key recommendations by the Central Bank to enhance its regulatory powers and to end its role as provider of development financing. In the final moments, the Central Bank was given another bonus. Central Bank officials from salary grade 20 (Assistant Division Chief) upwards were exempted from salary standardisation law. Although this was originally a provision in the Senate bill and the exemption applied to officials from salary grade 22 (Division Chief level), Rep. Ronaldo Zamora, House Chair of the panel proposed more generous provisions for Central Bank officials in the Conference Committee.[53] The motivation behind the generous offer by Rep. Zamora was unclear but this suggests the success of the Central Bank's advocacy for the vital necessity of attracting talented young personnel in the Bank to legislative leaders both in the House and in the Senate. It also showed how a leading politician could be very influential in the final provision of a law.

The establishment of the New Central Bank was a critical step in developing a stable economy and banking sector. The structural reforms achieved two essential objectives through the creation of an independent monetary authority and financial restructuring. The financial restructuring led to an improved macro economic policy. The Central Bank became more independent vis-à-vis the government and enhanced its regulatory powers vis-à-vis commercial banks. The Monetary Board has a majority of full-time private representatives, rather than part-time Cabinet members. The prime objective of the Central Bank is defined as that of achieving monetary stability and the fiscal functions of the Central Bank have been phased out. The Central Bank's role as provider of development finance has largely ended. These key measures are expected to secure the independence of the Central Bank from political intervention. It must be noted that after their retirement Central Bank officials, particularly deputy governors, become candidates for membership of the Monetary Board, a privilege previously enjoyed only by Central Bank governors.

The reform included various improved provisions to enhance the regulatory power of the Central Bank. First of all, the Monetary Board gained more governing power in

[53] See, Committee Records, Bicameral Conference Discussion on 9 June 1993, p.39.

terms of the Central Bank's operations. The status of Central Bank officials also improved. The Central Bank's officials from salary grade 20 (Assistant Division Chief) were now exempt from salary standardisation law. In terms of salary, there were no longer significant differences between Central Bank officials and commercial bankers except for senior officials. Second, the Central Bank's banking supervision powers were enlarged. It was now empowered to supervise and conduct examinations not only of banking institutions and quasi-banks but also of their subsidiaries and affiliates. The new law also stipulated higher penalties for violation of laws and regulations. Third, the Central Bank's capacity to handle troubled banks was improved. A new provision put a ceiling on emergency loans to troubled banks. The rules on receivership and liquidation were clarified and the role of the PDIC was enlarged. Fourth, the new law provided Central Bank officials with legal protection against suits and legal proceedings. Central Bank officials were not fully exempted from legal action by this legislation, but Central Bank officials including banking examiners were no longer financially liable as a result of suits arising from normal performance of duties. This was an important step in protecting Central Bank officials and in strengthening the Central Bank's regulatory powers, since the vulnerability of Central Bank officials to legal action significantly weakened the regulatory powers of the Central Bank vis-à-vis regulated banks. Fifth, a preventative measure against irresponsible DOSRI loans was enacted. Receivers of DOSRI loans waived their right to protect the secrecy of their deposits in all banks, as provided by Philippine law.

Changing Political Institutions and The Central Bank Reform under The Ramos Government

Due to the enactment of the New Central Bank Act, which had not been passed by the Aquino government, the Ramos government became the first administration to implement key structural reform in the banking sector through the legislative process. In pursuing its legislative agenda, the Ramos government performed well in comparison with the previous governments. Within one year, many critical reforms were implemented through the legislative process. As mentioned above, the World Bank and the IMF provided the government with a generous financial incentive to reform the

Central Bank. Business representatives including bankers were also supportive of the Central Bank reform, since it would improve the business environment by reducing interest rates. However, we must be careful not to overemphasise the importance of such support which already existed in the years of Aquino government, which nevertheless failed to implement the Central Bank reform. The successful implementation of reform by the Ramos government can only be understood in the context of emerging cooperative relationships between the President and the legislative leaders and these relationships were contingent on the new constellation of political institutions established by the 1987 Constitution.

When Ramos came to power, the Philippine economy was faced with serious uncertainties and difficulties, although it had recovered from the ruins of the mid-1980s. In 1990, a series of severe exogenous shocks contributed to depressing economic growth. A drought in early 1990 disrupted agricultural production and an earthquake in July 1990 caused serious damage to the infrastructure. Furthermore, the Gulf war dislocated about 50,000 Filipino overseas workers from Kuwait and Iraq and increased oil import bills. In 1991, economic growth was practically at a standstill (GNP growth was 0.5 per cent) and a high inflation rate was recorded (18.7 per cent). There was a real danger that the economy would be left far behind that of neighbouring countries. Political instability was still a crucial issue for the economy. The last coup attempt in December 1989, which damaged the financial centre of the country, was seen as an important factor impeding foreign financial flows and decelerating economic growth, although there were no coup attempts in 1990 and 1991. Facing these difficulties and uncertainties, the Ramos government launched "Philippines 2000" as a strategic framework to promote the economy to that of a Newly Industrialised Country (NIC) status by the year 2000. "Philippines 2000" was a critical framework for political and economic reforms, although it was not new as an economic strategy.

After Ramos won the 1992 election by a narrow margin, he appointed the Cabinet members of his new administration. Jose L. Cuisia, Jr., the governor of the Central Bank and the Chairman of the Monetary Board retained his post. Those holding key economic portfolios, who were also Monetary Board members were replaced. Ramon

del Rosario, Jr was appointed Secretary of Finance. Before joining the Cabinet, Mr. del Rosario was Chairman of the Board and Chief Executive Officer of Asian Bank Corporation. He had directorships in various companies including finance, construction and agricultural industries, and had once also been Executive Vice-President of San Miguel Corp. Rizalino Navarro, the former head of Sycip, Gorres and Velayo (SGV), became the Secretary of Trade and Industry. The NEDA was headed by Cielito F. Habito, a Harvard trained economist (PhD holder) who was teaching at UP Los Baños. Salvador M. Enriquez, Jr., who had been working for GSIS under the Aquino government, was appointed Budget Secretary.

It must be noted that, although the members of the Monetary Board had changed, due to the formation of the new Cabinet, the basic monetary and regulatory policy of the Central Bank had not altered. In terms of economic policy, there was strong continuity between the Ramos and the Aquino administrations. Since Ramos was endorsed by former President Aquino, he could easily continue the economic policy of the Aquino government. The President's trust in the Central Bank's policy had not changed. With regard to regulatory reform, the liberalisation initiated by the Aquino government was further promoted by the Ramos government. The Central Bank continued to liberalise the foreign exchange policy as planned, although the Central Bank was concerned about the potential loss of support from the new Presidency due to the replacement of the government after the elections (see Zialcita,1994:228). The President's support for the foreign debt policy of the Central Bank was also unchanged. The major policy to improve the financial system had not changed. The Central Bank promoted this goal in conventional ways: deregulation and greater market competition and increases in the size of financial institutions.

The strong constitutional power of the President and the old tactics used by the Presidents to push their legislative agendas must be seen as underlying the successful reform. After the restoration of regular legislative elections, the President's old tactics were more effective than in the Aquino period. Ramos was elected by 23.7 per cent of the vote, the smallest vote ever won by a Philippine President. Faced with a severe economic downturn, improving the economy was crucial if he was to consolidate

support for his government. An ambitious legislative agenda was formulated under the "Philippines 2000". It was obvious that the weak position of the Ramos's Lakas party in Congress was the first obstacle to the agenda. The Ramos's Lakas party was a mere electoral vehicle, whose members had won only 35 out of 200 seats in the House and 2 out of 24 seats in the Senate. In fact, at the beginning of the Ramos Presidency, the President was not very successful at establishing an amicable relationship with the Legislature. Conflicts between Ramos's allies and the opposition emerged over the appointment of a Cabinet member. The appointment of Finance Secretary Ramon del Rosario was rejected by the Commission of Appointments.[54]

Ramos employed the traditional tactics of Philippine Presidents to strengthen his control over the Legislature. He encouraged legislators from opposition parties to join his party by using the promise of patronage. Ramos backed Jose de Venecia for House Speakership, the most powerful position in the House; the promises of influential posts, including positions as Committee chairmen, were effectively used to encourage opposition members to join his allies. As Gutierrez (1994:8) points out, Ronaldo B. Zamora's case was a prominent example of how the tactics worked. Zamora was the former assistant majority floor leader under the Eighth Congress and was a key advisor to Mitra's presidential campaign in 1992. However, despite Mitra's defeat, Zamora became majority floor leader of a predominantly pro-Ramos House. He gained the post by organising a group of representatives to support Jose de Venecia's election for the speakership.

To mobilise further congressional support, Ramos increased the CDF (pork barrel funds) from US$420,000 to US$520,000 per House member and made its application so flexible that it could be used for practically any type of project, including infrastructure, scholarships, medicines, vehicle acquisition or training.[55] Thanks to these tactics, the pro-government party Lakas-National Union of Christian Democrats (NUCD) "rainbow coalition" had 170 members by April 1993, while the initial 86 members of Lakas ng Democratikong Pilipino's (LDP), the single biggest bloc after the

[54] See, for example, Malaya, 2 June 1993, "CA Finance Committee Rejects Del Rosario".

[55] See Miranda (1996:35), cited in Eaton (1998:207).

May 1992 elections, was reduced to 24 representatives in 1994.[56]

In the Senate, where the opposition LDP party held 16 of the 24 seats, Ramos successfully backed the replacement in December 1992 of Senate President Neptali Gonzalez by Edgardo Angara, who was more cooperative with regard to the ambitious legislative agenda (see Eaton, 1998:208). Angara shared the view that there was an urgent need for economic reform if the country was not to be left far behind the other ASEAN countries. In his speeches, Angara often stressed the importance of reform in the struggle to regain the economic glory of the 1960s.[57]

With no strong social forces outside the state to support opposition in Congress, opposition forces which were sceptical about the Central Bank policy, antagonistic towards the IMF and the World Bank and hostile to the Ramos government received little encouragement.

The business community was largely supportive of the establishment of the New Central Bank. The Bankers Association of the Philippines (BAP) largely supported the New Central Bank bill. The BAP stressed the importance of the independent monetary authority in its position paper: "it is our view that a more independent monetary authority is absolutely necessary to achieve broad economic objectives such as price stability, an efficient financial intermediation process as reflected in interest rates, and a strong financial system that supports sustained economic development".[58] The BAP also supported the financial restructuring of the Central Bank, since it was essential for monetary stability. The reduction of reserve requirements resulting from the financial restructuring would be beneficial for their businesses. Yet, the BAP should not be seen as a strong interest group which pushed the reform, since the banking sector had been

[56] By mid-August 1992, the parties had realigned with 87 members for Lakas-NUCD, 45 for Eduardo Cojuangco's Nationalist People's Coalition, and 35 left in the rump LDP. By December 1992, only 30 LDP representatives remained and by July 1993, this decreased to 25. See Business International, Country Report, April 5, 1993, cited in Eaton (1998:207). See also Gutierrez (1994:8).

[57] See, for example, "Opening Statement of Senate President Edgardo J. Angara before the Participants of the Economic Summit held at ang Maynila, Manila Hotel on 20 August 1993".

[58] See Bankers Association of the Philippines, "BAP Views of the Establishment of A Central Monetary Authority (CMA), Submitted for the Senate Committee on 13th January 1993.

profitable despite the high reserve requirements. Although reduction of the reserve requirements would be beneficial for banking businesses, it was not a serious matter for them, since banks could easily transfer the high intermediate costs to their lending rates. The Central Bank would strengthen its regulatory power over banks through the creation of the New Central Bank. The Central Bank would become more powerful vis-à-vis regulated banks. However, the BAP, which was dominated by big banks was in favour of the creation of the New Central Bank which would phase out the Central Bank's role as a provider of development finance and secure the stability of the financial system. The business community expected to benefit from the establishment of the New Central Bank as it brought macroeconomic stability, lower interest rates and increases in the creditworthiness of the country.

The Freedom From Debt Coalition (FDC) was a critical voice of the reform. The FDC was a leading policy-based advocacy group formed to gather together critics of the foreign debt policy of the Aquino government. The FDC was headed by Leonor M. Briones, Professor of the College of Public Administration, University of the Philippines. The FDC was often invited to send a representative to the Senate Committee as a resource person on issues relating to the Central Bank reform. The FDC criticised the Central Bank for the lack of transparency in its operations and for the mismanagement of monetary policy.[59] For example, they urged the abolition of all three special accounts in which the Central Bank's losses had been recorded, while the Central Bank insisted that the Revaluation of International Reserve Accounts (a self adjustment account) should be kept. They strongly advocated transparency in the process of dealing with the Central Bank's losses.[60] Some legislators, including Senator Raul Roco, were sympathetic to their position which emphasised the need for transparency in the Central Bank's operations.[61] However, it must be noted that the FDC

[59] See the Freedom from Debt Coalition, "On the CMA Bill and the Transfer of CB Liabilities", Submitted for the Senate Committee discussion on 13th January 1993.

[60] See Briones, Leonor M. (1993) "Public Interest and the Financial Restructuring of the Central Bank", conference paper presented at the conference on "the Establishment of the Central Monetary Authority and Financial Restructuring" organised by the Philippine Economic Society and the Friedrich Ebert Stiftung, on 5 March 1993 at Makati, Metro Manila.

[61] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 22 March 1992, pp.67.

essentially shared the view that the creation of an independent monetary authority and the financial restructuring of the Central Bank were urgent tasks for the economy.

Another group which influenced economic policy-making consisted of economists in the leading universities and research institutes, including the University of the Philippines, Asian Institute of Management, Ateneo de Manila University, Centre for Research and Communications and Philippine Institute for Development Studies. These organisations had been actively involved in the legislative process as advisors. They were also critical of the secrecy and mismanagement at the Central Bank. For example, Professor Benjamin E. Diokno noted that although the losses of the Central Bank were caused by the National Government's intervention in monetary affairs, the mistakes of Central Bank officials in the conduct of monetary and foreign exchange policy were undeniable.[62] However, although there were different opinions on the detailed provisions, there was broad agreement on the urgent need for the creation of the New Central Bank to stabilise macro-economic conditions.

Due to the new legislation, there were some potential losers, including small business owners, who relied on large funds from a single bank. Some legislators had direct interests in the banking sector and/or engaged in small businesses. According to Gutierrez's study (1994:14), 19 of the 50 members of the Committee on Banks were once, or were still, involved in banking business. Some of them were former directors or executives of commercial banks. They included Reps. Rolando Andaya, Lualhati Antonio, Renato Dragon, Felicito Payumo, Ricardo Silverio, Rodolfo Tingzon and Jose Villarosa. Some provisions of the New Central Bank bill, which were designed to strengthen the Bank's regulatory powers, potentially restricted the business activities of these legislators. The bill imposed higher penalties and stricter rules on DOSRI loans, which might directly influence their business activities. As noted above, under the new rules, if the legislators concerned were to borrow a large amount of money from banks with which they were connected, they would waive the right of secrecy regarding their deposits in all banks. In this case, without a court decision, the Central Bank would

[62] See Benjamin E. Diokno, Professor of Economics, School of Economics, University of the Philippines, "Comments on the Bill Creating the Central Monetary Authority (Senate Version -- as of 23 February 1993)", Submitted for the Senate Committee discussion on 13th January 1993.

have access to individual account information in any banks and hence would be able to launch an investigation. Despite the potential loss of rights, opposition to this provision did not materialise. Domestic businesses, including small ones, broadly supported the legislation since they expected it to lead to a reduction in interest rates. In the early 1990s, they had suffered seriously from a sharp rise in interest rates.

Old tactics and a broad support for the reform from businesses, including banks, helped to promote the Central Bank reform. Nevertheless, these should not be stressed too much as a cause of the reform. In the Philippine Congress, under a weak party system, the dominance of the pro-Ramos coalition did not entirely guarantee a smooth legislative process, particularly with regard to the individualistic voting behaviour in the Senate. In fact, with respect to banking reform, the "old tactics" had never worked in the old Congress under the 1935 Constitution. Under the Aquino government, the majority of the members of the Senate and the House of Representatives were elected as Aquino's supporters. However, the Legislature, in particular the Senate, strongly opposed the President's key legislative measures, including foreign debt policy and the US bases issue. The Aquino government failed to implement the Central Bank reform, despite strong support from the IMF, the World Bank, donor countries and local businesses including banks. The successful implementation of the Central Bank reform can be fully understood in the context of the new constellation of political institutions created by the 1987 Constitution.

Although the Ramos government inherited its economic strategy from the Aquino government, the transition from Aquino to Ramos was a critical trigger in changing policy-making institutions and organisations. The Ramos government articulated the problem of the close link between political instability and economic failure. Political instability was the main obstacle to attracting foreign investment and thus to promoting economic growth; and economic growth and poverty alleviation were crucial to solving the internal security problems. The government stressed the importance of political stability and national unity for economic development. In the Philippine context, along with internal armed conflicts, the conflict between the Executive and the Legislature was seen as a key obstacle to national unity and political stability. The government stressed

that "For the past decades, relationships between the Executive and Legislative have been characterised as adversarial in nature. It is not uncommon to hear of stalemates or gridlock occurring, due to inability of the two branches of government to resolve policy differences" (LEDAC,1993:1).

In the first Presidential State of the Nation Address (SONA), Ramos expressed his deep concern about this problem and pointed out that "a shift to a more consensual type of decision-making" was a vital necessity (LEDAC,1993:1). In order to build politically stable conditions as the basis of economic growth, the establishment of "a harmonious and productive working relationship between the Executive and Legislative branches of government" was one of the first tasks for the Ramos government, along with the peace settlement of internal armed conflicts (PMS,1997:2).[63] The "harmonious" relationship was boosted by the creation of the Legislative-Executive Development Advisory Council or LEDAC (Republic Act No. 7640 dated 9 December 1992), which facilitated the passage of priority legislation (PMS,1997:17). The LEDAC is composed of the President (chairman), Vice President, four Senators (Senate President, Senate President Pro-Tempore, Senate Majority Floor Leader, Senate Minority Leader), four Congressmen (Speaker and other three Congressmen including one member of a minority party), seven Cabinet members, and three other members (Local Government Unit Representative, Private Sector Representative and Youth Representative). Under the Ramos government, the LEDAC meeting was held once a week for many years. The role of Presidential Legislative Liaison Office (PLLO) was also enhanced.

As Professor Alex Magno, a Filipino political scientist of the UP, points out, a really distinctive feature of this government was "the extent to which the executive branch and legislative branch consult and consolidate their opinion" (see Caoili, et al.,1994:29-30). There are formal and informal consultation processes, not only between the House of Representatives and Malacañang but also between the Senate and Malacañang (ibid.). Senators were often invited to Malacañang for informal and formal meetings to discuss policy issues. This was in sharp contrast to President Aquino, who was hesitant to involve herself directly in the legislative process.

[63] In this PMS report, other major tasks seen as necessary to the restoration of political stability include: opening people's participation in governance and; police and military reform.

Apart from LEDAC, the Ramos government facilitated the construction of a common legislative agenda in various ways. It invited the legislative leaders to form an economic development plan. Senators (Edgardo J. Angara, Gloria Macapagal-Arroyo, and Alberto G. Romulo) and Congressmen (Felicito C. Payumo, Rolando R. Andaya and Salvador H. Escudero III) participated in the Steering Committee, chaired by Cielito F. Habito, Secretary of Socio-Economic Planning, whose brief was to prepare the Medium-Term Philippine Development Plan (MTPDP) for 1993-1998.

In addition, in order to consolidate a common legislative agenda, the People's Summit Leading to "A Social Pact for an Empowered Economic Development (SPEED)" was held in Summer, 1993. In July, the Senate passed Resolution No.544 urging the President to immediately convene an Economic and Social Summit. The ultimate objective of the Summit was to forge a national consensus towards moving the economy forward and propelling the country towards a Newly Industrialised Country (NIC) status by the year 2000 (LEDAC,1993:1). The Summit showed the extent of the cooperative relationship between the Executive and the Legislature.

It must be noted that the new institutional frameworks created by the 1987 Constitution encouraged legislative leaders to cooperate with the Executive in the promotion of socio-economic reforms. After the long Marcos dictatorship, the 1987 Constitution, which limited the presidency to a single 6-year term, opened the door for legislative leaders to stand as serious candidates for the Presidential seat. Importantly, the incumbent President was no longer a strong rival to legislative leaders who sought the next Presidential seat, since the Presidential term was limited to one term only under the 1987 Constitution. It should be noted that the result of the 1992 Presidential election provided a foundation which encouraged legislative leaders to cooperate with the President to reform the economy.[64] Legislative leaders, including the House Speaker, Jose de Venecia, the New Senate President, Edgardo Angara, and the Chairman of the Senate Committee on Banks, Raul Roco, harboured presidential ambitions.

[64] For a careful analysis of the 1992 election in the context of political change and continuity, see Putzel (1995).

For the legislative leaders, the 1992 election highlighted important lessons about Presidential elections under the newly-restored democracy. Ramos, who was endorsed by Aquino, won with 23 per cent of the votes, the smallest victory in all the country's Presidential elections. Miriam Defensor-Santiago surprisingly gained 20 per cent of the vote. She was a famous anti-corruption campaigner, but she lacked solid organisational support. The well-funded candidates, Eduardo Cojuangco Jr., (the National People's Coalition: NPC) a close associate of President Marcos and one of the country's richest businessmen and Ramon V. Mitra (the Laban Democratikong Pilipino: LDP), the candidate of the party which dominated Congress and had an extensive campaign machine, did not attract more votes than the "weak" candidate, Miriam Defensor-Santiago. Later Senator Roco stated that his political campaign for the 1998 Presidential election was inspired by the campaign of Miriam Defensor-Santiago for the 1992 election.

For legislative leaders who harboured ambitions for the next Presidential seat, support from the President and enjoying popular appeal as a reformer were crucial assets. For example, in the House, Speaker de Venecia, who had been severely criticised by the media for his involvement in suspect business dealings, was keen to clear his "bad" image for the purposes of promoting his career. In particular, his Landoil Resources Group, one of the most successful construction firms in the country, which conducted lucrative construction projects in the Middle East during the Marcos era, was investigated by the Presidential Committee for behest loans, although de Venecia denied any criminality of the deal.[65] After maintaining a cooperative relationship with the President, de Venecia was endorsed by President Ramos as the administration's candidate for the 1998 Presidential elections.

Senate President Angara, who became the President backed by Ramos, was a supporter of the reform agenda. Newly-elected senator Raul Roco, the Chairman of the Committee on Banks, was also keen to reform the economy and cooperated with the President. As the Chairman of the Committee, he enthusiastically undertook a massive amount of work to finalise the passage of the bill in a short time. It should be noted that

[65] See, for example, PDI, 23 October 1992, "P31B lent to cronies with little collateral".

the electoral term of senator Roco was limited to three years, due to the result of the 1992 election in accordance with the transitional provisions of the 1987 Constitution. He had to stand for the 1995 elections and was reelected as a senator. Later, both senators became candidates in the 1998 presidential election and both boasted to voters of their pivotal role in economic reform under the Ramos government. Angara claimed that most key economic reforms were enacted under his Senate presidency.[66] Roco was very proud of his role as the father of the Bangko Sentral ng Pilipinas. He claimed that one third of the Law was actually written by himself.[67]

The ambitious strategy for industrialisation, Philippines 2000, was not new as an economic plan but the strategy was nevertheless innovative, since it addressed institutional and organisational problems, namely the uncooperative relationship between the Executive and the Legislature, as an obstacle to economic reform. With the new constellation of political institutions created by the 1987 Constitution, the initiatives taken by the Ramos government to form a common legislative agenda were very effective in facilitating economic and political reform. Within one year, many critical reforms were implemented through the legislative process, including the repeal of the Anti-Subversion Act (Presidential Decree No. 1700), which paved the way for a comprehensive peace process with rebel groups (Republic Act No. 7636 dated 22 September 1992); the creation of a Department of Energy to address power shortages (Republic Act No. 7638 dated 9 December 1992); and setting a date for the elections in the ARMM (Autonomous Region in Muslim Mindanao, Republic Act No. 7647 dated 5 March 1993).[68] The Central Bank reform which had not been implemented by the Aquino government was one of these critical reforms.

[66] Speech by Edgardo Angara at Ateneo de Manila University, "The Demands of Leadership: Leadership Series II", 17 May 1997.

[67] Speech by Raul Roco at Ateneo de Manila University, "The Demands of Leadership: Leadership Series II", 28 June 1997.

[68] For the lists of legislation, see PMS (1997:17-18).

Conclusion

After the end of the Cold War, the Philippine government could no longer expect "special" support from the US government, in terms of lending from the IMF and the World Bank. Faced with economic downturn, the Ramos government was committed to the Central Bank reform in order to increase the creditworthiness of the country in the international financial system. Skilful use of the old tactics to consolidate the support of the President's allies in the Legislature was also important for the successful passage of the key legislation.

Nevertheless, the new constellation of political institutions created by the 1987 Constitution facilitated cooperation between the President and legislative leaders and was the most critical for the implementation of the Central Bank reform. Amicable relations were built by various means, including initiatives taken by the newly-elected President such as the formation of the LEDAC. New political framework instituted by the 1987 Constitution provided legislative leaders with an additional incentive to cooperate with the President's reform agenda, since his support was important for those who aspired to the next Presidential seat. The 1992 election, the first Presidential election under the new Constitution, also provided an important lesson for the legislative leaders indicating that populist appeal as a reformer was a significant tool that could be used to attract many votes in the Presidential election.[69]

The lack of strong opposition from the business community also helped to implement the Central Bank reform. However, the entry of new foreign banks, which is examined in the next chapter, can be seen as more controversial banking reform, since a reformist force had to face strong resistance from the powerful interest group constituted by big domestic commercial banks.

[69] For the importance of "populist images", see Putzel (1995:43).

Appendix 5-1:

The Functions and Accumulations of MAA, ESAA and RIR accounts

Monetary Adjustment Account (MAA)

This account absorbed the costs involved in the issuance of and interest payments on Central Bank securities, interest payments on National Government deposits and costs for minting and printing currency. These expenses pushed the MAA's outstanding balance from P6.9 billion in 1982 to P48.5 billion in 1991 (P59.8 billion as of November 1992). This sharp increase was largely due to huge interest payments on high-yielding Central Bank bills, namely Jobo bills and Joey bills and interest payments on National Government deposits. In addition, no revenue was generated to cover the cost of printing money.

Exchange Stabilisation Adjustment Account (ESAA)

This account absorbed, mostly, interest payments on foreign borrowings and foreign currency deposits and other external obligations. Over the years, the Central Bank had to borrow foreign exchange to cover the deficit between the dollars which the country gained from exports and grants and the dollars which the country spent on imports. From 1981 to 1991, the annual interest payments on foreign borrowings and other foreign obligations were P11 billion per year, on average. Following the 1983 financial crisis the ESAA's outstanding balance rapidly increased. It was further aggravated by the peso's depreciation over the years. The peso's value declined by an average of 14.8 per cent per year from 1983 to 1991. This meant that the Central Bank had to amortise its assumed foreign liabilities with more pesos per dollars. As a result, the Bank's debt servicing requirements increased sharply. From P3.1 billion at the end of 1982, the outstanding level of ESAA had risen to P87.8 billion by the end of 1991 (P86.3 billion as of November 1992).

Revaluation of International Reserve Accounts (RIR)

This special account was debited or credited as a result of the revaluation of the bank's net assets or liabilities in gold or foreign currencies. The law defined this account as a self adjustment account which the Central Bank did not amortise. During the economic crisis, swap and forward cover arrangements rapidly increased. As the peso depreciated, losses were accumulated. In addition, the differentials resulting from the change in the exchange rate were placed in blocked peso accounts because, if these differentials were actually paid, the money supply would have expanded tremendously. The Central Bank paid interest at the prevailing rate for the blocked peso accounts. Interest payments on these blocked swap liabilities amounted to P11.2 billion between 1986 and 1991. The RIR level soared from P1.8 billion in 1982 to P88.4 billion by 1985 and to P166.3 billion in 1991 (P163.5 billion as of November 1992).

Sources: The Central Bank, Script For A Computer Presentation on Video Tape (Audio Video): "Toward An Independent Central Monetary Authority" (the Central Bank, Video Script), pp.4-7 and House Committee on Economic Affairs, "Understanding and Addressing the Huge CB Deficit", Annex: CB Suspense Accounts.

Table 5-1. CB Loss / Special Accounts

CB Losses	**P334.6 billion**
1. Forward Exchange Cover	P51.6 billion
a) Oil Companies	P41.9 billion
b) National Food Authority	P7.6 billion
c) National Steel Corp.	P2.1 billion
2. Interest Payments on Foreign Loans	P77 billion
3. Concessional Loans and Market Operation	P101 billion
4. Opportunity Losses (CB's Holding Low Yielding NG Securities)	P105 billion
Special Accounts	**P302.5 billion**
1. Monetary Adjustment Account	P48.5 billion
a) Issuance and servicing of CB instruments	P35.3 billion
b) Interest on National Government deposits	P19.9 billion
c) Cost of minting and printing currency	P4.3 billion
2. Exchange Stabilisation Adjustment Account , of which:	P87.8 billion
Cost of servicing foreign loans	P91.3 billion
3. Revaluation of International Reserve	P166.3 billion

Sources: Congressional Planning and Budget Office (CPBO), "Central Bank Losses and the Proposed Central Monetary Authority", submitted to the House Committee on Banks and Financial Intermediaries, on 11 March 1993

Table 5-2. Differences Between House Bill No. 7037 and Senate Bill No. 1235

1. Capital
House: P10 billion. (Sec.2)
Senate: P50 billion. (Sec.1)
R.A. 7653: P50 billion (initially P10 billion). (Sec.2)

2. Composition of the Monetary Board
House: All members from private sector shall be full time. (Sec. 6)
Senate: 3 full time, 2 part time.
R.A. 7653: All members from private sector shall be full time. (Sec. 6c)

3. Remuneration of MB members
House: To be approved by Congress. (Sec.12)
Senate: Limits of P150,000 or P120,000 a month. Fixed by President. (Sec.12)
R.A. 7653: Fixed by President. (Sec.13)

4. Compensation of Personnel
House: Subject to the Salary Standardisation Law. (Sec. 14c)
Senate: Exemption from Salary Standardisation Law (above salary grade 21). (Sec. 14c)
R.A. 7653: Exemption from Salary Standardisation Law (above salary grade 19). (Sec. 15c)

5. Powers of the Governor
House: No quasi-judical powers.
Senate: Governor has quasi-judical powers. (Sec. 16e)
R.A. 7653: Governor has quasi-judical powers. (Sec. 17)

6. Departments
House: No statutory departments.
Senate: Dept of Economic Research is statutory dept. (Sec. 21)
R.A. 7653: No statutory departments.

7. Secrecy of Bank Deposits for potential DOSRI loans
House: Waiver applies to deposits in all banks. (Sec. 30)
Senate: Waiver of secrecy applies to deposits only in lending bank. (Sec. 25)
R.A. 7653: Waiver applies to deposits in all banks. (Sec. 26)

8. Definition of Insolvency

House: Insolvency does not include inability to pay caused by extraordinary demands induced by financial panic in the banking community. (Sec. 38)

Senate: Does not provide for such a qualification. (Sec. 29)

R.A. 7653: Insolvency does not include inability to pay caused by extraordinary demands induced by financial panic in the banking community. (Sec. 30a)

9. Penal Provisions

House: Lower penalties. (Sec. 107,108)

Senate: Higher penalties. (Sec. 32,33)

R.A. 7653: Higher penalties. (Sec. 34,35,36)

10. Distribution of Profits

House: 75% of net profits placed in a special deposit account to be applied to the redemption upon maturity of Government securities held by the BSP. (Sec. 100)

Senate: 50% of net profits reverts to National Treasury. (Sec. 42)

R.A. 7653: 50% of net profits reverts to National Treasury. (Sec. 44)

11. Issue Power

House: BSP has no such authority.

Senate: BSP has authority to arrest or conduct searches to maintain integrity of the currency. (Sec. 48)

R.A.7653: BSP has authority to arrest or conduct searches to maintain integrity of the currency. (Sec. 50)

12. Special Credit Operations

House: BSP may engage in special credit operations to promote lending operations of banks engaged in long-term financing. (Sec. 65)

Senate: No such provision.

R.A. 7653: No such provision.

13. Foreign Asset Position of the BSP

House: BSP has to maintain at all times a net positive foreign asset position. (Sec. 88)

Senate: No such provision.

R.A. 7653: BSP has to maintain at all times a net positive foreign asset position. (Sec. 71)

14. Coordination of Credit Policies

House: Government-owned corporations which perform banking or credit functions shall coordinate their general credit policies with those of the MB. (Sec.112)

Senate: No such provision.

R.A. 7653: Government-owned corporations which perform banking or credit functions shall coordinate their general credit policies with those of the MB. (Sec.109)

15. Structure

House: CB abolished. All assets & liabilities transferred to BSP. (Sec. 131)

Senate: CB shall continue to exist for the purpose of disposition and liquidation of assets and liabilities it may retain. (Sec.125d)

R.A. 7653: CB shall continue to exist for the purpose of disposition and liquidation of assets and liabilities it may retain. (Sec.131 and 132)

16. Financial Restructuring

House: A 25-year bond shall be issued by the NG in favour of BSP. The terms shall be determined by a Committee. (Sec. 131)

Senate: A committee shall determine what assets & liabilities shall be transferred to BSP. The MB shall recommend to Congress solutions to retire CB liabilities and losses. (Sec. 125)

R.A. 7653: A committee shall determine what assets & liabilities shall be transferred to BSP. (Sec. 132)

Sources: Internal Memorandum for Bicameral Conference Discussion on 8, 9 and 10 June 1993, "Differences Between H. No. 7037 & S. No. 1235";
Committee Records, Bicameral Conference Discussion on 8, 9 and 10 June 1993; and Republic Act 7653, New Central Bank Act

Chapter 6.
Banking Sector Reform under the Ramos Government (Part II): The Entry of New Foreign Banks

Introduction

The Philippine banking sector had been closed to new foreign entrants since the General Banking Act became effective in 1949. Since then only four foreign banks had operated in the country. The legislation to allow entry of new foreign banks was significant in signalling a change in the industry. A journalist, Stella Tirol-Cadiz, wrote that "[O]pening up banking to foreign competitors would have been unthinkable a decade ago. Liberalisation would have been resisted by powerful bank owners and officers".[1] Facilitating competition by liberalising the entry of new foreign banks had often been discussed but it was seen as an impossible measure due to strong opposition from the powerful oligarchy (see Hutchcroft,1993a:576). Under the Ramos government, the Bankers Association of the Philippines (BAP), which had been seen as a very powerful business organisation, desperately attempted to protect its business interests by pushing its own proposal. Nevertheless, their efforts were not entirely successful. They were able to influence the legislation but they could not prevent liberalisation. Although the legislation included some restrictive provisions, it was seen as a landmark legislation which had a large impact on the banking sector policy. This legislation became an important catalyst which opened up the banking sector. In particular, the BAP expressed its dissatisfaction with the legislation, because the number of entrants through majority-owned subsidiaries was not specified, although the law limited the number of branches which foreign banks could establish. Along with other liberalisation measures, the structural reform facilitated change in the banking sector. The big commercial banks had to face the fiercer competition encouraged by liberalisation.

Under the Ramos government, the liberal reformers had consolidated support to implement the structural reform, although the reform was less radical than the

[1] MALAYA, 29 November 1993, "Landmark law opens up banking".

government initially intended. There were various factors which encouraged reform under the Ramos government. The IMF, the World Bank and the US government had always been supportive of liberal reform. In particular, they were keen to stimulate financial liberalisation in the mid-1990s. Although the structural reform was not encouraged by conditionality lending, the policy preferences of the World Bank and the US government consistently gave the Philippine government strong incentives to open up the banking sector. In the latter half of the 1990s, multilateral trade and economic agreements including GATT, WTO, AFTA and APEC also encouraged liberalisation as a world trend. The liberal reform of other ASEAN countries, including Singapore, Indonesia, Malaysia and Thailand, helped to attract foreign investment, and were often referred to by pro-reformers as "successful" cases. The policy experience of these countries was therefore influential in facilitating liberalisation.

Nevertheless, foreign influence and pressure from the IMF, the World Bank and the US government cannot be seen as the only decisive factor behind the structural reform. Strong initiatives to liberalise the banking sector originated from the Executive branch. Under the Ramos government, liberal reform was formulated tactically, supported broadly and implemented forcefully. As we saw in the previous chapter, a new constellation of political institutions emerging as a consequence of the 1987 Constitution strengthened the interests and capacities of the President in advancing reforms in the banking sector. Liberal reform was backed by a political campaign which aimed to show the President's willingness to dismantle the power of the oligarchy. An "Anti-Oligarchy" campaign was broadly supported by the general public. The liberal reform of the Ramos government also gained broad support from business, the media and the general public by addressing immediate economic problems like power shortages and telephone services.

Liberal Coalition: "Anti-Oligarchy" Campaign

After global interest rates increased in the late 1970s, the importance of foreign investment was recognised as a vital necessity for the economic development of the Philippines. In the early 1980s, liberalisation was planned by the technocrats, but it was stalled by the serious economic turmoil during the late Marcos era (see Montes and Ravalo,1995:153-154). Under the Aquino government, an economic development strategy which stressed export promotion and foreign investment was adopted. To attract foreign funds and expand export products, various liberalisation measures were initiated. The Foreign Investment Act of 1991 was a key piece of legislation designed to attract foreign investment by liberalising the economy. Other liberalisation measures, including trade liberalisation (tariff reforms) and foreign exchange liberalisation, also began to be implemented. The liberalisation initiated by the Aquino government was further facilitated by the Ramos government, which implemented liberal reform in various areas including trade, energy and telecommunications. The entry of new foreign banks became one of the key measures in the liberalisation of the economy.

The strength of the government's commitment to liberal reform was closely connected to its political agenda. Amando Doronila observed that, for all the discussion of protectionism and liberalisation, the more important context of liberal reform in the banking sector was "the administration's campaign to break the cartels and monopolies / oligopolies that have been the base of economic and political power of the Filipino oligarchy".[2]

In the government, close allies of the President were at the centre of the political campaign. Among them, Jose T. Almonte, Director General of the National Security Council, the Presidential Security Adviser was a key strategist. The retired general with a background in intelligence was a supporter of the Reform the Armed Forces Movement (RAM) during the Marcos era, which played a critical role in the "EDSA revolution". He headed the Economic Intelligence and Investigation Bureau in the Finance Ministry under the Aquino government, where he began to track down

[2] PDI, 25 April 1994, "FVR has opportunity to crack bank cartel".

economic crime and self-serving business practices. As Presidential Security Advisor, he was a core member of the Ramos government and played a leading role in drafting the President's early speeches and providing input for the strategic framework of "Philippines 2000".

As a security expert, Almonte identified the country's main concern: the importance of poverty alleviation, particularly in rural areas, as a means to solve internal security problems.[3] Almonte was obsessed with the oligarchy and was convinced that the root of the country's problems lay in the dominance of "the predatory rent-seeking elite" in key industries (Coronel,1998:135-136). In seeking to crack down on monopolies (or cartels) and the dominance of the oligarchy, Almonte's approach was to use market forces and strong Presidential initiatives.[4] The Ramos government was undoubtably supported by some members of the "oligarchy". Most notably, former President Aquino, who endorsed Ramos, belonged to one of the most powerful families in the country. However, since President Ramos and Almonte who had a prominent career as a military commander were not seen as members of the "oligarchy", the promotion of the "Anti-Oligarchy" campaign was effective in generating broad support for the government from the general public.

A close ally of Jose Almonte was Antonio Carpio. He was a corporate lawyer who was a member of the Ramos campaign team and became presidential legal advisor in 1992. As a corporate lawyer, he realised that there were strong proponents of liberal reform in business. Many business elites were frustrated with the lack of infrastructure, the economic recession and the slow progress of reform. Coronel explains his commitment to the reform: "Like many who had a brush with student activism in the 1970s, he found Almonte's anti-oligarchy position enticing" (Coronel,1998:136).

There were also proponents of liberal reform in various government agencies and among staff in Congress. Romulo Neri, the Director of Congressional Planning and Budget Office (CPBO) was a strong proponent of liberal reform. The research body of the House of Representatives was established by Speaker Ramon V. Mitra after the

[3] Interview, Jose Almonte, Presidential Security Advisor, 2 June 1998.

[4] For his view on development strategy, for example, see Almonte (1996).

Legislature was restored under the Aquino government. The former professor of the Asian Institute of Management was appointed by Speaker Mitra as director of the office, but he also became a credible economic advisor to his successor, Speaker Jose de Venecia. Director Neri was described by the Speaker as a very talented economic advisor.[5] The relationship between the Speaker and the CPBO was so close that some saw the CPBO as the Speaker's office in the House.

Under the Ramos government, strong networks of liberal reformers were developed. The liberal reformers in various agencies cooperated with each other to push reforms and to curb opposition. Neri explained that there were members of the reform coalition in each of the key economic agencies, including the National Economic Development Authority (NEDA), Department of Finance, and Department of Trade and Industry.[6] They shared critical information, particularly on the opposition's movements through daily contacts and worked together to curb movements against liberal reform.

Ramos's initiatives to facilitate cooperation between the Executive and the Legislature encouraged the formation of informal and formal networks for the liberal coalition. Furthermore, the Ramos government was keen to mobilise support from the general public including various NGOs. As noted earlier, one such effort was the People's Summit on Social Pact for Empowered Economic Development (SPEED) which was organised by close collaboration between the Legislature and the Executive.[7] One of the pre-Summit meetings was held at Malacañang and had an attendance list of more than thirty pages.

Once the Executive and Legislative leaders had agreed on the importance of the reform, there was little chance for opposition forces to stop the reform entirely. Even the owners of the big domestic banks, who were supposed to be the most influential and

[5] Speech by Jose de Venecia Jr. at Ateneo de Manila University, "The Demands of Leadership: Leadership Series II", 28 June 1997.

[6] Interview, Romulo Neri, Director General, Congressional Planning and Budget Office, 23 June 1997.

[7] For the SPEED meeting, see, "Final Report: People's Summit on Social Pact for Empowered Economic Development", prepared by LEDAC Secretariat, October 1993.

politically powerful segment of the oligarchy, were not able to stop the reform, although they were successful in inserting some restrictive provisions into the legislation. In the following sections, the legislative process underlying the structural reform, the entry of new foreign banks, is examined as a means of exploring the politics of economic reform.

The Legislature, the House of Representatives in particular, is often seen as a stumbling-block to the reform of the existing system since it has always been dominated by the traditional "oligarchy", who are beneficiaries of the existing system. In fact, the House has opposed and modified critical economic reforms, most notably land reform[8] and tax reform.[9] However, the successful legislation that allowed the entry of new foreign banks showed the complexity of the dynamics of Philippine legislative politics. Surprisingly, the House formulated a very liberal bill which aimed to facilitate the entry of new foreign banks, while the Senate bill was a more restrictive guideline including provisions which were consistent with the BAP's position.

House Bill No. 8226: Drafting the Liberal Bill

Under the Ramos government, the legislative leaders in the House took initiatives to liberalise the banking sector without delay. This was consistent with the Executive's agenda to liberalise the economy. However, this liberalisation measure was not entirely new to the House. In the Ninth Congress, the House Committee already had a draft bill which aimed to amend the General Banking Act (R.A.337) for the entry of new foreign banks, since the bill had been approved for the third reading in the Eighth Congress. The new bill, which was similar to the previous one, was again filed and discussed in a Joint Committee comprising the Committee on Banks and Financial Institutions (Chaired by Jose Carlos V. Lacson) and the Committee on Economic Affairs (Chaired by Felicito C. Payumo). The main author of the bill was Margarito B. Teves, a member of the opposition party (LDP).

[8] For detailed analyses of key agrarian reform legislation under the Aquino government, see Putzel (1992, Chapter 8) and Magadia (1999, Chapter 3).

[9] For detailed analysis of tax reform focusing on VAT legislations under the Ramos government, see Eaton (1998, Chapter 5).

Between October 1992 and March 1993, the joint Committee discussed and finalised the bill. The Committee formulated the bill in consultation with the Central Bank, whose officials were often invited to the Committee discussions as technical advisors. They also had many hearings with representatives from resident foreign banks, offshore banking units (potential applicants for new entry), BAP and economists from PIDS and the Centre for Research and Communication. Position papers were submitted by various organisations and economists including: Resident Foreign Commercial Banks (Bank of America, Citibank, N.A., Hong Kong Shanghai Bank and Standard Chartered Bank); Offshore Bankers Association of the Philippines; Dr. Mario B. Lamberte, Vice-President, Philippine Institute for Development Studies; and Rural Bankers Association of the Philippines.[10]

The House bill was very "liberal" in the sense that it did not include restrictive provisions for the entry of new foreign banks. The Monetary Board of the Central Bank was given the authority to determine the details with respect to the pace, composition and extent of the liberalisation. Essentially, the bill could be seen as a set of broad guidelines to facilitate the entry of new foreign banks. First of all, the bill approved three modes of entry as follows: (1) the establishment of branches, (2) the acquisition of wholly or majority- owned subsidiaries and (3) investments of up to 70 per cent of the voting stock of an existing bank. Second, the bill stipulated neither the specific numbers of new foreign banks allowed to establish branches nor the numbers of branches that each foreign bank might open. Third, the bill did not limit in any way the entry of a foreign bank. With the Monetary Board's approval, a foreign bank could establish branches, acquire wholly-owned subsidiaries and own 70 per cent of the voting stock of an existing bank.

[10] See Statement by Resident Foreign Commercial Banks (Bank of America, Citibank, N.A., Hong Kong Shanghai Bank and Standard Chartered Bank); Offshore Bankers Association of the Philippines, "Comments on the proposed House Bill No.263" by J. Desmond Ormsby, 16 October 1992; Dr. Mario B. Lamberte, Vice-President, Philippine Institute for Development Studies, "Comments on House Bill No.263: An Act Liberalising the Entry and Operations of Foreign Banks in the Philippines" 19 October 1992; and Rural Bankers Association of the Philippines, "RBAP Position on House Bill No.263".

The bill included some preferential criteria for selecting a new foreign bank, but they were not very strict. They included the following: (1) it must be a foreign banking institution; (2) preference would be given to publicly-held banking corporations with global reputations for financial innovation and stability; (3) geographic representation, specifically in terms of the trade and investment relationship between the Philippines and the country of incorporation of the foreign bank; (4) reciprocity arrangement; and (5) technology transfer.

The initial bill (H.B. 263), which was very similar to the previous bill, did not even include a provision on capital requirements. In the previous bill, the authority to decide on capital requirements was given to the Monetary Board. Although a guideline on capital requirements was added to the bill through Committee discussion, the basic features of the bill did not change. The capital requirement was proposed by Rep. Ponce Enrile, a member of the joint Committee, who was one of the most powerful politicians in the post-war politics of the Philippines. In the Committee meeting, he argued that Congress should assume responsibility for establishing the policy and for the requirements for the entry of a new foreign bank into the country, rather than leave it to the Central Bank.[11] However, his proposed capital requirements, which were adopted by the Committee, were far less restrictive in comparison with those specified by the Senate bill.[12]

Initially, the Central Bank expressed its concern about the mode of entry. In the first joint meeting, Mr. Feliciano Miranda (Deputy Governor, the Central Bank) recommended that the entry of foreign banks should be only through the establishment of branches in the Philippines.[13] The Deputy Governor pointed out that since the existing law limited the holding of a Bank's share for a Filipino corporation (up to 30%) and for individuals (up to 20%) and banned the establishment of a majority or

[11] See Minutes of the Joint Meeting: Committee on Banks and Financial Institutions and Committee on Economic Affairs, 19 October 1992.

[12] See Minutes of the Joint Meeting: Committee on Banks and Financial Institutions and Committee on Economic Affairs, 9 February 1993.

[13] Committee Records: A Joint Committee; Committee on Banks and Financial Institutions and Committee on Economic Affairs, 19 October 1992, p.23.

wholly owned subsidiary by Filipino commercial banks, the entry of foreign banks through the acquisition of wholly or majority owned subsidiaries or through investments of up to 70 per cent of voting stock of an existing bank potentially gave foreign banks advantages vis-à-vis Filipino commercial banks. However, the amendment was not adopted by the Committee. Rep. Teves, the author of the bill, insisted that the bill would not advantage foreign banks due to the "even playing field" principle: whatever rule applied to foreign banks would also apply to domestic banks.[14] He suggested changes to the existing law which restricted the ownership of banks.

The principle of the bill, which aimed to amend the General Banking Act for the entry of new foreign banks, was supported by representatives from various banking organisations, including: Resident Foreign Commercial Banks; the Offshore Bankers Association of the Philippines; and the Rural Bankers Association of the Philippines. The entry of new foreign banks was a very sensitive matter for big commercial banks whose businesses were directly affected by the new entrants. The Bankers Association of the Philippines (BAP) which was dominated by such big commercial banks stressed the importance of the principle of an "even playing field" between domestic and foreign banks. However, it was not able to secure the insertion of more restrictive provisions into the House bill by lobbying. The Central Bank did not have a strong reason to push restrictive provisions since the flexible bill, which gave the Monetary Board broad authority to determine the details of the liberalisation measures, worked in its favour.

The House of Representatives has often been seen as an obstacle to reform of the economy due to the dominance of the "traditional elites" (or oligarchy) which have benefitted from the existing system. In fact, with regard to land reform, the House prevented the passage of a "liberal" bill under the Aquino government.[15] The House was not keen to increase revenues through tax reform.[16] However, with regard to the entry of new foreign banks the liberal bill was broadly supported in the House by legislators across party lines. Sixty-five legislators were listed as the co-authors of the bill, which

[14] Committee Records: A Joint Committee; Committee on Banks and Financial Institutions and Committee on Economic Affairs, 19 October 1992, p.24.

[15] See Putzel (1992, Chapter 8) and Magadia (1999, Chapter 3).

[16] For the case of VAT reforms under the Ramos government, see, Eaton (1998, Chapter 5).

was approved and sent to the Senate on 31 March 1993. The adoption of the liberal bill reflected the general acceptance of liberal reform in the House, the high expectations of liberal reform in the business community and the limited influence of the big banks with regard to this legislation in the House.

Since the Aquino government's adoption of an economic development strategy which emphasised foreign investments and export promotion, support for liberal reforms had gradually been growing among legislators and the business community. In particular, under the Ramos government, LDP (Liberalisation, Deregulation and Privatisation) was supported by many legislators after this approach proved effective in solving long-term problems in the country's infrastructure, such as energy shortages and underdeveloped telecommunications. The liberalisation of the banking sector by opening it up to the new entry of foreign banks was seen as a critical measure supplementing the Foreign Investment Act, passed under the Aquino government. In his Sponsorship Speech, Rep. Payumo emphasised that this bill was "vital in complementing the reform in trade, investments and foreign exchange which are necessary to stimulate economic growth and development".[17]

To attract foreign investment was seen as a vital necessity for improving the economy, and many expected to benefit from foreign investment. The business community expected that the entry of new foreign banks would generate competition among big commercial banks, and that this would lead to a decrease in interest rates. In addition, it was believed that the expansion of the new foreign banks would bring more new financial products, which would benefit many businesses.

The passage of the liberal bill in the House also suggested that the influence on the legislative process of the large families which had dominated the banking sector was not as decisive as previously assumed. Among the traditional elites, there were diversified business interests and policy preferences. All key supporters of the bill were from prominent political families who had a solid economic base and political support

[17] Sponsors of the bill stressed these merits. See, Sponsorship Speech of Rep. Lacson, Rep. Payumo and Rep. Teves, Records of the House, 30 March 1993 and 31 March 1993.

in their local constituencies.[18] The main author, Margarito V. Teves, is a member of a wealthy family from Negros Oriental, a sugar production area and a former chief economist of the Ayala Corporation. Sponsors of the bill included Jose Carlos V. Lacson (Negros Occidental), Felicito C. Payumo (Bataan) and Amado S. Bagatsing (Manila) who are all from wealthy families involved in politics. It is assumed that they have close relationships with the big banks which dominate the banking sector through their various business activities. Nevertheless, they were not supportive of the large families who had interests in big banks. For example, in his sponsorship speech, Amado S. Bagatsing, who is from a wealthy family which has been very influential in politics in Manila, urged the necessity of opening up the highly protected banking sector which had been dominated by the large families.[19] Many legislators, particularly the Speaker, the majority leader and the members of the joint Committee, could have proposed the addition of restrictive provisions to the bill if they had wished. However, there was little attempt to favour the big commercial banks in the House.

Senate Bill No. 1606: Insertion of Restrictive Provisions

After the House finalised the bill, the Executive and legislative leaders placed a high priority on it. The Senate leaders expressed their commitment to opening up the banking sector at the People's Summit on Social Pact For Empowered Economic Development (SPEED) in August and September 1993. The Senate Committee on Banks, Financial Institutions and Currencies, chaired by Sen. Raul S. Roco, started to study the bill from October 1993, although bills had been prepared since early 1993. In the Senate, three different bills were filed as follows: S.B. 839 (by Sen. Gloria Macapagal-Arroyo), S.B. 1474 (by Sen. Neptali A. Gonzales, Sen. Edgardo J. Angara, Sen. Blas F. Ople and Sen. Raul S. Roco) and S.B. 1563 (by Sen. Leticia Shahani).

Initially, the three bills were not very different from the House bill in terms of the key provisions, including the mode of entry and the capital requirement, although some

[18] For their family backgrounds and business interests, see Gutierrez (1994).

[19] See, the Sponsorship Speech by Rep. Bagatsing, Records of the House, 31 March 1993.

restrictive provisions were included.[20] Through numerous formal and informal discussions in the Committee, the caucus of Senators and floor meetings, the Senate bill was formulated. The Senate created a separate bill to regulate the entry of new foreign banks, while the House bill was an amendment to the existing law, namely the General Banking Act. The Senate bill, unlike the House bill, included many restrictive provisions for the entry of new foreign banks. First of all, the Senate bill restricted entry to only one of the following modes: (1) the establishment of branches; or (2) acquisition of up to 60% of the voting stock of an existing bank; or (3) investments of up to 60% in one new banking subsidiary. Second, the bill specified the number of foreign banks which were allowed to establish branches and the number of branches that could be opened by each bank. Third, the bill required higher capital requirements for new foreign banks. Fourth, the bill included more specific guidelines for the selection of new foreign banks. The restrictive provisions added to the Senate bill were a reflection of nationalist (protectionist) sentiments, scepticism about the Central Bank's regulation, opposition to the Ramos government and its economic policy, cautious attitudes to radical liberal policy and the influence of the BAP's desperate advocacy.

The Committee held many hearings with representatives from various business organisations and economists. Central Bank officials, including governor Singson, were also involved in the Committee discussions as advisors. Since the House bill had been finalised, it was also referred to the Senate for discussion along with the position papers on the bill. Through the committee hearings, representatives from various business organisations expressed their expectations of the liberalisation measures and support for the liberal bill. Only the Bankers Association of the Philippines (BAP) was vocally opposed to the liberal bill and demanded more restrictive provisions to the Senate bill in order to create a stricter guideline based on the "level playing field" principle .

[20] For the bills, see "Comparative Analysis Between R.A. 337, H.B. 8226, S.B. 839, S.B. 1474 and S.B. 1563", 10 January 1993, prepared for the Senate Committee on Banks, Financial Institutions and Currencies.

Strong support for the entry of new foreign banks came from the resident foreign banks.[21] In particular, Citibank, which had been the largest foreign bank in the country, expressed its interest in expanding its business into retail banking businesses. It was the only foreign bank which planned to request the establishment of more than six branches after the bill was enacted. They clarified support for the liberal bill as follows:

> "We support a liberal version of the banking bill, even though our banks will be the most directly impacted competitively by new entrants into the market. We do so out of a conviction that economic liberalisation brings economic dynamism and growth. The new legal framework for foreign banking in the Philippines that will emerge from Congress as well as the regulatory process to be adopted by the banking authorities to implement the liberalisation can be realised. Understandably, some sectors, particularly domestic banking interests, have been advocating a restrictive framework which will undermine the liberalisation program and minimise the benefits to the users of financial services."

Offshore banks, which were operating a very limited business in the country, strongly supported the entry of new foreign banks[22] as they were potential applicants. Offshore banking units (OBUs) had been operating in the country since 1976. However, they were only allowed to accept deposits from non-Philippine residents and provide loans in foreign currencies. They were neither permitted to conduct business in pesos nor to borrow money from local banks. Some of them, including a Japanese bank (Bank of Tokyo), showed strong interest in opening a branch and expanding their business.[23]

Resident foreign businesses also expressed their support for the entry of new foreign banks. The foreign Chambers of Commerce were invited to the Senate hearing and the Chambers, including American, Canadian and Australian-New Zealand Chamber of

[21] See The Position of the Resident Foreign Banks on the Liberalisation of Foreign Banking in the Philippines, 20 October 1993.

[22] See Offshore Bankers Association of the Philippines, "Comments on the proposed House Bill No.263" by J. Desmond Ormsby, 16 October 1992.

[23] See Susumu Nakaichi's (General Manager, Bank of Tokyo) comments in Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 12 January 1994, p.19.

Commerce of the Philippines, published a statement of their position in favour of the liberal approach in a local business daily.[24]

In the Philippine business community, many were strong supporters of the liberal bill. Although solid ties between the commercial banks and big business through interlocking directorates were strong, this did not determine their positions on the bill. The anticipated benefits seemed to be much more important than the old business ties. The Philippine Chamber of Commerce and Industry (PCCI), the most influential business chamber in the country, expressed its support for banking liberalisation. Federico C. Pascual who became the President of Allied Bank, stated that PCCI's constituency consisted of the users of funds and that the more competition there was in the market the better. They expected that the new foreign banks would stimulate the banking business and bring new financial products and better services for the Philippine business sector.[25]

PhilExport, which represented the interests of small exporters, was also in favour of the entry of new foreign banks. PhilExport had close ties with the United States Agency for International Development (USAID) which it used to facilitate private investment and trade opportunities in the Philippines. Mr. Gerry R. Anigan, Policy Group Coordinator of PhilExport, expressed strong support for the bill's goal of liberalising the entry of foreign banks. Although some predicted that the entry of new foreign banks would have an impact on the wholesale markets of big business in the country, PhilExport argued that the small businesses would be potential beneficiaries of the entry of new foreign banks. They stated that;

> "We agree with the Governor that the principal objectives here are investment promotion and technology transfer. We also wish to emphasise that another objective which will be useful to exporters is the opening up of information networks for their linkages with international markets."...

[24] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 12 January 1994; and Business Star, Letters, 14 December 1993.

[25] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 9 November 1993, p.45 and Philippine Chamber of Commerce and Industry (PCCI), Chamber Views: Perspectives on the Liberalisation of Entry of Foreign Banks and Their Scope of Operations.

> "We also see that the increased competition arising from the entry of foreign banks should help improve access of smaller businessmen, smaller exporters to credits, as well as improve the availability of credit at internationally competitive rates, and increase the options or the financial instruments available on the market."[26]

Even the National Economic Protectionism Association (NEPA), headed by Rene Ofreneo, did not offer any objection to the entry of foreign banks. In its view, as long as the majority of banks were controlled by Filipinos, liberalisation measures which would foster economic growth would be beneficial to Filipinos as a whole.[27]

After the House had passed the bill and the issue had begun to attract media attention, the Bankers Association of the Philippines (BAP) became desperate to clarify its position. The BAP was keen to insert restrictive provisions into the Senate bill. The BAP, particularly its President, Rafael B. Buenaventura, the President of PCIBank and a former Citibank manager (later Central Bank governor), enthusiastically advocated proposals for the entry of new foreign banks to various media, the Senate Committee and individual Senators. The BAP represented the interests of the big commercial banks, which had dominated the banking sector and would be faced with fierce competition from new and existing foreign banks. These banks were desperate to protect their businesses from powerful competitors, particularly Citibank.

Changing conditions fuelled a sense of threat among the big domestic banks. First, the liberalisation of the banking sector had already started through deregulation of the establishment of new branches and new domestic banks. The competition among banks was becoming fiercer. In 1993, the new Central Bank governor, Gabriel Singson, had already allowed the establishment of two new domestic banks. Second, big commercial banks were afraid of the aggressive stance of the resident foreign banks. In particular, Citibank was keen to expand its business into retail banking for wealthy individuals

[26] Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 6 January 1994, p.49.

[27] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 6 January 1994, p.45.

where the domestic commercial banks had an advantage. Third, the Central Bank, which had been a protector of the domestic banks, was not entirely in favour of the domestic banks' position. The Central Bank also expected that the entry of new foreign banks would facilitate foreign investment. Furthermore, Governor Singson seemed to be supportive of Citibank's position since he appreciated Citibank's contribution to foreign exchange generation during the economic and foreign currency crisis of 1982-1983.[28] Fourth, the House had authorised the liberal bill and the bill had gained broad support from domestic and foreign businesses. There was little support for the BAP's position from Philippine businesses which had close relationships through inter-locking directorates. The domestic commercial banks were often criticised for their wide profit margins and the large spread between lending and borrowing rates.

The BAP claimed that it recognised the merits of foreign equity and investment and welcomed the entry of new foreign banks subject to the principles of the level playing field and reciprocity, and to the institution of policies which would guarantee effective control by Filipinos of the country's financial and banking system.[29] The BAP severely criticised the liberal bill passed by the House. First, the BAP claimed that it was inaccurate to state that the Philippine banking sector was "more restricted and protective" vis-à-vis its ASEAN neighbours, since there were far fewer foreign banks in the Philippines than in the other countries, but the total assets of the foreign banks were not smaller than those in the other countries. Second, it was not accurate to state that the entry of foreign banks would enable "savings mobilisation" and "achieve greater efficiency through increased competition". Since the majority of foreign banks were interested only in wholesale business, the impact of the new entrants would limit the services offered to big corporations. Third, the BAP even expressed scepticism with regard to the contribution which new foreign banks might increase foreign investment because there had been two British banks whose investment contribution to the

[28] Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, p47.

[29] For the BAP's position, see "The Position of the Bankers Association of the Philippines on the Liberalisation of the Entry of Foreign Banks" submitted to the Senate Committee on 10 September 1993 and reprinted in PhilExport (1994); and Malaya, 29 November 1993, "All we Want is a level playing field" by Rafael B. Buenaventura.

economy had not been large.

Guided by the principle of the level playing field and effective Filipino control, the BAP proposed very restrictive provisions on the mode of entry, the size of capital requirement and the type of capital.[30] The BAP recommended the entry of new foreign banks by the establishment of branches only and wanted to limit the number of branches to three. In spite of the limited number of branches, the capital requirement of the new foreign banks would be equal to the level of the domestic commercial banks. The proposal also enforced strict ceilings on the transfer of capital from head offices (Net Due to Head Office accounts).

The BAP insisted that the large spread between lending and borrowing rates was caused by the high costs of intermediation. To defend its position, the BAP presented a research paper written by Jaime Laya, the former Central Bank governor. In the paper, Laya pointed out the three causes of high costs as follows: (1) high reserve requirements, 25% at that time; (2) Agri-Agra regulation which required that 10% of loanable funds be used for lending to agriculture and agrarian reform programme beneficiaries or used to purchase certain allowable government securities; and (3) 5% of Gross Receipt Tax (GRT).[31]

A fierce conflict came to light over this issue between the BAP and Citibank. The foreign bank claimed that the BAP's proposal was very restrictive. Citibank argued in its position paper that "in contrast to the BAP position, most of the countries that have liberalised ahead of the Philippines have taken a proactive 'market mode' posture in order to attract foreign banks into markets". There was a deep cleavage between their views. The BAP expressed concern over "misleading" information presented by the foreign bankers on the issue.[32] In a news conference, Buenaventura accused the foreign bankers of raising "false expectations that the liberalisation for foreign banks will achieve benefits to the Filipino public in general". The BAP also argued that its own

[30] See Table 6-1 "Proposals of the BAP".

[31] See Jaime C. Laya, Chairman, Laya Manabat Salgado & Co. "A Note on the Spread Between Borrowing and Lending Rates", in PhilExport (1994:14-16).

[32] See Malaya, 29 October 1993, "Rift widens between bankers".

proposals for the entry of new foreign banks were not restrictive by ASEAN standards.

Although the BAP could not push its position entirely on the Senate bill, its position, which stressed the importance of restrictive provisions on the entry of new foreign banks, appealed to the members of the Senate. Vocal support for the restrictive provisions came from some senators who emphasised the principle of Filipino control of the economy. Sen. Arturo M. Tolentino consistently opposed the bill and demanded restrictive provisions. He even argued that the bill violated the Constitution and expressed concerns about the "extinction of local banks" as a result of the entry of new foreign banks.[33] Sen. Wigberto Tañada, Minority Floor Leader, who had a reputation for his Pro-Filipino attitude, was also opposed to the entry of new foreign banks. He argued that the banking sector should be controlled by Filipinos and that the liberalisation measure would be unconstitutional. In addition, he thought that the Philippine banking sector could sufficiently and adequately respond to the growing needs of business, industry and agriculture.[34] Sen. Ernesto M. Maceda, a vocal critic of the Ramos administration and their economic policy was also strongly opposed to the bill. Sen. Nikki M.L. Coseteng, a former T.V. show hostess, also joined the opposition allies. These senators were much more sceptical about the entry of new foreign banks than the BAP, which agreed on the importance of foreign investment and capital for the Philippine economy.

Other senators also demanded that restrictive provisions should be included in the bill although they were not opposed to the entry of new foreign banks. The authors of the three bills, the core members of the caucus meeting, agreed that the Senate bill should provide more specific guidelines for the entry of new foreign banks. With respect to the mode of entry, Sen. Neptali A. Gonzales was in favour of the BAP's position. During a caucus meeting, he proposed an amendment which restricted mode of entry in line with

[33] See Sen. Arturo M. Tolentino's Press Release, 21 March 1994; Record of the Senate, 17 May 1994, Vol.V,No.80, pp.420-439, "Cof. Com. Rep. on S.1606/H.8226", Explanation of Vote of Sen. Tolentino, p.427.

[34] See, Record of the Senate, 17 May 1994, Vol.V,No.80, pp.420-439, "Cof.Com. Rep.on S.1606/H.8226", Explanation of Vote of Sen. Tañada, p.433.

the BAP's request.[35] Regarding the issue of the number of new foreign banks and the number of branches, the Committee decided on a limit of six banks (and two additional banks) and six branches. Higher capital requirements were also adopted. Various guidelines for the selection of the new foreign banks were specified by the bill. According to Sen. Roco, the stricter guidelines reflected scepticism among senators about the BSP's regulations.[36]

The Bicameral Conference Committee

When the Bicameral Conference Committee on the bill convened, there were large differences between the House and the Senate bills. While the Senate bill created a new law to regulate the entry of new foreign banks, the House bill aimed to amend the existing law, the General Banking Act, for the entry of new foreign banks. The key provisions differed in the following ways: (1) modes of entry, (2) number of foreign banks and number of branches opened by each bank, (3) guidelines for approval, (4) capitalisation, (5) capital ratios, and (6) equal treatment.[37] During the meetings of the Bicameral Committee, these differences occasionally intensified the sense of rivalry between the House and the Senate.

In April and May 1994, a series of formal and informal meetings, including the meetings of the four bicameral committees, was held to resolve the differences between the two bills. Central Bank officials, including governor Singson, often attended the meetings as technical advisors. The root of the differences between the House and the Senate bills stemmed from their basic stances: the House tended to stress the importance of flexibility in banking regulations while the Senate required stricter rules and guidelines for the entry of new foreign banks. There were fierce arguments

[35] See Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, p.22.

[36] See Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, pp.15-16.

[37] See Table 6-2 "The Comparison of S.B.1606, H.B.8226, BSP (Executive) Position and R.A. 7721.

between Rep. Teves, the main author of the House bill, and Sen. Roco, the Committee Chair of the Senate panel, over such issues as the mode of entry and the specific limitations on the number of banks and branches.

In general, the Bicameral Conference Committee tended to arrive at an intermediate compromise position between the House bill and the Senate bill. For example, the amount of permanently assigned capital agreed on was P210 million, a figure between that in the Senate bill (P300 million) and that in the House bill (P125 million). However, regarding the entry of new foreign banks, the Senate bill was more influential than the House bill in terms of the final outcome. The Senate panel was able to insert restrictive provisions regulating the mode of entry and the specific numbers of new foreign banks and branches. The Senate panel utilised their advantage. First of all, although the Central Bank demanded the deletion of some of the restrictive provisions of the Senate bill with the endorsement of the Executive, governor Singson did not openly express support for the House bill in the Bicameral Conference Committee. His role as technical advisor in the Committee could largely explain the "neutral" position of Singson as well as that of other Central Bank officials on the Committee. However, it must be noted that Senator Roco had a close relationship with the BSP since he played a critical role in establishing the New Central Bank, the Bangko Sentral ng Pilipinas (BSP) as the chairman of the Senate Committee on Banks. Second, the existence of resilient opposition in the Senate put unseen pressures on the House panel. There was vocal opposition to the entry of new foreign banks in the Senate. Because, unlike the House, the pro-Ramos coalition did not dominate the Senate (although Senate President Angara was supportive of Ramos's economic agenda), the support of the Senate for the liberalisation was not solid. Sen. Roco insisted that it was very difficult to reach a compromise on the provisions to be added to the Senate bill since some senators demanded more restrictive provisions.[38]

[38] See, for example, Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, pp.25-26.

The Committee adopted the Senate bill as a draft for discussion in the first meeting. The Senate bill, which was to create the new law, enjoyed some advantages in the Committee discussion. Since it included only provisions to regulate the new foreign banks, the issues could be much more easily clarified. The Senate panel was successful in gaining the support of the Central Bank on the form of the bill. Rep. Lacson, the Chair of the House panel, accepted the form of the Senate bill as the final outcome when governor Singson recommended it. Later, in the Committee, the chair of the House panel complained that "it would have been a big disadvantage on our part to start discussing this particular issue of the entry of foreign banks by using the Senate version as a draft".[39] The final bill included restrictive provisions which were not included in the House bill.

The most controversial issue was the mode of entry and statutory provisions on the number of new foreign banks and the number of branches opened by each bank. The House panel insisted that these regulations should be flexible enough to allow for adjustments to changing conditions, and that the authority to decide the numbers should be left to the Monetary Board. However, the Senate panel strenuously resisted pressure to change its position on this issue. To justify the Senate's position, Sen. Roco often referred to the Australian experience as an example of a failure resulting from an attempt to open up the banking sector without sufficiently restrictive guidelines.[40] After long debates, the House accepted that these numbers should be specified by law, while the Senate agreed that the maximum number of new foreign banks should be increased from eight to ten. The number of branches opened by each bank was limited to six. The three modes of entry were accepted, but each bank had to choose one of the three modes of entry. In addition, the final bill included the general policy of equal treatment, and specified a ceiling of ownership of foreign banks up to 30 per cent of the entire banking sector which was even more restrictive than the 40 per cent ceiling stipulated by the Senate bill.

[39] See Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 4 May 1994, p.71.

[40] See for example, Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, pp.33-34.

The Senate panel was able to persuade the House panel to accept the imposition of restrictive guidelines for the selection of the new entrants with some modification while the regulations on the Net Due to Head Office accounts (inwards remittances from the headquarters of foreign banks) was not restrictively specified by the law in accordance with the House position.[41]

Conclusion

The legislation regulating new foreign banks (R.A.7721) included some restrictive provisions which were not found in the liberal bill adopted by the House. Nevertheless, the entry of new foreign banks was a critical event for the banking sector which had been closed to new foreign entrants since 1949. The restrictive provisions on the mode of entry and the numbers of new foreign banks and branches were not so tight as to discourage the entry of foreign banks. Governor Singson commented that the number of foreign banks (eight) permitted by the Senate bill was not too restrictive. He suggested the Committee that it might be increased to ten.[42] The number of branches, which was limited to six, was also not an obstacle to new foreign entrants, since no potential applicants, except Citibank, were interested in opening more than four branches.[43] Although the law limited the number of foreign banks entering by establishing branches, the number of entrants through majority-owned subsidiaries was not specified, as the BAP had expressed concern about this mode of entry.[44] In fact, the entry of new foreign banks triggered competition in the sector. In the late 1990s, some big banks were merged in order to survive the new business environment which had

[41] See Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 11 May 1994, pp.10-11.

[42] See Committee Records: Senate Committee on Banks, Financial Institutions and Currencies, 6 January 1994, p.38.

[43] See Committee Records: Bicameral Conference Committee; Senate Committee on Banks, Financial Institutions & Currencies and House Committee on Banks and Financial Intermediaries, 21 April 1994, p.47.

[44] See, for example, Speech by Rafael B. Buenaventura at Financial Executives Institute of the Philippines (FINEX) 6th General Membership Meeting, "The Entry of Foreign Banks in the Country-Boon or Bane?".

been created by the various liberalisation measures.

The Ramos government further facilitated the economic liberalisation, initiated by the Aquino government. To encourage foreign investment and expand exports, the government implemented various liberalisation measures, including tariff reforms (trade liberalisation), telecommunications reform, foreign exchange liberalisation and the entry of new foreign banks. International influences played a critical role in liberalising the economy. Nevertheless, the entry of new foreign banks was not simply a passive reaction to pressures from outside the country. The case of the banking sector showed that the strong initiatives for liberalisation stemmed from the President, the centre of Philippine government.

Faced with an economic downturn in the early 1990s, the Ramos government was keen to reform the economy. Successful economic management was the key to mobilising support for the new President, who was elected with the smallest share of votes in Philippine history. Furthermore, the strong initiative to liberalise the banking sector emerged from the government on the back of a political ("anti-oligarchy") campaign which aimed to show the government's willingness to challenge the oligarchy's dominance of key industries. The constitutional strength of the Presidency and the President's tactical approach to the formation of a Pro-Ramos coalition in the Congress were important to the success of his legislative agenda. Most importantly, as was seen in the previous chapter, a new constellation of political institutions emerged as a consequence of the establishment of the 1987 Constitution which strengthened the interests and capacities of the President in advancing banking reform and weakened resistance among legislators. The six-year limit on the Presidency and the various initiatives taken by the new President facilitated the building of cooperative relationships between the President and legislative leaders, leading to structural reform.

The President's strong initiatives to reform the economy generated broad support. The entry of new foreign banks reflected rapid changes in the policy preferences of legislators, Philippine businesses, the media and the general public. Although there were pockets of resilient opposition to economic liberalisation, especially in the Senate,

liberalisation was no longer an economic strategy which easily generated hostile reactions throughout Philippine society. Liberalisation was previously a word which hinted at foreign dominance, massive layoffs and high prices due to the loss of subsidies. For example, under the Aquino government, the government's plan to liberalise the oil industry generated massive opposition, led to strikes of transportation workers and even spread rumours of another military coup. Dr. Paderanga, the former Director General of the NEDA, pointed out that there was a significant shift in policy preferences among legislators, businesses, the media and the general public.[45] As an economic strategy, liberalisation was accepted by many more people under the Ramos government than under the Aquino government.

In the domestic business community, there were many supporters of the liberalisation measures, which would create new business opportunities and foreign investment. Competition, facilitated by liberalisation measures, was expected to reduce prices and improve services. Businesses anticipated that the reform of the banking sector would reduce the costs of borrowing. In spite of the close ties between the banking sector and various industries, there was little support from other businesses for the BAP's position. Backed by businesses and the general public once a consensus had emerged among policy elites on the importance of the banking reform, the owners and managements of big banks who were supposedly the most powerful "oligarchy", were unable to stop the reform.

[45] Interview, Dr. Cayetano Paderanga, Jr. 10 June 1997.

Table 6-1. Proposals of the BAP

1. Mode of Entry of Foreign Banks

BAP proposes that foreign banks enter the Philippines as branches only:
(a) Branching will require less capital.
(b) Foreign banks themselves indicate they prefer to establish branches due to facility of operations.
(c) Monetary authorities may find it difficult to ensure effective control by nationals should foreign banks be allowed to gain control of Philippine banking corporations.
(d) There will be no need to amend the maximum legal ownership of foreigners in Philippine banks.

2. Size of Capital for Foreign Banks

Based on the principle of the level playing field, the capital requirements of banks are:
(i) P750 Million for a commercial bank license.
(ii) P1.5 Billion for a universal bank license.
Requiring that the size of capital be equal to that required for Philippine banks will assure:
(a) Equal and fair treatment for all classes of banks;
(b) The permanent presence and long term commitment of foreign banks; and
(c) Larger capital will make a foreign bank branch more competitive and more willing to COMMIT resources within the Philippine financial system.

3. Type of Capital

(a) Permanently assigned capital
(i) The maximum permitted ratios of Net Due to Head Office to permanently assigned capital are the following:
(1) 2 to 1 for a single branch:
(2) 1 to 1 for a maximum of 3 branches:
(3) For an expanded Commercial Bank, the required capital of P1.5 Billion would be through Permanently Assigned Capital of P750 Million and Net Due to Head Office of P750 Million.
(b) The maximum number of branches for a foreign bank fixed at three.
(c) The Monetary Board issues guidelines on the application and the use of the Net Due to Head Office, providing particularly that the amount is converted into local currency, invested and maintained in such local assets as the Monetary Board may direct.

Sources: "The Position of the Bankers Association of the Philippines on the Liberalisation of the Entry of Foreign Banks" submitted to the Senate Committee on 10 September 1993 and reprinted in PhilExport (1994).

Table 6-2. The Comparison of S.B.1606, H.B. 8226, BSP (Executive) Position and R.A. 7721

Modes of Entry

S.B. 1606 (Sec. 2)
With prior MB approval, a foreign bank may avail itself of ONLY one of the following modes of entry:
(1) establish a branch;
or (2) acquire up to 60% of voting stock in one existing bank;
or (3) invest up to 60% in one new banking subsidiary.

H.B. 8226
Subject to MB approval, foreign banks may:
(1) establish branches (Sec. 7, 9),
(2) establish wholly or majority-owned subsidiaries (Sec. 9),
(3) invest up to 70% of voting stock of an existing bank (Sec. 5, 9).

BSP (Executive)
With prior MB approval, a foreign bank may avail itself of the following modes of entry:
(1) establish a branch;
(2) acquire up to 60% of voting stock one existing bank;
(3) invest up to 60% of one new banking subsidiary.

R.A. 7721 (Sec. 2)
With prior MB approval, a foreign bank may avail of ONLY one of the following modes of entry:
(1) by acquiring, purchasing or owning up to 60% of the voting stock of an existing bank;
or (2) by investing in up to 60% of the voting stock of a new banking subsidiary incorporated under the laws of the Philippines;
or (3) by establishing branches with full banking authority.

Limits on Privilege, Number of New Foreign Banks and Number of Branches of a Bank

S.B.1606
Maximum of 6 or 8 foreign banks through entry by establishing branches (Sec. 6) and maximum of 6 branches of each bank (Sec. 2), (this limitation does not apply to the other modes of entry); and the privileges granted to foreign bank entrants shall expire five years from the effectivity of the Act

H.B. 8226
No limitation (subject to MB approval)

BSP (Executive)
The privileges granted to foreign bank entrants shall be re-examined by the Monetary Board after five years from the effectivity of the Act
R.A.7721
Maximum of 10 foreign banks (Sec. 6) and maximum of 6 branches (Sec. 4).
The privileges granted to foreign bank entering by establishing branches shall expire five years from the effectivity of the Act (Sec. 6)

Guidelines for Approval

S.B.1606 (Sec. 3)
Enforcing restrictive guidelines including, among others, reciprocity rights and inclusion among the top 100 foreign banks in the world or the top 3 banks in the country of origin
H.B. 8226
No restrictive guidelines
BSP (Executive)
Deletion of restrictive guidelines, particularly the requirement to be among the top 100 foreign banks in the world or the top 3 banks in their country of origin
R.A.7721
Enforcing restrictive guidelines including, among others, reciprocity rights, regional representation and among the top 150 foreign banks in the world or the top 5 banks in the country of origin

Capitalisation

S.B.1606 (Sec.4)
P300 million for 3 branches, P50 million for every additional branch
H.B. 8226
P125 million for 3 branches, P150 million for 4 branches, P175 million for 5 branches, P200 million for 6 branches, for 7 or more branches an amount equal to minimum capital requirement for domestic banks is required.
BSP (Executive)
Permanently assigned capital P200 million
R.A.7721 (Sec. 12)
For locally incorporated subsidiaries - equal to that required by MB of domestic banks, For branches - a permanently assigned capital of at least P210 million for 3 branches and an P35 million for every additional branch

Capital Ratios

S.B. 1606

For purposes of computing capital ratios of foreign bank branches, the Net Due To Head Office (NDTHO) account that is inwardly remitted and converted into pesos shall be added to assigned capital in the ratio prescribed by law or the MB.

H.B. 8226

The Net Due To Head Office together with the assigned capital at a maximum ratio of 5:1 will be used for calculating capital ratio.

R.A. 7721 (Sec. 4)

15% of NDTHO to be inwardly remitted and converted to Philippine currency, but exemption is provided for the amount invested in productive enterprises

Equal Treatment

S.B. 1606

Foreign banks enjoy the same privileges and be subject to the same limitations imposed upon a Philippine bank of the same category. These limits include the Single Borrowers Limit and Capital To Risk Asset Ratio under the General Banking Act and other related laws of the Philippines.

H.B. 8226

No provision

R.A. 7721

Foreign banks enjoy the same privileges and be subject to the same limitations imposed upon a Philippine bank of the same category. These limits include the Single Borrowers Limit and Capital To Risk Asset Ratio under the General Banking Act and other related laws of the Philippines.

Sources:

Summary Comparison of the Bills on Foreign Bank Entry Liberalisation, Prepared by the House Committee Staff, 19 April 1994; Differing Provisions Between Senate Bill No. 1606 and House Bill No. 8226, 25 April 1994, Prepared for Bicameral Conference Committee; and R.A. 7721.

BSP (Executive) Positions are from:

Letter from Teofisto T. Guingona, Jr., Executive Secretary, to Sen. Raul S. Roco, "the aide memoir from Bangko Sentral ng Pilipinas" 19 April 1994.

Chapter 7.
Conclusion

> "Weak banks are a worldwide phenomenon. They pose a continuing challenge for bank supervisors in all countries, irrespective of the political structure, financial system and level of economic and technical development. All bank supervisors have to be prepared to minimise their incidence and deal with them if they occur".[1]

In the beginning of the new century, the Bangko Sentral ng Pilipinas (BSP) has faced numerous challenges as a banking regulator. Under a more liberalised and globalised business environment, maintaining financial stability has become more difficult than before. There are also still large amounts of non-performing assets (NPA) in the banking sector. Banking frauds which lead to the insolvency of banks are repeatedly revealed. However, despite remaining weakness, the Philippine banking sector has experienced various developments and changes guided by policy reforms. The Philippines, which had been seen as "the Sick Man of Asia", was able to maintain relative stability in the economy and the banking sector despite the rapid depreciation of the currency in 1997. Faced with the "Asian economic crisis", unlike other ASEAN countries such as Malaysia, and in particular Thailand and Indonesia, the Philippines was able to avoid spending huge sums of public money to restructure the banking sector in the late 1990s. Although short term capital inflows to the economy increased in the mid-1990s, the relatively small amount of "hot money" was an important factor which allowed the Philippines to avoid the economic and banking crisis of the late 1990s. Nevertheless, there was also a broad consensus among economists and business analysts on the significance of banking sector reform as a cause of the relatively successful maintenance of economic and banking stability in the Philippines[2] along with relatively sound monetary, fiscal and foreign exchange policy.

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[1] Basle Committee on Banking Supervision (2002:3). Also, cited partly in *Business World, 13 August 2002*, Special Report: Second Quarter Banking Report.

[2] See, for example, Canlas (2000), Gochoco-Bautista (1999), Lim (1998), Sicat (1999), and Noland (2000).

In this context, this thesis has examined the politics of Philippine banking reform in the process of economic recovery from the economic crisis of the early 1980s. With respect to economic policy-making in the Philippines, the existing literature views the demands made either by foreign actors such as the US, the IMF and the World Bank or social forces (i.e. the oligarchy) as critical explanatory factors. In the existing literature on the Philippines' political economy, and in particular on the banking sector, there is a tendency to focus on the "weak" state, the "strong" society (oligarchy) and the strong continuity of these factors throughout Philippine history. However, this view limits our ability to understand the successes or failures of banking reform, the developments and changes in the banking structure, and the overall restoration of banking stability in the process of economic recovery between 1986 and 1995 since these views reduce Philippine politics to a relatively immediate expression of foreign or socially rooted demands.

As an alternative, this thesis argues that to understand the failures and successes of banking reform in the Philippines, the decisions of policy elites and institutions should be located at the centre of the analysis. In brief, the successful enactment and implementation of banking reform during the process of economic recovery was contingent on a new constellation of political institutions which emerged with the 1987 Constitution. This new constellation strengthened the interests and capacities of Presidents, the centre of the Philippine government, in advancing banking reform and weakening potential resistance among legislators and dominant social forces. This concluding chapter briefly recapitulates the arguments of this thesis on the politics of banking reform in the Philippines.

Banking Reforms and the Avoidance of the Banking Crisis of the 1990s

The Philippine banking sector has been seen as typical of a failed economy. Frauds, DOSRI loans, cartel-like behaviour and high financial intermediation costs have been viewed as obstacles to the developing economy. The defects of the banking sector were very clear during the economic crisis of the early 1980s. However, in the 1990s, a new puzzle emerged as the failed banking sector was rehabilitated and reformed to create a

banking sector which was more effective and stable in comparison with that in other ASEAN countries such as Malaysia, Thailand and Indonesia which, prior to the Asian foreign currency crisis, had been seen as the more successful economies.

In the process of recovery from the ruins of the economic and banking crisis of the early 1980s, banking sector reform was guided by two key principles: the facilitation of competition through liberalisation measures and the strengthening of the regulatory framework. Liberalisation does not guarantee an effective and stable banking sector. However, the ineffective structure of the Philippine banking sector, that had largely been occupied by state banks and was highly protected against new domestic and foreign entrants until 1986, was transformed by liberalisation. Along with Central Bank policies such as hikes of minimum capital requirements, liberal reforms facilitated the consolidation of the banking sector. The various structural and regulatory reforms implemented by the Aquino and, more fully, Ramos governments greatly contributed to the creation of a healthier banking sector, which was relatively resilient to the currency crisis of the late 1990s.

When the Aquino government took power through extraordinary means, the "EDSA revolution" in 1986, the banking sector was left in ruins. The huge foreign debt and non-performing assets of the banking sector, which was dominated by large state banks, clearly showed the failure of economic and banking reform under the Marcos government in the early 1980s. Soon after she took power, President Aquino initiated an important banking reform. She started to rehabilitate the state banks, namely the Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP), as a first step towards banking reform. The redirection of state activism in the banking sector and steady economic growth in the late 1980s revitalised the banking sector. In the early 1990s, the Central Bank initiated liberalisation in the banking sector to facilitate competition among banks while it maintained a cautious prudential regulation. The Central Bank also started to implement foreign exchange liberalisation. For many years, the commercial banking sector had been heavily protected by the restriction of new entries. Large and strong commercial banks had secured large profits. This highly protectionist policy started to change in the early 1990s. The Central Bank gradually

deregulated bank entry and branching. The policy shift toward liberalising the banking sector was further facilitated by the Ramos government. The banking sector, which had been closed to new foreign entrants since the Central Bank was established in 1949, was finally opened through legislation. The entry of new foreign banks further facilitated competition among banks.

Along with the new Central Bank policy, the more competitive business environment encouraged the consolidation of the banking sector. The structure of the banking sector, which had been dominated by state banks, was rapidly altered after the economic and banking crisis of the early 1980s. After the currency crisis of the late 1990s, the changes in the structure of the banking sector became even clearer. Due to mergers among commercial banks, the big private commercial banks became larger than state banks. During the economic recession, the profitability of the banking sector decreased, although the banking business is still profitable for solvent banks. The relatively low profitability and fierce competition among banks is a recent feature of the banking sector, which for a long time had been largely protected and highly profitable. In the newly competitive environment, the representatives and owners of banks are now forced to be more concerned about solvent lending activities and effective management, although banking frauds will never be wholly eradicated.

The 1993 Central Bank reform can also be seen as an important factor contributing to the relative monetary and banking stability of the late 1990s, although banking reform is an endless process which aims to foster a healthier financial sector in changing economic conditions. The establishment of the new Central Bank, Bangko Sentral ng Pilipinas (BSP) in 1993 was a significant reform which strengthened the regulatory power of the monetary authority. The huge losses of the old Central Bank, which pushed interest rates upward, were finally liquidated. Due to the Monetary Board reform and reduction of development finance, the new Central Bank became more able than before to isolate itself from political interests. Today, the Monetary Board is composed of seven members with a fixed term of six years each except for one representative of the government. The President also appoints the other six members of the Monetary Board including the Central Bank governor. However, once appointed,

the six members' tenure is protected by law. Due to the differences in the tenures of Presidents and Monetary Board members, a newly elected President cannot replace Board members, including the Central Bank governor. The strict restrictions placed on BSP's lending to the National Government have also been beneficial in maintaining monetary stability. The Central Bank also keeps the foreign currency accounts in surplus. Central Bank officials are provided better legal protection against legal action. Their salaries have been increased by the exemption of higher rank officials from the salary standardisation law for public servants.

It is also noteworthy that, since the experience of the banking crisis of the early 1980s, the Central Bank has adopted a more assertive attitude towards regulating the banking sector. The minimum capital requirement for banks has been steadily increased to improve the stability of the banking sector. The minimum capital requirement for expanded commercial banks (universal banks) has been steadily increased from 500 million pesos in 1986 to 4.5 billion pesos in 1999. To meet these increasing minimum capital requirements, diversification of ownership has been encouraged. Every commercial bank must also maintain a high capital adequacy ratio, defined by the Central Bank as the ratio of net worth (capital account) to risk assets. In 1992-1997, the capital adequacy ratio stayed within the range of 16.9 per cent to 20.2 per cent (Intal and Llant,1998:18, Table 5). This is twice as high as the Bank for International Settlements (BIS) requirement of 8 per cent.

In terms of monetary policy, the performance of the BSP still needs to be observed carefully. However, there are some positive signs which suggest that the BSP is maintaining monetary stability relatively well. Since the BSP was established, key monetary indicators, including inflation rates, interest rates and the level of base money, have fallen (see Lamberte,2002:23-26). The establishment of the BSP, which removed the huge losses of the old Central Bank and strengthened the regulatory power of the monetary authority, helped to foster better monetary conditions and a healthier banking sector before the currency crisis occurred. In addition, after the currency crisis the Central Bank took the necessary action to maintain monetary and banking stability, although the deceleration of the economy hurt the banking sector and the insolvency of

weak banks was unavoidable. After the currency turmoil, in order to strengthen the stability of the banking sector, the BSP implemented regulatory reforms. The BSP raised bank capital requirements, loan-loss provisions and liquidity cover for foreign exchange loans, and implemented stricter limits on loans to the real-estate sector. It also redefined past-due loans and enhanced information disclosure and accountability.[3] Importantly, despite the Presidential elections in the midst of rapid foreign currency depreciation, the Central Bank was able to keep the banking sector relatively stable and the election of a new President did not adversely affect monetary and banking policy. The relatively autonomous policy-making power of the Central Bank, which was secured by establishing the New Central Bank, was a precondition of maintaining relative banking stability.

The Policy Elites-Institutions Centred Approach

In the past two decades, the Philippine banking sector has experienced radical changes. In the early 1980s, the worst economic crisis led to the worst banking crisis in the country. However, key banking reform was not implemented by the authoritarian Marcos regime in decline, despite the emergency. President Aquino, who took power by extraordinary means, the "EDSA revolution" of 1986, initiated reforms in the banking sector, although she did not successfully implement structural reform through the legislative process. The Ramos government implemented critical structural reforms in the banking sector. The Ramos government became the first administration which was able to implement structural reform in the banking sector through the legislative process, namely the establishment of the new Central Bank, Bangko Sentral ng Pilipinas, and the entry of new foreign banks.

To understand the successes and failures of banking reform, this study has located policy elites and institutions at the centre of the analysis. The fact that the decisions of policy elites, including Presidents, legislators and state officials (Central Bank officials), centred on their career interests is critical to the attempt to explain the outcomes of banking reform. Demands from societal and international actors are influential in banking reform, but these demands are mediated through domestic political institutions

[3] See Canlas (2000:56-61), Paderanga (1998) and Gochoco-Bautista (1999:51-55).

and influence the decisions of policy elites. Changing political institutions crucially influence the decisions of policy elites and the interactions among them as they pursue their own career interests.

With respect to the Philippine state, arguments which stress the role of the "weakness" of the state vis-à-vis social forces (oligarchy) have been the dominant view in studies which seek to explain the continuing failure of policy reform and the economy. The problems in the banking sector have been seen as typical of a failed economy. For example, in his influential study, Hutchcroft (1998) argues that the banking sector can be seen as a typical example of "ineffectual state regulation" and "rampant favouritism" which is understood in the context of a "patrimonial state" and a "predatory oligarchy". He stresses the strong continuity of these structural problems in the Philippine banking sector, state and society through its post-war history to the middle of the 1990s. However, this view limits our ability to examine the politics of banking reform in the process of economic recovery. Contrary to Hutchcroft's stress on the continuing fundamental characteristics of the banking sector, since the banking crisis in the early 1980s there have been visible changes and developments in the banking sector in terms of its structure, the role of state banks, the level of competition, regulatory policy and overall stability, although economists agree that there are still many sources of financial inefficiency and instability. Banking sector recovery in the Philippines shows that even a "weak" state can be relatively successful in enhancing its regulatory authority in terms of monetary and banking management, and in implementing liberalisation measures, despite opposition from dominant social forces, namely domestic commercial bank owners in the 1990s.

From a comparative perspective, Hutchcroft (1998) classifies the Philippines as a case of "booty capitalism" which faces greater obstacles in terms of economic development than Indonesian and Thai capitalism ("bureaucratic capitalism"). However, arguments based on this broad typology critically limit our ability to understand the banking sector in the Philippines after the economic crisis of the early 1980s. In fact, the Philippines was able to avoid a banking crisis despite a rapid decline of the currency. During the currency crisis, the Philippine banking sector was more stable than its counterparts in

Indonesia and Thailand in the late 1990s.

Hutchcroft's analysis (1998), assumes that dominant social forces (or oligarchy) constitute a united social actor and he thus overestimates the influence of the oligarchy on policy decisions. This view is problematic in an examination of banking reform, in particular in a consideration of liberalisation in the banking sector. If the banking sector had been dominated by a united oligarchy, there would have been no liberalisation since the entry of new foreign and domestic banks would potentially have facilitated greater competition. In fact, there have been consistent conflicts among Philippine elites in and out of the state over key economic policy and banking reform as Hutchcroft recognises. Support (or opposition) from various social actors have been influential in the successes and failures of banking reform. In the case of banking reforms such as the rehabilitation of state banks, liberalisation measures and the entry of new foreign banks, the existence of beneficiaries are important in discouraging opposition and implementing reforms (see de Dios,1998:74). As noted earlier, when legislation was enacted to derestrict the entry of new foreign banks, local banks opposed this critical liberalisation measure, while other local businesses were supportive. In spite of the close links between local business and big banks, local businesses were in favour of banking liberalisation, since they expected that it would lead to lower interest rates.

Hutchcroft (1998) also views the Central Bank as a typical case of ineffectual state regulation and emphasises the strong continuity of the Bank's weakness throughout its history. However, this view is also problematic. In fact, the regulatory powers of the Central Bank and its autonomy vis-à-vis the government and regulated banks have improved since the banking crisis of the early 1980s. Few economists see a strong continuity in the role of the Central Bank and its regulatory powers under the Marcos, Aquino and Ramos governments. Under the Marcos dictatorship, the Central Bank, which played a critical role in development finance, was unable to maintain its autonomy vis-à-vis the President and political affairs. Faced with an economic and banking crisis, the role of the Central Bank as monetary authority and banking regulator was severely undermined by the President's interference in Central Bank decisions. After Aquino took power, the Central Bank, which was backed by the

President, started to implement regulatory reforms more smoothly. Unlike her predecessor, President Aquino did not intervene in the Central Bank's decisions regarding banking policy. Under the Ramos government, the regulatory powers of the Central Bank were strengthened by the enactment of the New Central Bank Act, a critical bank reform. The Central Bank secured more distance from the government as a result of the monetary board reform and the reduction of development finance. The Central Bank's huge deficits, which caused high inflational pressure were restructured. The Central Bank also enhanced its regulatory power by establishing the new Central Bank.

International financial structures, the policy preferences of the IMF, the World Bank, the US government and other donor countries have always been influential factors in Philippine economic and banking policy reform. The Aquino and in particular, Ramos governments have implemented liberalising reforms and have also reformed the central bank in order to improve its creditworthiness in international financial markets. Yet, the pressures from foreign actors cannot been seen as the single decisive factor in banking sector reform. From the early 1980s, liberal reform has been the main policy concern of the IMF, the World Bank and the US government. However, the Philippine experience shows that the adoption of liberal reform in the banking sector and other sectors has never been a simple process enforced by powerful foreign actors. Despite the strong trend towards financial liberalisation in the 1990s, the structure, regulatory framework and overall stability of the banking sector varied across countries.

The change of US security interests in the 1990s, has often been viewed as a major cause of liberalisation in the economy (see Hutchcroft,1998). Proponents of this view assume that after the end of the "Cold War" and the closure of US bases, the US government no longer saw any need to shield the Philippines from the demands of the IMF and the World Bank to open the economy. However, pressure from the IMF and the World Bank should not be seen as the decisive or sole factor in promoting reforms in the Philippine banking sector. Neither can one persuasively argue that US support of the new Aquino government due to security interests was a decisive factor in mitigating the pressure from the IMF and World Bank to reform the economy.

Especially after the Philippines declared a moratorium on foreign debt payments in 1983, the policy preferences of foreign creditors, including the US government, the IMF, the World Bank and other donor countries were influential in the making of economic policy. However, faced with an economic crisis, the Marcos government repeatedly delayed the implementation of the economic stabilisation measures recommended by the IMF due to considerations of domestic politics, namely the 1984 legislative election. In addition, a critical banking reform, namely the rehabilitation of the state banks, was not implemented, despite support from the IMF and the World Bank. During the Aquino period, a critical banking reform, the Central Bank reform, was not implemented, due to the deadlock between the President and the newly restored Legislature, although the World Bank provided strong financial incentives through conditionality lending. It should also be noted that although the Ramos government did not receive strong financial support through conditionality lending, the reform measure to open the banking sector to new foreign entrants was successfully implemented, despite strong opposition from big domestic commercial banks.

The relationship between US security concerns, its preferences in terms of economic policy and the policy stances of the IMF and the World Bank is also less than clear. Despite US support of the Marcos government, the IMF and the World Bank put strong pressure on Marcos to reform the economy including public spending, and to implement the coconut and sugar industry reforms. The shortage of foreign exchange due to the strict stance of the IMF and the World Bank decelerated the economy and fuelled opposition to the US backed President. In spite of its security concerns, the US also forcefully recommended an unpopular foreign debt policy to the Aquino government which fuelled opposition to the government. Foreign debt policy was the most controversial economic issue in the early years of the Aquino government.

A "policy elites and institutions-centred approach" essentially places policy elites, including Presidents, legislators and state officials at the centre of economic reform policy-making. The fact that the interests of policy elites centre on their career interests is crucial to their policy choices. The core of any President's career interests is the

desire to stay in power. If they can serve for consecutive terms, reelection becomes a high priority. If Presidents face a real threat of being overthrown, their first wish is to be able to complete their term. If they cannot serve consecutive terms, they will aim to maximise their political influence within their political parties or among their allies. Legislators are most concerned about reelection. The vote in the next election is always crucial for their career. State officials want first to secure their posts in office and then to win promotion.

It is important to note that the interests of policy elites are not identical with those of the oligarchy and international actors, including the US government, the IMF, the World Bank and other donor countries. Politicians, including the President and legislators, might chose to protect the interests of wealthy social forces (oligarchy or cronies) for electoral purposes. Yet, as the failure of the Marcos dictatorship showed, this is often not an optimal strategy for politicians. The high risks involved in such a strategy became clearer after democratic electoral contests were restored. For state officials, misconduct which maximises their material benefits in the short term can also potentially terminate their career. Serving foreign interests (or rumours about such activities) is surely damaging for policy elites and may end their careers. Thus, policy elites in the Philippine state authority can be seen as potentially autonomous from societal and foreign actors. They make policy decisions which serve neither the interests of dominant societal forces (oligarchy) nor those of powerful foreign actors when they serve their own interests.

Political institutions are influential in determining the decisions of policy elites and the interactions among them, which centre on their career interests. Political institutions can be defined as either formal (e.g. statute laws and regulations) or informal. The Constitution, which defines the power of the President, Legislature and State is at the centre of formal political institutions. It also determines the electoral rules for Presidents and legislators which are essential for their career interests. A particular form of formal political institution does not lead directly to the success or failure of banking reform. Informal institutions, which include customs, social norms and self-imposed codes of conduct, are also influential in shaping the policy decisions of policy

elites. Nevertheless, as Philippine experiences show, changing formal political institutions have had a significant impact on the decisions of policy elites, policy coordination among them and the level of the Central Bank's autonomy, all of which are influential in determining the success or failure of banking reform.

The policy elite and institutions-centred approach, which locates the decisions of policy elites and the interactions among them in the context of changing political institutions at the centre of the analysis can offer a systematic and coherent explanation for the failures and successes of banking reform in the Philippines. This thesis has argued that the successful enactment and implementation of banking reform in the process of economic recovery between 1986 and 1995 was contingent on a new constellation of political institutions which emerged with the establishment of the 1987 Constitution. This new constellation strengthened the interests and capacities of Philippine Presidents in advancing banking reforms and weakened potential resistance among legislators and social actors. The decisions of policy elites, the interaction among them in the context of changing Philippine political institutions and their influence on banking reform outcomes are briefly recapitulated below.

After independence, the Philippines adopted a democratic form of government under the 1935 Constitution, which was a Presidential system with a bicameral legislature until 1972. The regulatory framework of the banking sector was established by the Central Bank Act and General Banking Act in 1949. After a steady economic recovery supported by funds from the United States during the 1950s, economic growth decelerated at the beginning of the 1960s. Demands for economic reform to restore economic growth grew in the 1960s. In the late 1960s, faced with banking instability, the Central Bank first began to advocate structural reform in the banking sector to strengthen the regulatory framework under the first Marcos government (1965-1969). In the early 1970s, the massive behest loans of growing state banks were revealed, and the necessity of banking reform became evident under the second Marcos government (1969-1972). After President Marcos was reelected, he faced rising criticism and became more keenly supportive of the banking reform recommended by the Central Bank in response to public demands. Yet, the Marcos government failed to implement

structural reform in the banking sector. Between 1949 and 1972, under the 1935 Constitution, there was no key structural reform in the banking sector through the legislative process. This period of the economy and the financial system was also characterised by frequent monetary instability caused by massive election-related spending.

Under the 1935 Constitution, the President's interests and capacities in promoting banking reform were not strong enough to overcome opposition from legislators. Under the 1935 Constitution, the frequent legislative elections, in particular Presidential elections, every four years, which allowed reelection of the incumbent President, inevitably encouraged election-related spending and discouraged the Central Bank from tightening monetary policy. More importantly, the fierce rivalry between the President and legislative leaders, in particular the senators, which was often fuelled by tactical considerations for the next Presidential election, was a serious obstacle to reform of the banking sector through the legislative process. Legislative leaders who were seeking the next Presidency faced a serious dilemma: legislative actions that promoted economic and banking reform benefitted the incumbent President, who was their main rival.

Since the political party system, which disciplined the behaviour of legislators and provided the rules for electing leaders, was underdeveloped in the Philippines, there were few formal or informal institutions and organisations which helped to build a consensus between the President and the Legislature on important economic policy measures. It should also be noted that the Central Bank authority did not enjoy strong powers as a monetary authority. On the first Monetary Board before the 1972 reform, the decision-making body of the Central Bank was chaired by the Minister of Finance and the Central Bank governor was one of seven members on a par with representatives from two state banks, namely the Philippine National Bank (PNB) and the Development Bank of the Philippines (DBP).

In 1972, President Marcos declared martial law and closed the Legislature. This transformation of political institutions strengthened the interests and capacities of the President in promoting reforms in the banking sector. The concentration of power

overcame the problem of policy coordination in the early years of the dictatorship. Important structural reforms to enhance the regulatory power of the Central Bank were implemented by Presidential decrees soon after the declaration of martial law. The importance of banking reform was stressed by the government as an achievement of the martial law regime. However, the concentration of power provided fertile ground for Presidential cronyism under the dictatorship. The banking sector had experienced unprecedented levels of presidential cronyism and favouritism under the Marcos dictatorship. State banks expanded, as did behest loans. Marcos crony banks also expanded rapidly in the 1970s. Expansion of Presidential cronyism eroded the stability of the banking sector. As development finance by the Central Bank, which largely benefitted the dictator and his cronies was expanded, the role of the Central Bank as a monetary authority and banking regulator was severely undermined.

In the 1970s, the Philippine economy maintained a relatively high economic growth rate but this was largely fuelled by foreign and domestic borrowing. With changing international economic conditions, the Philippines had to face its most serious economic and banking crisis in the early 1980s. Faced with this crisis, the Presidential dictatorship in decline showed its inability to reform the economy and banking sector.

By the early 1980s, the problems of policy coordination between the President, Cabinet members and Central Bank officials and other close allies of the President were revealed as the dictatorship began to lose its grip on power. In 1978, the creation of the Ministry of the Human Settlement by the first lady, Imelda Marcos, triggered the loss of the government's control over government spending. In the early 1980s, under strict budget constraints, conflicts between Monetary Board members who were in favour of macro economic stabilisation measures and Imelda Marcos and close Marcos cronies, who opposed austerity measures, intensified. The restoration of legislative and local elections added to the complexity of governing the country, although the elections were not fair and the President dominated law-making. The implementation of economic stabilisation measures was repeatedly delayed due to the 1984 elections. Critical economic reforms, including reforms of the coconut, sugar and banking sector, were not implemented under the Marcos government, despite strong pressure from the IMF

and the World Bank. The sugar and coconut industries were dominated by powerful Marcos cronies, namely Roberto Benedicto and Eduardo Cojuangco respectively. Both of these men, who also owned big banks, occupied important positions in the ruling Marcos party, Kilusang Bagong Lipunan (KBL).

In the economic and banking crisis, the weakness of the Central Bank as a monetary authority and banking regulator was clearly revealed. The Central Bank, which played a critical role in development finance, allocation of foreign exchange and rescue of ailing companies, including banks, was vulnerable to the President's interventions. The majority of the Monetary Board members were representatives from the government (Cabinet members). Election related spending reemerged as a serious threat to monetary stability. Central Bank initiatives, which aimed to strengthen the banking sector and to restore public confidence by implementing tough measures against insolvent banks, were curbed by the direct intervention of the President. The insolvent state banks, which were at the centre of the Philippine banking sector, exemplified the failure of economic and banking reform under the Marcos dictatorship. Faced with growing opposition, President Marcos was most concerned about consolidating political support from his close allies, who opposed dismantling the coconut and sugar industries and banking reform due to their business interests. Marcos was more interested in the immediate goal of reelection in the snap Presidential election of 1986 than in implementing economic and banking reform to improve the economy in the long term. Under the dictatorship, there was no restoration of public confidence in the banking sector.

In 1986, when the newly elected President Aquino took power, the Philippines faced serious economic problems, including huge foreign debts. There was no short-term solution to the deep problems of the Philippine economy, such as low economic growth rates, large inequity of wealth and an ineffectual state apparatus. Nevertheless, the transition from Marcos to Aquino triggered a change in banking policy and policy-making. The banking sector started to recover as a consequence of policy reform under the Aquino government.

In terms of banking reform, the Aquino government had mixed results. Immediately after Aquino took power, the interests and capacities of the President in promoting reforms in the banking sector were strengthened by generating broad support from mass and foreign lenders, and by maintaining the President's domination of law-making power until the Legislature was restored. During this period, an important banking reform, the rehabilitation of state banks, was implemented. The rehabilitation of state banks, which were left insolvent with huge non-performing assets by the previous government, was the first step towards the restoration of the banking sector. It should also be noted that under the Aquino government, the Central Bank restored amicable relations with the President. Unlike President Marcos, President Aquino did not intervene in the decisions of the Central Bank regarding banking policy. With support from the President, the Central Bank implemented regulatory reforms in the banking sector more successfully than under the Marcos government in the early 1980s.

However, the fierce conflicts between the President and legislative leaders, in particular the senators, prevented the successful implementation of further structural reform through the legislative process. There were no effective formal or informal institutions and organisations which facilitated cooperation between the President and Legislature in enacting important economic measures under the newly restored legislative system. Due to a transitional provision of the 1987 Constitution, there were no legislative elections held between 1987 and 1992. Thus legislators did not need to cooperate with the President in order to be able ask for her support in an approaching election. President Aquino was not keen to create a formal body to facilitate policy coordination between the President and legislative leaders. She committed herself to a very strict stance of not intervening in the legislative process since such intervention might have hurt her popularity, which had been generated by opposing the dictatorship and respecting the "democratic" system. The importance of Central Bank reform was broadly recognised and the reform was endorsed by the World Bank. However, the Aquino government was not able to implement Central Bank reform.

The Aquino government had embarked on an economic strategy based on liberalisation and the enhancement of regulatory powers in order to expand exports and attract foreign investment in the early 1990s. The Ramos government further promoted this economic strategy. In terms of banking reform, the Ramos government became the first administration to implement key structural reforms in the banking sector through the legislative process. The establishment of the New Central Bank and the entry of new foreign banks can be seen as critical structural reforms in the banking sector.

Although the Ramos government inherited its economic strategy from the Aquino government, the transition from the Aquino to Ramos government was accompanied by important changes in political institutions, which influenced the decisions and interests of policy elites and the interactions among them. Under the new constellation of political institutions created as a result of the 1987 Constitution, the interests and capacities of the President in advancing banking reforms were enhanced.

The New political institutions created under the 1987 Constitution provided legislative leaders with strong incentives to cooperate with the President in reforming the economy and banking sector. The 1987 Constitution replaced the basic framework of the previous 1935 Constitution, including the Presidential system and the bicameral Legislature. Importantly, the Presidential term was now limited to only one term of six years. Under the 1987 Constitution, for legislative leaders who harboured ambitions for the next Presidential seat, the incumbent President was no longer a rival in the next elections. In addition, the results of the 1992 Presidential election, the first held under the new Constitution, suggest that popular support for "reform" and the endorsement of the incumbent President were very important for electoral success. Thus, for legislative leaders concerned about their prospects as candidates in the next Presidential election, there were strong incentives to cooperate with the President on his reform agenda, particularly, before the President decided which candidate to supporrt. The establishment of a cooperative relationship between the President and legislative leaders was a significant precondition for successful implementation of structural reforms in the banking sector.

Amicable relations between the President and legislative leaders were also encouraged by the Ramos leadership, as can be seen in measures such as the formation of the Legislative and Executive Development Advisory Council (LEDAC), which played a critical role in building a consensus on priority bills. Under the Ramos government, the LEDAC met once a week for many years and became the most effective body in the country's history in coordinating communications between the Executive and the Legislature on policy issues. The Ramos government also encouraged legislators to participate in forming an economic development plan. Furthermore, in 1993, a People's Summit on Social Pact for Empowered Economic Development (SPEED) was organised through cooperation between the President and legislative leaders to mobilise public support for the government's economic and social agenda. Cooperative efforts between the President and legislative leaders on priority bills reached a high point under the Ramos government.

In the Philippines, the lack of a responsible party system was seen as a serious obstacle to economic reform due to poor coordination between the President and legislative leaders. However, under the 1987 Constitution, the President was able to take the initiative in building cooperative relations with Legislature and the Ramos government was thus able to pursue its legislative agenda more successfully than previous Presidents.

Concluding Comments

In the last two decades, there has been little improvement in terms of international financial stability. Developing economies are severely constrained by the unstable international financial system. The Philippines has faced numerous challenges to its attempts to develop its economy and banking sector in this unstable international financial system. Political instability, corruption, cronyism and ineffectual state regulation are still serious matters which undermine economic development. The domination of economic wealth by a small number of elites (or new and old oligarchy) continues. Nevertheless, the economy and the banking sector have experienced notable changes. After the end of the Marcos dictatorship, the Philippine banking sector

recovered under the Aquino and Ramos governments from the ruins of the banking crisis of the early 1980s. The Philippines, which was the most vulnerable economy among Southeast Asian countries to the international economic shocks of the early 1980s, was relatively successful in avoiding the worst-case scenario of the economic and banking crisis caused by the rapid decline of the currency in the late 1990s. The successful enactment and implementation of banking reform in the Philippines, which contributed to the recovery and development of the banking sector, was contingent on a new constellation of political institutions emerging as a consequence of the 1987 Constitution. This new constellation strengthened the interests and capacities of Presidents in promoting banking reform and weakened resistance among legislators and the dominant social forces (or oligarchy).

After the currency crisis, the Philippine economy and banking sector showed mixed signs of disappointment and hope. Although the Philippine banking sector did not face a real threat of collapse in the financial system, the persistent weaknesses of the banking sector were revealed. Banking frauds, which led to the insolvency of banks, continued to emerge. The viability of the state banks' lending activities was still in doubt. President Estrada's misconduct revealed that even one of the top commercial banks was not entirely trustworthy in terms of its banking business. The recent collapse of the Urban Bank highlighted the difficulty of banking supervision in a liberalised environment which allows commercial banks to invest in their investment banking arms.[4]

However, it is also possible to see the positive effects of banking reform after the economic crisis of the early 1980s. The BSP has continued to regulate the banking sector without serious intervention from successive presidents. The BSP has also tried to become more accountable for its own actions. Since the BSP was established, it has maintained a good reputation among businesses as a monetary authority. Although the Estrada administration was not keen to use the LEDAC to facilitate cooperation

[4] For the case of the Urban Bank, see *Business World, 16 August 2000,* "Second Quarter Banking Report: Some hard lessons from the Urban Bank collapse (What Happened and Can it Happen Again?)".

between the President and legislative leaders on high priority bills,[5] the function of the LEDAC remained unchanged and the Legislature was able to amend the General Banking Act of 2000 under the Estrada government. The regulatory power of the BSP, the Central Bank, was enhanced and foreign participation was also encouraged by the legislation. Despite the serious political turmoil fuelled by financial scandals, the banking sector maintained relative stability.

This thesis has demonstrated that the positive effects of the emerging political institutions, which strengthened the interests and capacities of the Presidents in advancing banking reforms, were most clearly visible under the Ramos government. Yet, dark shadows were growing over the relative optimism of the mid 1990s. Above all, the unexpected fall of President Estrada showed the weakness of formal political institutions which enforce regular change in the Presidency. Due to this irregularity, his successor, Gloria Macapagal-Arroyo, who was promoted from the office of Vice President, was allowed to stand for the next election as an incumbent President. Faced with approaching Presidential elections, incumbent Presidents rarely reduce government spending to strengthen economic fundamentals. At the beginning of the 21st century, the Philippines is still in the early stages of developing the formal and informal political institutions necessary to facilitate reform initiatives through the legislative process and to encourage the Central Bank to further develop the banking sector according to its mandate.

[5] For the LEDAC under the Estrada, see, for example, *Business World, 4 November 1998* "Estrada to reconvene economic planning body", *Business World, 1 July 1999,* "Estrada administration tinsel gov't, Roco claims", and *Business World, 20 October 1999* "More coordination urged in lawmaking process".

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Committee Records and Minutes: House Committee on Government Reorganisation
Senate
The Senate Records
Committee Records: Senate Committee on Banks, Financial Institutions and Currencies

9th Congress, 1992-1995
House
Record of the House of Representatives
Committee Records and Minutes: A Joint Committee; Committee on Banks and Financial Institutions and Committee on Economic Affairs
Committee Records and Minutes: Committee on Banks and Financial Institutions
Senate
Senate Records
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Interview List

Name	Title	Date
Atty. Anthony Abad	Commissioner, Tariff Commission	17 June 1998
Prof. Gerardo Agulto, Jr.	Professor, CBA, UP	24 June 1997
Ms. Editha Alido and	Department of Economic Research, BSP	25 Nov. 1997
Mr. Fernando Y. Silvoza	Department of Economic Research, BSP	25 Nov.1997
Mr. Jose Almonte	Presidential Security Advisor, 1992-1998	2 June 1998
Dr. Carlos C. Bautista	Professor, CBA, UP	23 June 1997
Dr. Dante Canlas	Deputy Director General, NEDA (National Development Office) Professor, School of Economics, UP	4 Nov. 1997
Dr. Olivia C. Caoili	Professor, Political Science, UP (Vice President, Academic Affaires)	3 March 1997
Mr. Guillermo Carague	Monetary Board Member, BSP	25 Nov. 1997
Ms. Sheila Coronel	Executive Director, Philippine Center for Investigative Journalism	15 May 1998
Mr. Dennis David	Vice President, RBG Credit Support Service Division	13 August 1997
Dr. Amando Doronila	Editorial Consultant, Philippine Daily Inquirer	22 April 1997
Mrs. Nori Deus	Deputy Director of HRM and head of Group1 and 3, BSP	14 October 1997
Ms. Charito Elegir	Director IV, PMS	8 May 1997
Dr. Jesus Estanislao	Finance Secretary, 1989-1992	3 July 1998
Atty. Ramon Federizon	Committee Secretary of Banks & Financial Intermediaries	15 May 1997
Mr. Joseph Francia	Secretary General, Federation of Philippine Industry	19 May 1998
Mr. Masao Fujioka	President, Asian Development Bank, 1981-1989	9 July 1998
Mr. Antonio Gatmaitan	Former President of Commercial Bank of Manila	3 June 1998
Dr. Mario Lamberte	Vice President, Philippine Institute for Development Studies	23 June 1998

Name	Title	Date
Mr. Roel Landingin	Business Editor, Manila Times	26 May 1998
Dr. Joseph Lim	Professor, School of Economics, UP	14 March 1997
Prof. Victor S. Limlingan	Professor, Asian Institute of Management	30 June 1997
Mr. Guillermo Luz	Executive Director, Makati Business Club	21 July 1997
Prof. Solita Monsod	Director General, NEDA, 1986-1989	4 June 1998
	Professor, School of Economics, UP	
Mr. David Nellor	Residential Representative,	6 July 1998
	IMF Manila Office, 1995-1997	
Mr. Romulo Neri	Director General,	23 June 1997
	Congressional Planning and Budget Office	
Dr. Cayetano Paderanga, JR.	Monetary Board Member, BSP	10 June 1997
	Professor, School of Economics, UP	22 June 1998
Ms. Janna Sheng	Secretary,	22 June 1998
	House Committee on Economic Affaires	
with Ms. Daisy Mongado	Office of Cong. Teves	
Ms. Mercedes B. Suleik	DBP Vice President, Strategic Planning	29 Oct 1997
	Former Deputy Director, BSP	
Mr. John Syquia	Vice President,	21 July 1997
	Corporate Finance ING Barings	
Dr. Vicente Valdepenas, Jr.	Monetary Board Member, BSP	16 June 1998
	Director General, NEDA, 1983-1986	
Mr. Cesar Virata	Prime Minister, 1981-1986	19 June 1998