Financial Achievement of 1960

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Note & Comment

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One favorable occurrence of 1960 has been the steady replenishment of the country's reserve of foreign exchange. At the beginning of 1960 the reserve stood at slightly more than $160 millions. At present it is a little over $200 million—an increase of 25% in the country's dollar holdings in the course of the year. Such an event is without precedent in the post-war years. In fact, the foreign exchange reserve of the country was being depleted so rapidly that in December 1949 exchange controls were imposed to stanch the outflow of dollars.

It has required a decade to achieve a state of balance in the Philippines' external payments. The balance was arrived at in 1959; the substantial favorable balance of $40 millions was gained only in 1960. It must be noted that this favorable turn of events was not brought about by exchange controls alone. Rather, it is due to moves which have revalued the peso in terms of the dollar and other foreign currencies, giving the peso a more realistic international value. The first of these moves was made in July 1959, with the passage of the Margin Act. The result of the imposition of the 25% margin fee was to raise the buying price of the dollar to ₱2.50 for most uses. The next moves were made in April and in November of 1960, with the first stages of decontrol. These have made the dollar much more expensive in terms of pesos. Right now the dollar costs ₱3.60 for most uses. Also, those with dollars to sell get more pesos for them, though the selling rate is well below the buying rate.

The chronic imbalance of payments from 1945 to 1959 due to the peso's overvaluation has thus been somewhat righted by a partial, rather one-sided devaluation. Combined with fairly tight exchange controls, this has led to a replenishment of foreign exchange reserves.

The building up of a store of foreign exchange is not an end in itself, but a means to the health and orderly improvement of the economy. In the judgment of financial experts the reserve had fallen too low. An inadequate reserve will limit the country's financial maneuverability within and will expose it unduly to shocks from without. It is a good thing to have rebuilt the reserves to the level of $200 millions. Nonetheless, this cost the Philippines something in 1960: replenishing reserves slows down economic growth.

We can look at it in the this way: for years, prior to 1959, this country financed economic development in part by means of inflation. This kind of behavior shows up immediately in an outward drain of reserves. During inflation the country grows in part at the expense of its past savings accumulated in the reserve of foreign exchange earned in previous years and saved up. During the course of inflation reserves are used to support a higher level of investment — or perhaps even of consumption — than could have been financed out of current income and savings. Checking inflation will help stanch the outflow of reserves by imposing the condition that investment must be financed out of current savings, and consumption must be paid for out of current income. But merely checking inflation will not lead to an increase in the country's store of dollars.

1960's replenishment of the foreign exchange reserves has meant that the Philippines has been investing in foreign exchange. Instead of importing $40 millions worth of capital machinery, equipment and raw materials for the purpose of raising the output and expanding the productive plant of the country, the $40 millions was saved and added to the reserve.

Businessmen have been painfully aware of the slowdown of economic expansion. They noticed unhappily how scarce and tight loans were and how dear it had become to borrow money for business purposes. The banks made all the loans they could: they got lent up. Excess reserves disappeared and, with them, the bankers' capacity to make additional loans. The recent easing of credit restrictions on the part of the Central Bank is a sign that monetary policy is shifting away from investing further in foreign exchange. Yet it appears that monetary policy should be aimed at maintaining the reserve at its present level.

The marks of an adequate reserve are these. First, the reserves should be enough to allow the country in certain years to grow at a rate faster than the savings of that year permit, in order to speed up economic growth and to free it from utter dependence on year-to-year savings. Second, the reserves should permit the monetary authorities to regulate the supply of money for the internal good without having to be timorous about the external effects of their policy. For example, when the Federal Reserve lowered its interest rate recently for the purpose of encouraging monetary expansion within the United States, gold flowed out of the country in the form of short-term liquid capital seeking higher rates of interest abroad. The reserve should be ample enough to tolerate this kind of reaction. Third, whether the external payments of a raw-materials-exporting country like the Philippines will balance in any given year depends in part on the prices received for exports compared with the prices paid for imports. This country should be able to afford a temporary unfavorable balance, when the terms of trade turn against it. A reserve much below $200 millions will limit this freedom of movement. On the other hand, it is good for a country to have to watch its reserve vigilantly; it forces the monetary and fiscal authorities to behave themselves economically, and it compels businessmen to produce efficiently and competitively.

Inflation has recently gone out of fashion in the world's leading economies. There is now a New Environment, as it is called: the big countries have achieved a measure of price stability not known for the past 20 years. These countries are learning to live without inflation. Their policy makers are striving to hold back the increase in the supply of money to a rate matched by the increase in the supply of goods and services. This will keep new money from forcing prices upward. So far as economic growth goes, the New Environment means that development has to be financed by means of true savings, and not in part by means of inflation. The Philippines must grow economically. This country is in urgent need of economic improvement. Mr. Per Jacobsson, Managing Director of the International Monetary Fund, made this report in July 1960:

> Of the aggregate national income of all the countries that are members of the International Monetary Fund, the share of the industrialized countries—the United States, Western Europe and Japan—is about 75%, while their share of the total population is only 25%. Thus, the share of the national income of the primary producing countries is 25%, and their share of population is about 75%.

One fourth of the people get three-fourths of the income, while three fourths of the people get one fourth of the income. On the average, rich countries are nine times richer than the poorer ones. Now, the Philippines is in the poorer group. There is urgent need here for economic advance.

Yet, if we are to learn to live without inflation, whence will come the funds to finance growth? From current savings. But the truth is hard. In recent years our own savings, even when abetted by doses of foreign aid from the United States, have just about sufficed to keep the economy's growth in pace with the growth of population. The statistician can find no persuasive evidence that per capita incomes have been rising in the last couple of years. Neither can that casual observer of the public's state of well being, the man on the street.

What of the savings of foreigners which might be tapped in the form of investment from abroad? It is instructive to look at the record of Germany's foreign investment, because the Germans have given evidence of their willingness to invest here. Between 1952 and mid-1960, West Germany had invested 2.45 billion Deutsche Mark abroad — roughly, $600 millions. One third of this was invested in Europe, in lands which are not capital-poor in the sense in which the Philippines is capital-poor; one fourth was invested in Canada and the United States; one fourth found its way into Latin America. This leaves only one-sixth for the underdeveloped countries of Africa and Asia. Evidently, Germans find it easy and attractive to invest in Europe and America, but not so easy or attractive to invest in countries like the Philippines.

One of the costs of economic nationalism — of coolness toward foreign ownership and management—is a retardation of economic growth. Perhaps this is a cost which the Filipino people are fully willing to shoulder; only it should be borne knowingly and willingly. This particular consequence of economic nationalism is not something to be fobbed off on an unwitting and unwilling public.

However, if the country neither wants nor can get much direct foreign investment, what about *getting international loans for development?* The Philippines has been quite successful in obtaining development loans. At the start of the year 1960, the country's external debt stood above $300 millions. But there is a limit to the amount of expansion a country can afford to finance by means of loans. The servicing of a debt of $300 millions drains $45 millions a year out of the country. At present the Philippines can well afford that much — about 9% of its 1959 export earnings, but it certainly cannot afford to double the amount of its foreign loans.

There is an opinion commonly held in this country that development loans are preferable to direct foreign investment. The opinion is not wholly sound. It rests on two reasons. First, foreign loans do not bring foreign ownership and management into the business of the country. This is true, but not an unmixed advantage. This country needs not only to grow but also to diversify its capacity to produce. Foreign management is often the only means of learning how to do new things. Second, the interest rate on loans, being lower than the rate of profit on foreign investment, does not so heavily tax the country's foreign exchange payments. This is an illusion.

Foreign direct investment, once it comes into the country, typically remains here. Think of Philippine Manufacturing Company. Unlike the principal of a loan, this investment does not have to be repaid. Second, the profits of successful enterprises are ploughed back into the expansion of the business and of the national economy.

Only a fraction of profit is repatriated in the form of foreign exchange. This is so true that it is a touchy matter with the Communist Party of the Philippines. The Party has accused the economic imperialists of increasing their ownership of the Philippines not by bringing in fresh doses of dollars but by growing on the profits sweated out of the Filipino people. It indicts foreign investors precisely for not taking their profits out of the country.

My point is this: there is hardly a limit to the amount of foreign investment this country might accommodate. There is a definite limit to the amount it can afford to borrow.

The national mood at the start of 1961 need not be one of melancholy. The budget has been balanced and foreign payments have been set right. The New Environment invites the nation to live without inflation and thus harden the peso, while it is hoped that gradual decontrol will compel businessmen to live without banning imports. Both consumers and producers will find the atmosphere of competition and sound money more stimulating than that of overprotection and slowly eroded purchasing power.

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The Suspension of Congressman Osmeña

On 23 June 1960, Sergio Osmeña, Jr., Congressman from the 2nd District of Cebu and arch-critic of President Carlos P. Garcia, delivered the fifth of his philippics against the Chief Executive. In the course of his hour-long privilege speech, Congressman Osmeña made the following accusation:

> It is said, Mr. President, that you vetoed the measure nationalizing rice and corn because of a previous commitment you had given to President Chiang Kai-shek at Taipeh. But ugly tongues are continually wagging that you had ten million reasons for vetoing the measure each reason of which cost ₱1.00. Is it true, Mr. President, that the money was delivered to a former member of your Cabinet and that it took at least two days to count the same?

On motion of Congressman Zosa, the reference to the ten-million peso bribe was deleted from the records as being unparliamentary. After the customary interpellations, the House proceeded to take up other business.

Fifteen days later, on 8 July 1960, the House of Representatives passed Resolution No. 59 creating a fifteen-man special committee "to investigate the truth of the charges against the President of the Philippines made by Honorable Sergio Osmeña, Jr." The special commit-